Sunderland Marine Mutual Insurance Company Limited

Registered Number: 16432

Annual Report and Financial Statements

Year Ended 31st December 2013

CONTENTS

Sunderland Marine Mutual Insurance Company Limited
Company Information
Year Ended 31st December 2013

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 strategic report for the year ended 31st December 2013.

Status

The company is limited by guarantee without share capital.

The company was a mutual company until the completion of the merger with The North of England Protecting and Indemnity Association Limited on 28th February 2014, when it was demutualized.

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 policyholders 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 insurance and 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 to this strategy. Stability of financial strength to withstand market conditions and unforeseen events, and continuity of cover, 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 (15.0%), North America (44 5%), Europe (11.4%), Australasia (18.0%), and others (11.1%), and for aquaculture they are UK (15.2%), North America (49.5%), Australasia (11.9%) and South America (23.4%).

Business environment

Despite the pervading competitive environment, with capacity for marine insurance showing only minimal signs of reduction, the company achieved high levels of retention.

Over the course of the year Sterling strengthened against the Australian, Canadian, New Zealand, United States and South African currencies. 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 largely 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 policyholders and counterparties. These KPIs comprise:-

- Written premium
- Combined ratio (net claims costs plus net operating expenses less other operating income and goodwill 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 less other operating income and goodwill 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 £92,453,000 has decreased by 3.0% from £95,325,000 in 2012. Taking out the currency effect the decrease, in real terms, was 3.3%.

Operating performance has improved from last year although trading conditions remain difficult with a technical underwriting deficit of £715,000 (2012: £3,032,000). Positive investment return in the non-technical account of £1,087,000 (2012: £2,499,000) produced a surplus before tax of £372,000 (2012: deficit of £533,000). Net of tax the deficit was £168,000 (2012: £1,326,000).

The expense ratio has decreased to 27.5% (2012: 31.3%) due mainly to increased reinsurance commission receivable partly offset by reduced premium net of reinsurance. The loss ratio has decreased to 70.4% (2012· 72.4%) as net claims have fallen although the improvement is partly offset by reduced premium net of reinsurance. The combined ratio has reduced to 97.9% (2012: 103.7%).

Marine

The marine division accounted for 82.2% of written premiums in 2013 (2012: 78.5%).

The business is written worldwide. Protection and Indemnity business is focussed on the USA, Europe and Australia and Personal Accident has a UK and Australian bias.

Gross written premium for marine business in 2013 increased by 1 5% due to a combination of increases on existing business and new business attaching during the year. A significant proportion of the new business was non-fishing accounts including tugs, barges and short sea cargo vessels.

The results from marine underwriting showed continued improvement in performance following the progress made in 2012. Claims patterns remained stable for both hull and liability covers.

A significant turnaround in the last two years, in what remains an extremely competitive environment, has been accomplished through hull and liability rate increases together with a policy of higher deductibles and some restructuring of conditions to limit the company's exposures. The loyalty of the company's policyholders remains strong with retention levels of over 90% by policy number.

Aquaculture

The aquaculture division accounted for 17.8% of gross written premium in 2013 (2012: 21.5%).

Written premiums decreased by 19.6%. The reduction in premium was mainly due to significantly lower levels of penalty premiums being charged because of improved loss experience in the year. Premium growth has also been curtailed by the loss of some income from the tuna industry. A final production value lower than forecast for one major account also negatively affected total earned premium These factors were mitigated by continued premium rate increases and new business attachments during 2013 which are anticipated to continue into 2014.

Investment return

The company's investment portfolio has changed slightly over the course of the year. The company is in the process of divesting itself of its holding in AIS Ltd, a listed investment trust which is a hedge fund investment. The proceeds of the sale will be reinvested in multi asset investments.

Asset allocation remains heavily weighted toward bond investment, with the Board retaining its cautious approach to investment strategy, with an emphasis on capital preservation and stable income generation The portfolio has generated a return of £1,087,000 (2012:£2,499,000). This is slightly below expectation and is reflective of lower assets under management and a rise in bond yields in the second half of the year. As portfolio duration is relatively short overall, the impact on portfolio performance of the latter was limited.

Investment risk is monitored closely and remains comfortably within the budget set by the board The risk budget is likely to remain at current low levels during 2014. Given the current level of assets under management and the relatively high bond weighting in the investment portfolio, attendant returns are likely to continue to be relatively low by historic standards.

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 regulators are the UK's Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) under whose auspices the capital regime for regulated insurance businesses continues to evolve. They replaced the former regulator, the Financial Services Authority, with effect from 1st April 2013.

The company has developed a framework using the PRA'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 PRA requirements, and to the published solvency margin.

The solvency margin has strengthened this year from 86.8% in 2012 to 94 9% in 2013. The reduction in reserves in the year has been offset by lower earned premium net of reinsurance.

The total capital and reserves of the group are £34,699,000 compared with £35,278,000 at 31st December 2012. The reserve fund of the company is £26,007,000 (2012· £26,007,000) and the surplus retained in the income and expenditure account of the group is £8,327,000 (2012 £9,069,000).

The company is working towards Solvency II and has developed a framework for review and development of its governance, risk management and capital systems to aim to achieve compliance by the implementation date.

Mutuality and policy years

The company was a mutual company until the completion of the merger with The North of England Protecting and Indemnity Association Limited on 28th February 2014, when it was demutualized. The company will continue on this basis for the foreseeable future. The directors have formally closed policy years 2011 to 2014. All policy years are now closed.

Cash flow

Operations utilised £2,338,000 of cash (2012: utilised £6,317,000), principally resulting from the continuing effects of changes to the reinsurance programme made in 2012.

Portfolio investments decreased by £3,628,000 (2012: decrease £8,918,000). Deposit and short-term cash holdings were increased by £1,080,000 (2012. increase £1,534,000).

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 10 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 costs and administration expenses exceed the amount of premium income earned.

Market risk

Market risk is the potential adverse financial impact of changes to foreign exchange rates, 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 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 risk

Group risk is the potential for one or more 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.

By order of the board

A.S. Rowland
Secretary
25th March 2014

The directors present their report and financial statements for the year ended 31st December 2013.

Directors

The table below shows the composition of the board and its committees at 31st December 2013.

A legend is shown in support of the table.

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

Director	Board	Audit	Defence Advisory	Executive	Investment	Nomination	Remuneration	Risk	Security
A J Alden (executive director)	*		*					*	
J D. Alford	*				c				
A D.W. Allan (Vice Chairman)	*	*	*	*	*	c	*	*	*
J P Crichton	*		*					*	
W.J.J. Crowe	*	*							
T.F. Hart (Chairman)	c	*	c	*	*	*	c	c	c
C.J Hilton	*		*					*	
P M. Johnson •	*	c		*	*		*		
F J Mattera	*								
G.C. Parkinson (executive director)	*		*	c	*	*		*	*
T. Rutter (executive director)	*								
P.I. Talley	*								
S. W. Taylor	*	*							
A C Vipond (executive director)	*		*					*	

- Mr Johnson was appointed as a member of the Remuneration Committee on 25th June 2013.

Retirements/appointments in 2014

The merger with The North of England Protecting and Indemnity Association Limited was approved by the membership of the company at an Extraordinary General Meeting on 28th January 2014. In accordance with the Framework Agreement the following directors retired from the Board on 28th February 2014:

A J Alden
J D Alford
A D W Allan
J P Crichton
W J J Crowe
C J Hilton
T Rutter
P I Talley
S W Taylor
A C Vipond

It is intended that the following directors will be appointed to the Board following PRA approval of their application to carry out a controlled function with the company:

L B Christensen
J M de Groot
P A Jennings
P B Shirke
A A Wilson

Directors' biographical details

Trevor F. Hart (69) 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. He is also a company nominated director of the corporate trustee of the company's pension scheme. He was previously a marine underwriter with a Lloyds' syndicate and is based in England.

Lars B Christensen (50) Vice-Chairman

Mr Christensen is the vice-chairman of The North of England Protecting and Indemnity Association Ltd He is also the executive vice-president of D/S Norden A/S. He is based in Denmark.

Job M de Groot (53)

Mr de Groot is a non-executive director of The North of England Protecting and Indemnity Association Ltd He is a qualified lawyer and manager of the legal department for Van Oord NV. He is based in the Netherlands.

Paul A Jennings (51)

Mr Jennings is the Joint Managing Director of The North of England Protecting and Indemnity Association Ltd He is based in England.

Peter M. Johnson (65)

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 was a director of Bellway plc, retiring on 31st January 2014. He is a Trustee of the Scholefield Charitable Trust and a fellow of the Institute of Chartered Accountants in England and Wales. He is based in England.

