Company Registration No: 01810801

DIRECT LINE INSURANCE LIMITED

DIRECTORS' REPORT AND FINANCIAL STATEMENTS

31 DECEMBER 2012

Group Secretariat
Direct Line Insurance Group plc
Churchill Court
Westmoreland Road
Bromley
BR1 1DP

CONTENTS

DIRECT LINE INSURANCE LIMITED 01810801

OFFICERS AND PROFESSIONAL ADVISERS

DIRECTORS	P Edwards (20th August 2013) D P Evans J P Greenwood C Morton (20th August 2013) H Tomlinson (20th August 2013)
SECRETARY	P A Hutchings
REGISTERED OFFICE	Churchill Court Westmoreland Road Bromley BR1 1DP
AUDITOR	Deloitte LLP Chartered Accountants London

Registered in England and Wales

DIRECTORS' REPORT

The directors present their annual report and the audited financial statements for the year ended 31 December 2012

ACTIVITIES AND BUSINESS REVIEW

Activity

The principal activity of the Company was the provision of general insurance and the Company was regulated by the Financial Services Authority (FSA) The Company ceased underwriting activities on 10 December 2011

In preparation for the new European Union Solvency II regulations which were anticipated to be implemented in January 2014 it was decided that the group structure of the insurance division of the Royal Bank of Scotland Group plc should be simplified as part of this the ownership of the Company was transferred from RBS Insurance Group Limited to U K Insurance Limited on 10 December 2011

RBS Insurance Group Limited changed its name on 3 February 2012 to Direct Line Insurance Group plc

The Company is a subsidiary of Direct Line Insurance Group plc (DLIG) which provides the company with direction and access to all central resources it needs and determines policies in all key areas such as finance risk, human resources or environment For this reason, the directors believe that performance indicators specific to the Company are not necessary or appropriate for an understanding of the development, performance or position of the business The annual report of Direct Line Insurance Group plc reviews these matters on a group basis Copies can be obtained from Direct Line Group Secretariat Churchill Court Westmoreland Road, Bromley BR1 1DP the Registrar of Companies or through the Group's website at www directlinegroup com

Review of the year

Business review

The directors are satisfied that the Company has not traded in the year due to part VII transfer

In accordance with an Order granted by the High Court of Justice on 10 December 2011 under the insurance business transfer scheme in Part VII, S112 of the Financial Services and Markets Act 2000 (FSMA) all of the insurance business and cash and other investments of an aggregate value equal to the insurance business of Direct Line Insurance Limited were transferred to U K Insurance Limited Also on 10 December 2011 Direct Line Insurance Limited entered into a Surplus Asset Transfer Agreement with U K Insurance Limited to transfer their surplus assets and to discharge all their liabilities remaining after the Part VII transfer

U K Insurance Limited has assumed full responsibility for all of the administration and settlement of both current and any future claims arising in the insurance business transferred and will acquire all rights to future premiums of existing policies and the amounts held on the balance sheet for unearned premiums in relation to the policies transferred

Financial performance

The Company's financial performance is presented in the statement of comprehensive income on page 6

The comparative data in the statement of comprehensive income and accompanying notes include the business (reflected as discontinued operations') which was transferred using an insurance business transfer scheme under Part VII of the Financial Services Markets Act 2000 and via a Surplus Asset Transfer Agreement which was entered into between the company and U K Insurance Limited

No dividend has been paid in 2012 (2011 £1,104 0 million)

At the end of the year the balance sheet showed total assets of £100 (2011 £100)

Going concern

These financial statements have been prepared on a basis other than that of a going concern The basis of preparation is referred to further in note 1

SHARE CAPITAL

On 14 December 2011 the Company reduced the issued share capital from £155 million to a nominal amount of £100

DIRECTORS' REPORT (Continued)

DIRECTORS AND SECRETARY

The present directors and secretary who have served throughout the year except where noted below are listed on page 1

From 1 January 2012 to date the following changes have taken place

Directors	Appointed	Resigned
C P Sullivan		27 January 2012
I Falconer		23 February 2012
S K Howard		26 February 2012
J Hanson		4 July 2013
A Palmer		4 July 2013
P Geddes		20 August 2013
J Reizenstein		20 August 2013
C Morton	20 August 2013	
P Edwards	20 August 2013	
H Tomlinson	20 August 2013	

DIRECTORS' RESPONSIBILITIES STATEMENT

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 a directors' report and financial statements for each financial year and the directors have elected to prepare them in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union 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 at the end of the year and the profit or loss for the financial year as far as concerns members of the Company In preparing these financial statements under International Accounting Standard 1, the directors are required to

- select suitable accounting policies and then apply them consistently,
- present information, including accounting policies in a manner that provides relevant reliable, comparable and understandable information
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions other events and conditions of the entity's financial position and performance, and
- make an assessment of the Company's ability to continue as a going concern

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the directors' report and financial statements comply with the requirements of the Companies Act 2006 They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

DISCLOSURE OF INFORMATION TO AUDITOR

Each of the directors at the date of approval of this report confirms that

a) so far as they are aware there is no relevant audit information of which the Company's auditor is unaware, and
b) the directors have taken all the steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information

This confirmation is given and shall be interpreted in accordance with the provisions of section 418 of the Companies Act 2006

Deloitte LLP have expressed their willingness to continue in office as auditor

DIRECTORS' INDEMNITIES

Direct Line Insurance Group plc has made qualifying third party indemnity provisions for the benefit of its directors which were made during the year and remain in force at the date of this report

Approved by the Board of Directors and signed on behalf of the Board

Darrell Evans
Director
20 August 2013

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DIRECT LINE INSURANCE LIMITED

We have audited the financial statements of Direct Line Insurance Limited ("the Company") for the year ended 31 December 2012 which the Statement of Comprehensive Income, the Balance Sheet, the Cash Flow Statement the Statement of Changes in Equity and the related notes 1 to 19 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

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

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement, 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

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

In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 December 2012 and of its result for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

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

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DIRECT LINE INSURANCE LIMITED (Continued)

Emphasis of matter - Financial statements prepared other than on a going concern basis

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of the disclosure made in note 1 to the financial statements, which explains that the financial statements have been prepared on a basis other than that of a going concern

David Rush (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
20 August 2013

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2012

	Notes	2012 £ Million	2011 £ Million
Discontinued operations			
Insurance premium revenue	2	-	1,618 2
Insurance premium ceded to reinsurers	2	-	(37 4)
Net insurance premium revenue		-	**1,580