Frederick J. Mattera (62)

Mr Mattera was appointed as a non-executive director in 1998. He is a retired commercial fisherman and president of the Point Club. He is actively involved in marine safety training as head of NESTCo He is based in the USA.

Geoffrey C. Parkinson (58)

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. He is the chief executive officer of the company and is based in England.

Pratap B Shirke (65)

Mr Shirke is the chairman of The North of England Protecting and Indemnity Association Ltd and director of ASP Ship Management Company. He is based in England.

Alan A Wilson (58)

Mr Wilson is the Joint Managing Director of The North of England Protecting and Indemnity Association Ltd. He is based in England.

Directors' interests

Other than those executive directors who have contracts of employment with 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 contributions

No political contributions were made (2012: £nil)

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 financial statements.

Disclosure of information to the auditor

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 auditor is 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 auditor is aware of that information.

Auditor

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

By order of the board

A.S. Rowland
Secretary
25th March 2014

Company registration number: 16432

The UK Corporate Governance Code

The company does not seek to comply with the UK Corporate Governance Code, as issued by the Financial Reporting Council. The company aims to adhere to the principles and provisions of the UK Corporate Governance Code annotated by the Association of Financial Mutuals ('the Code').

The board considers that, except where stated, throughout the year ended 31st December 2013, the company has applied the relevant principles.

Leadership

The role of the board

The board meets four times a year, or more frequently as required, 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.

The board's principal role is to focus on:

- strategic aims and objectives, and monitoring 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.

To assist directors in complying with their statutory and other responsibilities under the Companies Act 2006 and all other applicable statutes and regulations the Board has adopted a procedure manual which is reviewed and approved annually.

Division of responsibilities

Beneath the board there is in place clear and appropriate apportionment of responsibilities amongst the executive directors and senior managers. There is also clear segregation of the roles of chairman and chief executive as evidenced by separate job descriptions contained within the board procedure manual.

The chairman

The chairman is responsible for the leadership of the board and ensures the board's effectiveness on all aspects of its role, as detailed above, within a framework of prudent and effective controls which enables risk to be assessed and managed

The Chairman sets the board's agenda and ensures that adequate time is available for discussion of all agenda items, in particular strategic issues. He ensures that the directors receive accurate, timely and clear information He also promotes a culture of openness and debate by facilitating the effective contribution of non-executive directors, in particular, and ensuring constructive relations between the executive and non-executive directors.

Board effectiveness

Composition and balance

The board at 31st December 2013 comprised the non-executive chairman, nine non-executive directors and four executive directors. From 28th February 2014 the board comprised the non-executive chairman, two non-executive directors and one executive director. It is intended that, following PRA approval of the appointment of Messrs Christensen, de Groot, Jennings, Shirke and Wilson the board will comprise the non-executive chairman, five non-executive directors and three 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 independent director. All the non-executive directors are judged to be 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

During 2013 the nomination committee reviewed the structure, size and composition of the board and the board committees. When carrying out its review the committee focused on the board's optimal balance and composition. All appointments are made on merit and take into account geographic and gender diversity, together with key areas of experience such as industry-specific, insurance, legal, risk and accounting.

Biographies of all the current directors appear on page 8. Membership of the board committees during 2013 is set out on page 7. The board is satisfied that the balance and range of expertise, experience and qualifications is appropriate for the current needs of the business

Development

The chairman ensures that, on appointment, non-executive directors receive a tailored induction programme. 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. Individual training requirements for the directors are identified through the evaluation process.

Board committees

During 2013 the board had established audit, defence advisory, executive, investment, nomination, remuneration, risk and security committees. Following the merger all committees were disbanded except the audit and risk committees. In addition a further committee, the policyholder committee, was established.

Audit committee

The members of the audit committee until 28th February 2014 are shown on page 7. It is intended that J.M. de Groot, P.M. Johnson and P.B. Shirke will be the members of the committee.

The committee meets at least twice a year, or more frequently if required, and its key 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 reports from the compliance function and internal audit;
- making recommendations to the board for it to put to the member for its approval in general meeting in relation to the appointment of the external auditor and their remuneration;
- approving non-audit work provided by the external auditor 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 and monitoring the effectiveness of the anti-bribery policy.

The external auditor, the executive directors, the group's senior financial and compliance management and the internal auditor attend meetings of the committee as required.

The committee discharges its responsibilities through its consideration of the preceding points and in addition:

- the committee reviews and approves the scope, approach and timeline of the external audit and internal audit; and
- reviews the external auditor's management letters and management's response to them.

These provide sufficient assessment of the independence and effectiveness of the external auditor and the audit process.

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 auditor without the executive directors or representatives of senior management present.

Risk committee

The members of the risk committee until 28th February 2014 are shown on page 7. The current members of the committee are P.M. Johnson and T.F. Hart. It is intended that L.B. Christensen will be appointed to the committee. The committee meets at least twice 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.

Policyholder committee

The policyholder committee was established following the merger for the principal purpose of providing a means of engaging with the company's policyholders The members of the committee are F.J. Mattera (chairman), W.J.J. Crowe, S.W. Taylor and P.I. Talley. The committee will meet at least twice a year. Its responsibilities include:

- Keeping the company's board informed of issues and changes within the markets in which the company operates;
- When requested by the parent's nominations committee, provide recommendations to that committee in relation to non-executive director appointments to the company's board, the

appointment of the chairman of the board, and the appointment of any successor to the company's chief executive officer; and
- To ensure adequate and appropriate communication with policyholders.

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

The following committees existed during 2013 but were disbanded on 28th February 2014.

Defence advisory committee

The members of the defence advisory committee during 2013 and until the committee was disbanded are shown on page 7. The committee met only as required. It advised the board on the group's defensive strategy. The committee was disbanded on 28th February 2014.

Executive committee

The members of the executive committee during 2013 and until the committee was disbanded are shown on page 7. Meetings were held as circumstances required. The duties of the committee were 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 considered other matters relating to the group upon which senior management may have needed guidance with a view to making recommendations to the board. The committee was disbanded on 28th February 2014.

Investment committee

The members of the investment committee during 2013 and until the committee was disbanded are shown on page 7. The committee met four times a year, or more frequently if required, and its principle objective was to ensure that the company's investment strategy reflects objectives approved by the company. Its responsibilities included recommending investment guidelines for the management of liquid assets of the company through asset allocation benchmarks, performance objectives and performance benchmarks for the group's funds and monitoring the investment performance. The committee was disbanded on 28th February 2014.

Nomination committee

The members of the nomination committee during 2013 and until the committee was disbanded are shown on page 7. The committee met at least once a year, or more frequently if required, and the overriding objectives of the committee were to establish a formal, rigorous and transparent procedure for the appointment of new directors to the board and to approve appointments to senior management positions. Its responsibilities included:

- reviewing the structure, size and composition (including the skills, knowledge, experience and diversity including gender) 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.

Due to the niche nature of the sectors which dominate the company's business, the nomination committee and the board, following due consideration, did not utilise external search consultancies or advertising in the appointment of chairmen or non-executive directors. The committee was disbanded on 28th February 2014.

Remuneration committee

The members of the remuneration committee during 2013 and until the committee was disbanded are shown on page 7. All the committee members were non-executive directors. The committee met at least once a year, or more frequently if required, and its principle objectives were to ensure and determine for board approval that:

- There was a formal process of considering, in a fair and thorough manner, the remuneration of.-
  - the company's directors; and
  - persons appointed as advisors to any of its committees.
- The company adopted a coherent approach to remuneration in respect of all employees; and
- There was oversight of the company's remuneration policy and outcomes in respect of all senior employees.

In addition, the committee would consider, in a fair and thorough manner, the structure and implementation of any bonus plan which may have been introduced for staff. The committee was disbanded on 28th February 2014.

Security committee

The members of the security committee during 2013 and until the committee was disbanded are shown on page 7. The committee used to meet at least once a year or more frequently if required. It evaluated 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. The committee was disbanded on 28th February 2014.

Company secretary

Under the Companies Act 2006 there is no longer the requirement for there to be a "company secretary" of a limited company. This is reflected in the company's articles of association which have taken the form of the model articles. However, the company has decided that the position should be retained. In accordance with the company's articles there is no longer the stipulation that the appointment and removal is a matter for the board as a whole, as recommended by the Code, although their recommendation is taken into account in this regard.

Meetings and attendance

Forum	**Number of members**	**Attendance at Meeting**							
		Jan	**Mar**	**April**	**Jun**	**Sep**	**Oct**	**Nov**	**Dec**
Board	14	13	14	13	14	14	12	-	14
Audit	5	-	5	-	-	-	-	5	-
Investment	5	-	5	-	5	5	-	-	5
Nomination	3	-	-	-	-	-	-	-	3
Remuneration	2 (3 after 25 06 13)	-	2	-	2	-	-	-	-
Risk	7	-	7	-	-	-	-	-	4
Security	3	3	-	-	-	-	-	-	-

"-" denotes no meeting.

The defence advisory and executive committees meet as required. No meetings of these committees were held during 2013.

Performance evaluation

The board has established a formal annual evaluation of its own performance, and that of its committees, individual directors and the chairman. 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. The review of responses relating to the chairman is the responsibility of the vice chairman.

The Code suggests that evaluation of the board should be externally facilitated at least every three years. This was first introduced by the Code in 2010 and thus compliance was suggested by 2013. However, following the merger, the board will consider the appropriateness and value of such an exercise during the course of 2014.

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.

Accountability

The board as a whole is accountable for the performance of the company. The annual report and financial statements provides a comprehensive review of the group's financial and operational performance in 2013

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 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 is satisfied with the effectiveness of the group's system of internal control following a review of these controls. 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.

Risk management

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. The committee meets as required.

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.

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

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, 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.

Relations with policyholders

The company's website at www.sunderlandmarine.com contains up to date information on the group. The company produces a regular newsletter which is available on the company's website. The company pursues a policy of personal contact and wide dialogue with policyholders Policyholders 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@sunderlandmarine.com.

By order of the board

A.S. Rowland
Secretary
25th March 2014

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.

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 all executive directors had a contract of employment which provided for a year's notice from either party. The executive directors' contracts do not include compensation for severance as a result of a change of control.

Following the merger three of the four executive directors retired as directors.

Non-executive directors

The letters of appointment for non-executive directors include provisions allowing either party to terminate the appointment by giving three months' notice.

The directors' remuneration is disclosed in note 6.

Statement of directors' responsibilities in respect of the annual report and the financial statements

The directors are responsible for preparing the annual 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 surplus or deficit 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 judgments 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 2013 set out on pages 20 to 68 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 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 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 Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31st December 2013 and of the group's deficit 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 Strategic Report and 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
25th March 2014

Sunderland Marine Mutual Insurance Company Limited
Consolidated Income and Expenditure Account
Year Ended 31st December 2013

Technical account - general business	**Note**		**2013 £'000**		**2012 £'000**
Earned premiums, net of reinsurance					
Gross premiums written			92,453		95,325
Outward reinsurance premiums			(57,811)		(55,816)
			34,642		39,509
Change in the gross provision for unearned premiums	26		637		(7,862)
Change in the provision for unearned premium, reinsurers' share	18		1,302		9,017
			1,939		1,155
			36,581		40,664
Claims incurred, net of reinsurance					
Claims paid					
Gross amount			(62,685)		(61,863)
Reinsurers' share			31,609		27,252
			(31,076)		(34,611)
Change in provision for claims					
Gross amount	26		(3,823)		(8,899)
Reinsurers' share	18		9,130		13,651
Unexpired risk reserve			-		422
			5,307		5,174
			(25,769)		(29,437)
Net operating expenses before goodwill and purchase costs		(12,636)		(15,243)	
Goodwill and purchase costs		(1,482)		(1,537)	
Net operating expenses	5		(14,118)		(16,780)
Other operating income					
Brokerage income: group and share of joint ventures		3,939		3,961	
Less: share of joint venture's brokerage income		(1,570)		(1,724)	
Group brokerage income			2,369		2,237
Share of joint venture operating profit	10		222		284
Balance on the technical account – general business			(715)		(3,032)

Sunderland Marine Mutual Insurance Company Limited
Consolidated Income and Expenditure Account (continued)
Year Ended 31st December 2013

Non-technical account – general business	**Note**	**2013**	**2012**
		£'000	**£'000**
Balance on the technical account - general business		(715)	(3,032)
Investment income	7	2,037	2,490
Unrealised gains on investments	8	186	486
Investment expenses and charges	9	(1,136)	(477)
Operating surplus before goodwill and purchase costs		1,854	1,004
Goodwill and purchase costs		(1,482)	(1,537)
Operating surplus/(deficit)	10	372	(533)
Surplus/(deficit) on ordinary activities before tax	11	372	(533)
Tax on surplus/(deficit) on ordinary activities	13	(540)	(793)
Deficit on ordinary activities after tax		(168)	(1,326)
Minority interests		(65)	(94)
Deficit after taxation attributable to the member of the parent company for the financial year		(233)	(1,420)

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 2013

	Note	2013 £'000	2012 £'000
Group deficit for the financial year		(233)	(1,420)
Foreign exchange rate movements	25	(234)	85
Actuarial (deficit)/surplus on pension scheme	36	(278)	493
Revaluation of properties	15	166	-
Total losses recognised since the last annual report		(579)	(842)

Sunderland Marine Mutual Insurance Company Limited
Consolidated Balance Sheet
As at 31st December 2013

	Note		2013 £'000		2012 £'000
Assets					
Intangible assets					
Goodwill	14		3,870		3,341
Investments					
Land and buildings	15	8,068		8,249	
Investment in group undertakings and participating interests	16	-		606	
Financial assets					
- Equity securities at fair value through income	17	3,552		4,144	
- Debt securities at fair value through income	17	37,806		42,549	
- Derivatives at fair value through income	17	486		363	
- Deposits with credit institutions		10,234		11,208	
			60,146		67,119
Reinsurers' share of technical provisions					
Provision for unearned premiums	18	23,546		23,820	
Provision for unearned commission	18	(4,957)		(4,633)	
Claims outstanding	18	35,892		28,433	
			54,481		47,620
Debtors					
Debtors arising out of direct insurance operations	19	20,094		25,210	
Debtors arising out of reinsurance operations	20	8,697		10,202	
Other debtors	21	3,428		2,846	
			32,219		38,258
Other assets					
Tangible assets	22	530		532	
Cash and cash equivalents		7,527		6,101	
			8,057		6,633
Prepayments and accrued income					
Accrued interest and rent		294		429	
Deferred acquisition costs	23	6,159		6,135	
Other prepayments and accrued income		337		256	
			6,790		6,820
Total assets			165,563		169,791

Sunderland Marine Mutual Insurance Company Limited
Consolidated Balance Sheet (continued)
As at 31st December 2013

	Note		2013 £'000		2012 £'000
Liabilities					
Capital and reserves					
Revaluation reserve	24	365		202	
Other reserves: reserve fund	24	26,007		26,007	
Income and expenditure account accumulated surplus	24	8,327		9,069	
Total capital and reserves	25		34,699		35,278
Minority interest			187		190
Technical provisions					
Provision for unearned premiums: gross amount	26	38,244		40,728	
Claims outstanding: gross amount	26	63,245		62,044	
			101,489		102,772
Financial liabilities					
- Derivatives at fair value through income	28	141		37	
- Creditors arising out of direct insurance operations		1,974		2,757	
- Creditors arising out of reinsurance operations	29	19,691		23,839	
- Borrowings	30	1,415		-	
- Other creditors, including taxation and social security	31	3,457		2,539	
			26,678		29,172
Accruals and deferred income			1,568		1,343
			164,621		168,755
Pension liability	36		942		1,036
Total liabilities			165,563		169,791

These financial statements were approved by the board of directors on 25th March 2014 and were signed on its behalf by:

T.F. Hart

G.C. Parkinson

Company registration number: 16432

Sunderland Marine Mutual Insurance Company Limited
Company Balance Sheet
As at 31st December 2013

	Note		2013 £'000		2012 £'000
Assets					
Investments					
Land and buildings	15	7,630		7,824	
Investments in group undertakings and participating interests	16	10,903		17,826	
Financial assets:					
- Equity securities at fair value through income	17	3,552		-	
- Debt securities at fair value through income	17	37,459		18,730	
- Derivatives at fair value through income	17	486		274	
- Deposits with credit institutions		9,316		9,797	
			69,346		54,451
Reinsurers' share of technical provisions					
Provision for unearned premiums	18	23,262		36,830	
Provision for unearned commission	18	(4,892)		(10,651)	
Claims outstanding	18	35,763		57,626	
			54,133		83,805
Debtors					
Debtors arising out of direct insurance operations	19	20,274		25,294	
Debtors arising out of reinsurance operations	20	8,697		10,202	
Other debtors	21	789		1,377	
			29,760		36,873
Other assets					
Tangible assets	22	211		342	
Cash and cash equivalents		3,930		3,355	
			4,141		3,697
Prepayments and accrued income					
Accrued interest and rent		279		163	
Deferred acquisition costs	23	6,240		6,224	
Other prepayments and accrued income		245		211	
			6,764		6,598
Total assets			164,144		185,424

Sunderland Marine Mutual Insurance Company Limited
Company Balance Sheet (continued)
As at 31st December 2013

	Note		2013 £'000		2012 £'000
Liabilities					
Capital and reserves					
Revaluation reserve	24	2,155		10,026	
Other reserves: reserve fund	24	26,007		26,007	
Income and expenditure account accumulated surplus	24	9,007		912	
Total capital and reserves	25		37,169		36,945
Technical provisions					
Provision for unearned premiums: gross amount	26	37,722		40,050	
Claims outstanding gross amount	26	62,872		61,665	
			100,594		101,715
Financial liabilities					
- Derivatives at fair value through income	28	141		37	
- Creditors arising out of direct insurance operations		2,074		2,775	
- Creditors arising out of reinsurance operations	29	19,879		40,998	
- Borrowings	30	1,415		-	
- Other creditors, including taxation and social security	31	737		787	
			24,246		44,597
Accruals and deferred income			1,193		1,131
			163,202		184,388
Pension liability	36		942		1,036
Total liabilities			164,144		185,424

These financial statements were approved by the board of directors on 25th March 2014 and were signed on its behalf by:

T.F. Hart

G.C. Parkinson

Company registration number: 16432

Sunderland Marine Mutual Insurance Company Limited
Consolidated Cash Flow Statement
Year Ended 31st December 2013

	Note	2013 £'000	2012 £'000
Net cash outflow from operating activities	33	(2,338)	(6,317)
Dividends received from joint venture		216	112
Interest paid			
Bank interest paid		(120)	(157)
Taxation			
UK corporation tax paid		(124)	(211)
Capital expenditure			
Purchase of tangible fixed assets		(125)	(157)
Sale of tangible fixed assets		85	507
Acquisition			
Acquisition of subsidiary net of cash acquired	14	388	(335)
Financing			
Dividend paid by subsidiary undertaking		(71)	(97)
Expense from settlement of derivatives		(459)	(729)
		(2,548)	(7,384)
Cash flows were invested as follows:			
Increase in cash holdings	34	1,080	1,534
Portfolio investments			
Purchase of equity securities at fair value through income		1,236	120
Purchase of debt securities at fair value through income		43,599	88,333
Sale of equity securities at fair value through income		(2,143)	(207)
Sale of debt securities at fair value through income		(46,342)	(97,164)
Purchase of land and buildings		22	-
Net investment of cash flows		(2,548)	(7,384)
Movement in opening and closing portfolio investments net of financing			
Net cash inflow for year		1,080	1,534
Cash flow - portfolio investments		(3,628)	(8,918)
Movement arising from cash flows	34	(2,548)	(7,384)
Changes in market values and exchange rate effects	34	(3,953)	(868)
Short leasehold land and buildings acquired with subsidiary	14	22	-
Total movement in portfolio investments net of financing		(6,479)	(8,252)
Portfolio investments net of financing at 1st January		72,251	80,503
Portfolio investments net of financing at 31st December	34	65,772	72,251

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 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 annual 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.

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, case by case 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.

Accounting policies *(continued)*

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 are 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 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.

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.

Accounting policies *(continued)*

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 methods used for review of reserve adequacy are the chain ladder triangulation and the Bornhuetter-Ferguson methods.

The chain ladder triangulation 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 Bornhuetter-Ferguson method is a blend of the chain ladder method and of the loss ratio method whereby ultimate claims levels are estimated by applying a judgementally selected ultimate loss ratio to the ultimate earned premium for each accident year. The weight applied to each of these methods varies depending on the maturity of the accident year, with the later accident years having more weight given to the loss ratio method and less weight given to the level of claims incurred to date.

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'*.

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 are as set out in notes 17 and 28.

The group holds derivative financial instruments to hedge its foreign currency exposure and to support the 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.

Accounting policies *(continued)*

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.

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
Short leasehold land and buildings		7% 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.

Accounting policies (continued)

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 substantively 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.

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.

Accounting policies *(continued)*

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 member 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 approve 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 policyholders. The regulator monitors the group closely to ensure that it is satisfactorily managing affairs for the policyholders' 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.

Risk management *(continued)*

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 to catastrophic events by the use of reinsurance.

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 by type of contract excluding the unexpired risk reserve and reinsurance commission.-

	2013			2012		
	Gross £'000	**Reinsurance £'000**	**Net £'000**	**Gross £'000**	**Reinsurance £'000**	**Net £'000**
Marine	86,565	(47,610)	38,955	86,570	(39,257)	47,313
Aquaculture	14,924	(11,828)	3,096	16,202	(12,996)	3,206
Total	101,489	(59,438)	42,051	102,772	(52,253)	50,519

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

	2013			2012		
	Gross £'000	**Reinsurance £'000**	**Net £'000**	**Gross £'000**	**Reinsurance £'000**	**Net £'000**
Australasia	15,883	(8,333)	7,550	18,160	(8,073)	10,087
Europe	16,637	(9,688)	6,949	16,100	(8,086)	8,014
North America	40,933	(27,818)	13,115	42,257	(25,337)	16,920
United Kingdom	16,542	(8,958)	7,584	15,618	(6,793)	8,825
Others	11,494	(4,641)	6,853	10,637	(3,964)	6,673
Total	101,489	(59,438)	42,051	102,772	(52,253)	50,519

Risk management *(continued)*

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 claims notified, claims handling and loss adjustment expenses and claims incurred but not reported (IBNR) for each successive accident year at the balance sheet dates.

			Gross claims incurred			
	2008	**2009**	**2010**	**2011**	**2012**	**2013**
Accident year at end of	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Accident year	46,381	54,648	49,771	53,137	72,004	70,512
One year later	45,213	54,542	49,182	51,957	69,691	
Two years later	44,375	54,225	48,902	51,253		
Three years later	45,620	54,553	47,949			
Four years later	45,008	54,974				
Five years later	44,018					

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 during 2013 updated 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 Conduct 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 policyholder 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 investment managers. The guidelines impose strict diversification limits by credit rating, maturity and per issuer.

Risk management *(continued)*

The maximum exposure to credit risk amounts to £87,786,000 (2012: £98,116,000). This exposure includes all financial assets (with the exception of equities and derivatives) as detailed in note 32. 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	2013 Debt securities £'000	2013 Outward reinsurance debtors £'000	2012 Debt securities £'000	2012 Outward reinsurance debtors £'000
AAA	15,473	-	25,871	-
AA	10,693	5,745	5,841	7,621
A	4,474	1,862	4,463	2,127
BBB	3,306	747	3,397	85
BB	1,675	-	1,003	-
B	1,264	-	1,328	-
CCC - C	541	-	565	-
Not rated	380	56	81	113
Total	37,806	8,410	42,549	9,946

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 2013	No contractual maturity £'000	Less than one year £'000	Total £'000
Derivative financial liabilities	-	141	141
Creditors arising out of direct insurance operations	1,974	-	1,974
Creditors arising out of reinsurance operations	19,691	-	19,691
Borrowings	1,415	-	1,415
Other creditors, including taxation and social security	3,457	-	3,457
Total	26,537	141	26,678

Risk management *(continued)*

At 31st December 2012	No contractual maturity £'000	Less than one year £'000	Total £'000
Derivative financial liabilities	-	37	37
Creditors arising out of direct insurance operations	2,757	-	2,757
Creditors arising out of reinsurance operations	23,839	-	23,839
Other creditors, including taxation and social security	2,539	-	2,539
Total	29,135	37	29,172

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 are 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 asset backed securities.

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.

Risk management *(continued)*

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

At 31st December 2013	**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	3,552	-	-	3,552
Debt securities at fair value through income	14,664	22,413	729	37,806
Derivatives at fair value through income	-	486	-	486
Deposits with credit institutions	10,234	-	-	10,234
	28,450	22,899	729	52,078
Financial liabilities				
Derivatives at fair value through income	-	(141)	-	(141)

At 31st December 2012	**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	4,144	-	-	4,144
Debt securities at fair value through income	15,789	26,011	749	42,549
Derivatives at fair value through income	-	363	-	363
Deposits with credit institutions	11,208	-	-	11,208
	31,141	26,374	749	58,264
Financial liabilities				
Derivatives at fair value through income	-	(37)	-	(37)

Risk management *(continued)*

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

	Total £'000
Balance at 1st January 2013	749
Purchases	672
Sales	(735)
Realised gains	30
Unrealised gains	13
Balance at 31st December 2013	729

The realised gains are included within investment income in the income and expenditure account. The unrealised gains are included within unrealised 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 financial 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 (price 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 during 2013 was 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. During 2013 there was 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.

Risk management *(continued)*

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 2013	**Assets**	**Liabilities**	**Net assets/ (liabilities)**	**Forward contracts**	**Net assets/ (liabilities) after forward contracts**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Australian Dollars	22,305	(13,698)	8,607	(7,636)	971
Canadian Dollars	26,774	(16,431)	10,343	(11,918)	(1,575)
Euro	15,117	(19,316)	(4,199)	1,700	(2,499)
Norwegian Kroner	129	(134)	(5)	-	(5)
New Zealand Dollars	5,067	(4,172)	895	-	895
US Dollars	37,658	(43,900)	(6,242)	5,203	(1,039)
South African Rand	2,429	(1,303)	1,126	(579)	547
	109,479	(98,954)	10,525	(13,230)	(2,705)
Sterling	56,084	(31,910)	24,174	13,230	37,404
	165,563	(130,864)	34,699	-	34,699
At 31st December 2012					
Australian Dollars	23,645	(16,609)	7,036	(8,453)	(1,417)
Canadian Dollars	29,285	(20,378)	8,907	(10,325)	(1,418)
Euro	16,871	(21,906)	(5,035)	4,919	(116)
Norwegian Kroner	85	(194)	(109)	-	(109)
New Zealand Dollars	5,061	(4,021)	1,040	(608)	432
US Dollars	34,536	(39,894)	(5,358)	4,782	(576)
South African Rand	2,891	(1,344)	1,547	(730)	817
	112,374	(104,346)	8,028	(10,415)	(2,387)
Sterling	57,417	(30,167)	27,250	10,415	37,665
	169,791	(134,513)	35,278	-	35,278

Risk management *(continued)*

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:

	2013 £'000	**2012 £'000**
0.5% increase in interest rates	(194)	(246)
0.5% decrease in interest rates	213	289

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 group's exposure to sovereign debt and financial institutions' debt securities in European countries by maturity:

	2013				**2012**			
	Less Than Five years £'000	**Five To Ten years £'000**	**Over twenty Five years £'000**	**Total £'000**	**Less Than Five years £'000**	**Five To Ten years £'000**	**Over twenty Five years £'000**	**Total £'000**
Ireland	-	-	-	-	148	-	-	148
France	727	-	-	727	721	-	-	721
Germany	901	219	-	1,120	2,259	-	40	2,299
The Netherlands	379	-	-	379	1,042	263	-	1,305
Denmark	91	-	-	91	-	91	-	91
Finland	601	-	-	601	500	100	-	600
Norway	39	-	-	39	383	-	-	383
Supranational	303	-	-	303	-	-	-	-
Turkey	-	-	-	-	267	-	-	267
Portugal	-	-	-	-	16	-	-	16
Italy	-	-	-	-	24	-	-	24
Spain	161	-	-	161	7	-	-	7
Luxembourg	67	-	-	67	98	114	-	212
Romania	-	43	-	43	-	-	-	-
Sweden	157	-	-	157	-	-	-	-
Switzerland	68	-	-	68	-	-	-	-
	3,494	262	-	3,756	5,465	568	40	6,073

The exposure classified as Supranational relates to debt securities issued by the European Investment Bank and the European Bank for Reconstruction and Development.

Risk management *(continued)*

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

	2013 £'000	2012 £'000
10% increase in equity price	355	414
10% decrease in equity price	(355)	(414)

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.

__Capital management__

The required capital, as measured by the UK Prudential Regulatory Authority's (PRA'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 2013.

The group capital comprises the capital and reserves of £34,699,000 shown in the consolidated balance sheet. The company manages capital on an adjusted solo solvency basis as prescribed by the PRA. This core tier one capital was £37,168,000 as at 31st December 2013 (2012: £36,956,000) of which a total of £21,221,000 (2012: £20,748,000) was held in local currency to support local solvency requirements in Australia, USA, Canada and New Zealand.

At 31st December 2013, the insurance subsidiary Sunderland Marine (Africa) Limited held regulatory capital of £1,338,000 (2012: £1,465,000).

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 business product and geographical analysis of gross premium income, result before taxation and net assets has not been provided.

3. Analysis of gross written premiums

Gross written premiums resulting from risks arising:

	2013 £'000	2012 £'000
Direct business in the United Kingdom	13,879	11,917
Direct business in other countries	76,854	82,116
Non direct business	1,720	1,292
	92,453	95,325

4. Prior years' claims provisions

Over 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:

	2013 £'000	2012 £'000
Direct	3,790	1,307
Inward reinsurance	215	357

5. Net operating expenses

	2013 £'000	2012 £'000
Acquisition costs	14,284	14,966
Change in deferred acquisition costs (note 23)	(425)	(1,539)
Administration expenses	13,409	13,871
Reinsurance commissions and profit participation	(13,855)	(11,792)
Change in unearned reinsurance commission (note 18)	705	1,274
	14,118	16,780

6. Particulars of employees

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

	2013 No	2012 No
Number of staff – full time	103	108
Number of staff – part time	18	18
	121	126
Staff employed by the joint venture company	35	36
	156	162

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

	2013 £'000	2012 £'000
Wages and salaries	6,816	6,899
Social security costs	487	417
Staff pension costs	906	875
Directors' pension costs	170	61
	8,379	8,252

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

	2013 £'000	2012 £'000
Emoluments receivable	1,328	1,326
Value of company pension contributions to defined benefit schemes	61	61
	1,389	1,387

6. Particulars of employees (continued)

Fees of £21,740 (2012: £68,521) payable to one director were paid, with the addition of VAT, to his company, Sandwood Services Limited. Fees of £11,209 (2012. £34,140) payable to another director were paid to his company Sthagdaa Limited.

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 £419,116 (2012: £411,140) including pension contributions of £nil (2012· £nil). His accrued pension at the year-end was £133,358 (2012: £131,084) and his accrued lump sum was £375,000 (2012: £375,000).

Four directors accrued benefits under a company pension scheme (2012. 4)

7. Investment income

	2013 £'000	2012 £'000
Interest income: group and share of joint venture	514	672
Less· share of joint venture's interest income	(1)	(2)
Interest income	513	670
Other investment income	1,144	1,458
Interest on defined benefit pension plan obligation	(1,207)	(1,134)
Expected return on defined benefit pension plan assets	1,440	1,277
Exchange gain	147	219
	2,037	2,490

Income from listed investments included in other investment income was £1,090,000 (2012: £1,401,000).

8. Unrealised gains on investments

	2013 £'000	2012 £'000
Unrealised gains on investments	186	486

9. Investment expenses and charges

	2013 £'000	2012 £'000
Investment management expenses, including interest	290	350
Derivative charge	440	25
Losses on the realisation of investments	406	102
	1,136	477

10. Operating surplus/(deficit)

Of the group operating result, £222,000 surplus (2012: £284,000) is attributable to the share of the operating result in the joint venture.

11. Surplus/(deficit) on ordinary activities before tax

	2013 £'000	2012 £'000
Surplus/(deficit) on ordinary activities before tax is stated after charging/(crediting).		
Overdraft interest	118	157
Depreciation on freehold land and buildings	142	142
Depreciation on short leasehold land and buildings	2	-
Depreciation on tangible fixed assets	217	309
Profit on sale of fixed assets	(18)	-
Amortisation of goodwill	1,482	1,537
Exchange and translation gains	(549)	(228)
Derivative charge	440	25
Operating lease costs - land and buildings	320	319
- other items	184	233
Auditor's remuneration:		
Audit of these financial statements	154	152
Amounts receivable by the auditor and their associates in respect of		
Audit of financial statements of subsidiaries	53	73
Other assurance services pursuant to legislation	205	210
Audit of pension scheme	5	4
Corporate finance services	194	54
All other services (principally pension advice)	27	148

12. Surplus attributable to member of the parent company

The surplus in the accounts of the parent company was £8,441,000 (2012: £2,851,000)

13. Tax on surplus/(deficit) on ordinary activities

	2013 £'000	2012 £'000
The charge for taxation is computed as follows:		
UK corporation tax on the taxable surplus/(deficit) for the year at 23.25% (2012: 24.5%)	(32)	137
Adjustment in respect of previous periods	(131)	(7)
	(163)	130
Double taxation relief	-	(5)
	(163)	125
Overseas tax	648	540
Adjustment in respect of previous periods	23	(10)
	671	530
Share of joint venture's current taxation	44	59
Share of joint venture's adjustment in respect of previous periods	-	(18)
	44	41
Total current taxation	552	696
Deferred tax		
(Reversal)/origination of timing differences	(20)	97
Share of joint venture's deferred tax	8	-
Total deferred taxation (note 27)	(12)	97
Tax on surplus/(deficit) on ordinary activities	540	793

13. Tax on surplus/(deficit) on ordinary activities (continued)

	2013 £'000	2012 £'000
Factors affecting the tax charge for the period		
Surplus/(deficit) on ordinary activities before tax	372	(533)
Current tax at 23.25% (2012. 24.5%)	86	(131)
Effects of:		
Non taxable income	(1,630)	(1,240)
Expenses not deductible for tax purposes	241	579
Higher rates of overseas tax	2,278	1,037
Capital allowances in excess of depreciation	36	143
Other short-term timing differences	(24)	(240)
Double taxation relief	-	(5)
Adjustments to tax charge in respect of previous periods	(108)	(35)
Losses utilised	(330)	-
Deferred tax asset not recognised	3	588
Total current tax charge	552	696

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

14. Goodwill

Group

	2013 £'000
Cost	
At 1st January 2013	10,022
Adjustment due to exchange rates	(67)
Addition	2,031
At 31st December 2013	11,986
Amortisation	
At 1st January 2013	6,681
Adjustment due to exchange rates	(47)
Charged in year	1,482
At 31st December 2013	8,116
Net book value	
At 31st December 2013	3,870
At 31st December 2012	3,341

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, Van Olst de Graaff & Co BV, Assurantiekantoor P M Arkesteijn and Marine Underwriters is being amortised over five years.

Goodwill in respect of the acquisition of Knighthood Corporate Assurance Services Plc is being amortised over 10 years from the date of the original acquisition.

On 20th February 2012 the company acquired an additional 9% shareholding in Van Olst de Graaff & Co BV, an insurance broker trading in the Netherlands for a consideration of £335,000 satisfied solely by cash. 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 Goodwill of £242,000 arising on the acquisition is being amortised over five years.

On 1st December 2013 the company acquired the remaining 51%, which it did not already own, of Knighthood Corporate Assurance Services Plc, an insurance broker trading in England. 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	
Land and buildings	22
Tangible assets	206
Other debtors	2,099
Prepayments	82
Cash at bank	2,888
Other creditors	(4,021)
Accruals	(39)
Deferred tax	(8)
Corporation tax	(87)
Net assets acquired	1,142
51% of fair value of shareholders' funds acquired	582
Goodwill arising on acquisition	2,031
Total consideration	2,613

The consideration was satisfied by cash of £2,500,000, the gift of a company car valued at £33,000 and deferred consideration of £80,000.

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

The deficit arising from Knighthood Corporate Assurance Services Plc in December 2013 was £173,000.

14. Goodwill (continued)

In respect of the acquisition of the shares in Knighthood Corporate Assurance Services plc, schedule 6 paragraph 9 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 requires that goodwill is calculated as the excess of consideration paid over the identifiable assets and liabilities of a subsidiary undertaking at the date it becomes a subsidiary undertaking. Where a company acquires the remaining share capital of a joint venture, this has the effect that the group's share of profits and losses and reserve movements of its joint venture becomes reclassified as goodwill.

The directors consider that using this methodology would fail to give a true and fair view. They have therefore opted to account for the acquisition in line with paragraph 89 of FRS2, that is to calculate goodwill as the sum of goodwill arising from each purchase of an interest in the relevant undertaking. The effect of this departure increases goodwill and reserves by £387,000 There is no impact on the reported deficit for the year.

15. Land and buildings

	Freehold land and buildings £'000	Short leasehold £'000	Total £'000
Group			
Cost or valuation			
At 1st January 2013	8,580	-	8,580
Adjustment due to exchange rates	(256)	-	(256)
Revaluation through reserves	(290)	-	(290)
Addition	22	-	22
Acquired with subsidiary	-	69	69
At 31st December 2013	8,056	69	8,125
Depreciation			
At 1st January 2013	331	-	331
Adjustment due to exchange rates	(9)	-	(9)
Charge for the year	142	2	144
Revaluation through reserves	(456)	-	(456)
Acquired with subsidiary	-	47	47
At 31st December 2013	8	49	57
Net book value			
At 31st December 2013	8,048	20	8,068
At 31st December 2012	8,249	-	8,249

15. Land and buildings (continued)

	Freehold land and buildings £'000
Company	
Valuation	
At 1st January 2013	8,134
Adjustment due to exchange rates	(246)
Revaluation through reserves	(272)
Addition	22
At 31st December 2013	7,638
Depreciation	
At 1st January 2013	310
Adjustment due to exchange rates	(8)
Charge for the year	133
Revaluation through reserves	(427)
At 31st December 2013	8
Net book value	
At 31st December 2013	7,630
At 31st December 2012	7,824

The group's freehold property in the UK was revalued to £6,000,000 at 21st November 2013 by external valuers Bradley Hall 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.

Overseas freehold property amounting to £1,240,000 at 2nd September 2013 was valued by suitably qualified external valuers, Sutherland Farrelly Pty Ltd. Overseas freehold property amounting to £418,000 at 26th August 2013 was valued by suitably qualified external valuers CBRE Valuation and Advisory Services. The properties were valued on the basis of open market value for existing use.

Overseas freehold property amounting to £398,000 was valued by suitably qualified external valuers, Duke & Cooke Limited, Valuers & Property Specialists during August 2010.

The total cost of all freehold land and buildings at 31st December 2013 was £8,600,000 (2012: £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	82%	Brokerage
Harlock Murray Underwriting Limited	Canada	100%	Broking & management services
Knighthood Corporate Assurance Services Plc	England	100%	Insurance broker

At December 2012 Knighthood Corporate Assurance Services Plc was treated as a joint venture by virtue of the joint control exercised over the financial and operating policies of the company At December 2013 Knighthood Corporate Assurance Services Plc was treated as a subsidiary following the acquisition by the company of the remaining 51% shareholding, which it did not already own.

The reinsurance arrangement between the company and SM Insurance (Bermuda) Limited ceased on 30th September 2013. At this date the invested assets and technical provisions of SM Insurance (Bermuda) Limited were transferred to the company On 17th December 2013 SM Insurance (Bermuda) Limited proposed a dividend payment to the company of £7,680,000

The effect of these transactions in the company balance sheet has been to reduce the investment in group undertakings by £7,680,000, increase investments by £24,195,000, reduce reinsurers' share of technical provisions by £34,689,000 and reduce creditors arising out of reinsurance operations by £18,174,000. Total capital and reserves of the company were unaffected as the dividend receipt in the income and expenditure account was offset by a reduction in the revaluation reserve.

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

	Shares in group undertakings £'000
Group	
At 1st January 2013	606
Share of profits of joint venture	222
Share of joint venture current taxation	(44)
Share of joint venture deferred taxation	(8)
Dividend paid	(216)
Transferred to assets and liabilities on acquisition	(560)
At 31st December 2013	-
Company	
At 1st January 2013	17,826
Adjustment due to exchange movements	(439)
Decrease in loans owed by subsidiary undertakings	(216)
Revaluation of subsidiaries through reserves	(7,869)
Revaluation of subsidiaries through income and expenditure account	(1,012)
Acquisition	2,613
At 31st December 2013	10,903

Sunderland Marine (Africa) Limited and SM Insurance (Bermuda) Limited have been valued at net asset value in the company balance sheet at 31st December 2013.

Knighthood Corporate Assurance Services Plc was revalued in the company balance sheet by suitably qualified external valuers at 8th August 2013.

Salvus Bain Management (USA) LLC was revalued in the company balance sheet by suitably qualified external valuers at 31st December 2010.

The investment in Harlock Murray Underwriting Limited held by the company at December 2010 was revalued in the company balance sheet by suitably qualified valuers. The valuation was increased during 2011 by the cost of acquiring the remaining shares in the company.

The investment in Van Olst de Graaff & Co BV held by the company at December 2010 was re-valued in the company balance sheet by suitably qualified valuers The valuation was increased during 2012 by the cost of acquiring another 9% of the shares in the company.

The directors have updated the valuations of Salvus Bain Management (USA) LLC, Harlock Murray Underwriting Limited and Van Olst de Graaff & Co BV at 31st December 2013. There were no material differences arising in the valuations of Salvus Bain Management (USA) LLC and Harlock Murray Underwriting Limited. The valuation of Van Olst de Graaff & Co BV was revalued downwards by £1,012,000 due to a fall in the company's revenue which is anticipated to continue for the forseeable future.

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

	2013 £'000	2012 £'000
Share of joint venture's assets	-	1,455
Share of joint venture's liabilities	-	(849)
	-	606

At the previous year end the balance due to the group from its joint venture was £333,000.

The total cost of investments in group undertakings at 31st December 2013 is £11,792,000 (2012. £9,179,000).

17. Financial assets

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Equity securities at fair value through income				
Market value	3,552	4,144	3,552	-
Cost	3,371	4,298	3,521	-
Debt securities at fair value through income				
Market value	37,806	42,549	37,459	18,730
Cost	37,524	42,118	37,566	18,772
Derivatives at fair value through income	486	363	486	274

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 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 2013	23,820	(4,633)	28,433	47,620
Adjustment due to exchange movements	(1,576)	381	(1,671)	(2,866)
Movement during the year	1,302	(705)	9,130	9,727
At 31st December 2013	23,546	(4,957)	35,892	54,481
Company				
At 1st January 2013	36,830	(10,651)	57,626	83,805
Adjustment due to exchange movements	(1,779)	514	(1,985)	(3,250)
Movement during the year	5,487	(2,113)	4,893	8,267
Transfer from subsidiary	(17,276)	7,358	(24,771)	(34,689)
At 31st December 2013	23,262	(4,892)	35,763	54,133

19. Debtors arising out of direct insurance operations

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Amounts owed by policyholders	19,979	25,113	20,159	25,197
Amounts owed by intermediaries	115	97	115	97
	20,094	25,210	20,274	25,294

20. Debtors arising out of reinsurance operations

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Debtors arising out of inward reinsurance operations	287	256	287	256
Debtors arising out of outward reinsurance operations	8,410	9,946	8,410	9,946
	8,697	10,202	8,697	10,202

21. Other debtors

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Corporation tax	133	-	133	-
Other taxation	81	811	81	746
Deferred taxation (note 27)	346	355	123	115
Other debtors	2,868	1,680	452	516
	3,428	2,846	789	1,377

22. Tangible fixed assets

	Fixtures & fittings £'000	Motor vehicles £'000	Computers £'000	Total £'000
Group				
Cost				
At 1st January 2013	988	343	1,152	2,483
Adjustment due to exchange movements	(17)	(20)	(30)	(67)
Additions	7	58	60	125
Disposals	(7)	(255)	(246)	(508)
Acquired with subsidiary	457	296	189	942
At 31st December 2013	1,428	422	1,125	2,975
Depreciation				
At 1st January 2013	867	165	919	1,951
Adjustment due to exchange movements	(13)	(12)	(26)	(51)
Charge for the year	49	49	119	217
On disposals	(7)	(160)	(241)	(408)
Acquired with subsidiary	439	122	175	736
At 31st December 2013	1,335	164	946	2,445
Net book value				
At 31st December 2013	93	258	179	530
At 31st December 2012	121	178	233	532

22. Tangible fixed assets (continued)

	Fixtures & fittings £'000	Motor vehicles £'000	Computers £'000	Total £'000
Company				
Cost				
At 1st January 2013	409	172	491	1,072
Adjustments due to exchange movements	(5)	(15)	6	(14)
Additions	5	20	42	67
Disposals	-	(70)	(30)	(100)
At 31st December 2013	409	107	509	1,025
Depreciation				
At 1st January 2013	343	72	315	730
Adjustments due to exchange movements	(2)	(8)	7	(3)
Charge for the year	30	27	101	158
Disposals	-	(46)	(25)	(71)
At 31st December 2013	371	45	398	814
Net book value				
At 31st December 2013	38	62	111	211
At 31st December 2012	66	100	176	342

23. Deferred acquisition costs

	£'000
Group	
At 1st January 2013	6,135
Adjustment due to exchange movements	(401)
Movement during the year	425
At 31st December 2013	6,159
Company	
At 1st January 2013	6,224
Adjustment due to exchange movements	(399)
Movement during the year	415
At 31st December 2013	6,240

24. Capital and reserves

	Revaluation reserve £'000	Reserve fund £'000	Income & expenditure account: Translation reserve £'000	Income & expenditure account: I&E reserve £'000	Income & expenditure account: Total £'000
Group					
At 1st January 2013	202	26,007	(277)	9,346	9,069
Deficit for year	-	-	-	(233)	(233)
Foreign exchange rate movements	(3)	-	(231)	-	(231)
Actuarial deficit recognised in pension scheme	-	-	-	(278)	(278)
Revaluation of properties	166	-	-	-	-
At 31st December 2013	365	26,007	(508)	8,835	8,327

	Revaluation reserve £'000	Reserve fund £'000	Income & expenditure account: Translation reserve £'000	Income & expenditure account: I&E reserve £'000	Income & expenditure account: Total £'000
Company					
At 1st January 2013	10,026	26,007	(838)	1,750	912
Surplus for year	-	-	-	8,441	8,441
Revaluation of properties	155	-	-	-	-
Revaluation of subsidiaries	(7,869)	-	-	-	-
Foreign exchange rate movements	(157)	-	(68)	-	(68)
Actuarial deficit recognised in pension scheme	-	-	-	(278)	(278)
At 31st December 2013	2,155	26,007	(906)	9,913	9,007

25. Reconciliation of movements on capital and reserves

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
At 1st January	35,278	36,120	36,945	37,340
(Deficit)/surplus for year	(233)	(1,420)	8,441	2,851
Revaluation of subsidiaries	-	-	(7,869)	(3,733)
Revaluation of properties	166	-	155	-
Foreign exchange rate movements	(234)	85	(225)	(6)
Actuarial (deficit)/surplus recognised in pension scheme	(278)	493	(278)	493
At 31st December	34,699	35,278	37,169	36,945

26. Technical provisions – gross amounts

	Provision for unearned premiums £'000	Claims outstanding £'000	Total £'000
Group			
At 1st January 2013	40,728	62,044	102,772
Adjustment due to exchange movements	(1,847)	(2,622)	(4,469)
Movement during the year	(637)	3,823	3,186
At 31st December 2013	38,244	63,245	101,489
Company			
At 1st January 2013	40,050	61,665	101,715
Adjustment due to exchange movements	(1,742)	(2,551)	(4,293)
Movement during the year	(586)	3,758	3,172
At 31st December 2013	37,722	62,872	100,594

27. 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 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
At 1st January	355	463	115	377
Adjustment due to exchange movements	(21)	(11)	(11)	(6)
Adjusted provision at 1st January	334	452	104	371
Movement during year	12	(97)	19	(256)
At 31st December	346	355	123	115
Differences between the accumulated depreciation and taxation allowances on fixed assets	179	129	(14)	(38)
Other timing differences	167	226	137	153
	346	355	123	115

The timing differences above relate to accumulated losses in jurisdictions where the group has a taxable presence. They have been recognised only to the extent that it is probable that they are recoverable in the next five years.

28. Derivative liabilities

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Derivatives at fair value through income	141	37	141	37

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

29. Creditors arising out of reinsurance operations

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Amounts owing to subsidiary undertakings	-	-	188	17,178
Other creditors arising out of reinsurance operations	19,691	23,839	19,691	23,820
	19,691	23,839	19,879	40,998

30. Creditors – borrowings

Creditors include bank borrowings which are due for repayment as follows:

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Bank overdraft	1,415	-	1,415	-
	1,415	-	1,415	-
Amounts repayable:				
In one year or less or on demand	1,415	-	1,415	-
	1,415	-	1,415	-

Interest was charged at 1 65% above base rate on the overdraft

31. Other creditors including taxation and social security

	Group 2013 £'000	Group 2012 £'000	Company 2013 £'000	Company 2012 £'000
Corporation tax	55	124	8	124
Other taxes and social security	705	507	549	425
Other creditors	2,697	1,908	180	238
	3,457	2,539	737	787

32. Financial assets and liabilities

Group

At 31st December 2013	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	3,552	-	-	3,552	3,552
Debt securities at fair value through income	37,806	-	-	37,806	37,806
Derivatives at fair value through income	486	-	-	486	486
Deposits with credit institutions	-	10,234	-	10,234	10,234
Debtors arising out of direct insurance operations	-	20,094	-	20,094	20,094
Debtors arising out of reinsurance operations	-	8,697	-	8,697	8,697
Other debtors	-	3,428	-	3,428	3,428
Cash and cash equivalents	-	7,527	-	7,527	7,527
At 31st December 2013	41,844	49,980	-	91,824	91,824
Financial liabilities					
Derivatives at fair value through income	(141)	-	-	(141)	(141)
Creditors arising out of direct insurance operations	-	-	(1,974)	(1,974)	(1,974)
Creditors arising out of reinsurance operations	-	-	(19,691)	(19,691)	(19,691)
Borrowings	-	-	(1,415)	(1,415)	(1,415)
Other creditors, including taxation and social security	-	-	(3,457)	(3,457)	(3,457)
At 31st December 2013	(141)	-	(26,537)	(26,678)	(26,678)

32. Financial assets and liabilities (continued)

At 31st December 2012	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	4,144	-	-	4,144	4,144
Debt securities at fair value through income	42,549	-	-	42,549	42,549
Derivatives at fair value through income	363	-	-	363	363
Deposits with credit institutions	-	11,208	-	11,208	11,208
Debtors arising out of direct insurance operations	-	25,210	-	25,210	25,210
Debtors arising out of reinsurance operations	-	10,202	-	10,202	10,202
Other debtors	-	2,846	-	2,846	2,846
Cash and cash equivalents	-	6,101	-	6,101	6,101
At 31st December 2012	47,056	55,567	-	102,623	102,623
Financial liabilities					
Derivatives at fair value through income	(37)	-	-	(37)	(37)
Creditors arising out of direct insurance operations	-	-	(2,757)	(2,757)	(2,757)
Creditors arising out of reinsurance operations	-	-	(23,839)	(23,839)	(23,839)
Other creditors, including taxation and social security	-	-	(2,539)	(2,539)	(2,539)
At 31st December 2012	(37)	-	(29,135)	(29,172)	(29,172)

33. Reconciliation of surplus/(deficit) on ordinary activities before taxation to net cash outflow from operating activities

	2013 £'000	2012 £'000
Surplus/(deficit) on ordinary activities before taxation	372	(533)
Share of profit of joint ventures	(222)	(284)
Amortisation of goodwill	1,482	1,537
Depreciation	361	451
Profit on sale of fixed assets	(18)	-
Derivative charge	440	25
Loss on sale of liquid investments	406	102
Adjustment to carrying value of liquid investments	(186)	(486)
Foreign exchange rate fluctuation	3,581	1,250
Tax suffered on investment income	(671)	(530)
Bank interest charge	118	157
Pension contributions in excess of expense in income and expenditure account	(372)	(494)
Increase in reinsurers' share of technical provisions	(6,861)	(20,645)
Decrease/(increase) in debtors	8,262	(10,788)
Decrease/(increase) in prepayments and accrued income	112	(1,266)
(Decrease)/increase in technical provisions	(1,283)	13,858
(Decrease)/increase in creditors	(8,045)	11,212
Increase in accruals and deferred income	186	117
Net cash outflow from operating activities	(2,338)	(6,317)

34. Movement in cash, portfolio investments and financing

	Deposits and cash at bank net of overdraft £'000	Equity securities £'000	Debt securities £'000	Land and buildings £'000	Total £'000
At 1st January 2013	17,309	4,144	42,549	8,249	72,251
Cash flow	1,080	(907)	(2,743)	22	(2,548)
Acquired with subsidiary	-	-	-	22	22
Changes to market value	-	315	(535)	22	(198)
Changes in currencies	(2,043)	-	(1,465)	(247)	(3,755)
At 31st December 2013	16,346	3,552	37,806	8,068	65,772

35. Commitments under operating leases

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

	2013 Land & buildings £'000	2013 Other items £'000	2012 Land & buildings £'000	2012 Other items £'000
Group				
Operating leases which expire:				
Within one year	22	48	157	25
Within two to five years	331	103	120	139
	353	151	277	164

36. Pension commitments

Group and Company

Defined benefit pension scheme

	2013 £'000	2012 £'000
Present value of funded defined benefit obligations	(29,041)	(25,652)
Fair value of plan assets	28,099	24,616
Deficit	(942)	(1,036)

36. Pension commitments (continued)

Movements in present value of defined benefit obligation

	2013 £'000	2012 £'000
At 1st January	25,652	22,983
Current service cost	665	573
Past service cost	109	-
Interest cost	1,207	1,134
Actuarial losses	1,481	1,230
Benefits paid	(281)	(444)
Contributions by members	208	176
At 31st December	29,041	25,652

Movements in fair value of plan assets

	2013 £'000	2012 £'000
At 1st January	24,616	20,960
Expected return on plan assets	1,440	1,277
Actuarial gains	1,203	1,723
Contributions by employer	913	924
Contributions by members	208	176
Benefits paid	(281)	(444)
At 31st December	28,099	24,616

Expense recognised in the income and expenditure account

	2013 £'000	2012 £'000
Current service cost	665	573
Past service cost	109	-
Interest on defined benefit pension plan obligation	1,207	1,134
Expected return on defined benefit pension plan assets	(1,440)	(1,277)
Total	541	430

36. Pension commitments (continued)

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

	2013 £'000	2012 £'000
Net operating expenses	774	573
Investment income	(233)	(143)
	541	430

The total amount recognised in the statement of total recognised gains and losses in respect of actuarial gains and losses is a deficit of £278,000 (2012: surplus of £493,000).

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

	2013 £'000	2012 £'000
Equities	12,483	10,372
Bonds	13,759	12,510
Hedge fund of funds	1,718	1,286
Cash	139	448
	28,099	24,616
Actual return on plan assets	2,643	3,000

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

36. Pension commitments (continued)

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

	2013 %	2012 %
Discount rate	4.65	4.65
Expected rate of return on plan assets	5.75	5.75
Expected return on plan assets at beginning of the period	5.75	6 0
Future salary increases	3.0	3 0
Inflation	3.65	3.20
Mortality	S1PACMI + u'pin	S1PAmc + u'pin

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 65 years old to live for 22 years (male) and 24 years (female).

The most recent full actuarial valuation of the pension scheme was completed for the period ended 31st December 2011

History of plan

The history of the plan for the current and prior periods is as follows.

Balance sheet	2013 £'000	2012 £'000	2011 £'000	2010 £'000	2009 £'000
Present value of scheme liabilities	(29,041)	(25,652)	(22,983)	(21,103)	(18,257)
Fair value of scheme assets	28,099	24,616	20,960	20,209	16,994
Deficit	(942)	(1,036)	(2,023)	(894)	(1,263)

	2013 %	2012 %	2011 %	2010 %	2009 %
Experience adjustments on scheme liabilities as a percentage of scheme liabilities	(5.1)	(4.8)	(1.2)	(5.2)	(20.7)
Experience adjustments on scheme assets as a percentage of scheme assets	4.3	7.0	(6.0)	5.5	13.4

The company expects to contribute approximately £1,473,000 to its defined benefit plan in the next financial year.

36. Pension commitments (continued)

The company contributed £181,000 (2012: £175,000) to the pension scheme for administration expenses, insurance premiums for death in service benefits and the pension protection fund levies.

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 £256,000 (2012. £282,000) There were no outstanding or prepaid contributions at either the beginning or the end of the financial year. Contributions of £46,000 (2012· £81,000) were also made to a government superannuation scheme.

37. Guarantees

The reinsurance arrangement between the company and SM Insurance (Bermuda) Limited ceased on 30th September 2013. At this date the invested assets and technical provisions of SM Insurance (Bermuda) Limited were transferred to the company and SM Insurance (Bermuda) Limited has been released from the guarantee in favour of Barclays Bank Plc.

The company has granted a number of guarantees in favour of its subsidiary company Sunderland Marine (Africa) Limited. The level of guarantees range from R3,000,000 to unlimited The guarantees provide comfort to the policyholders of Sunderland Marine (Africa) Limited as the company will stand as a guarantor on certain policies written by that company

These guarantees are in the normal course of business. Whilst the outcome of some of these matters cannot precisely be foreseen, the directors do not expect any of these arrangements, after allowing for provisions already made, to result in significant loss to the company.

38. Post balance sheet event

On 28th February 2014 The North of England Protecting and Indemnity Association Limited acquired the company by becoming the sole member limited by guarantee

From 28th February 2014 the company's immediate parent undertaking will be The North of England Protecting and Indemnity Association Limited which will be the ultimate parent company, incorporated in England.

The largest group in which the results of the company will be consolidated from 28th February 2014 will be that headed by The North of England Protecting and Indemnity Association Limited. No other group financial statements will include the results of the company The consolidated financial statements of this group will be available to the public and may be obtained from The North of England Protecting and Indemnity Association Limited, The Quayside, Newcastle upon Tyne, NE1 3DU.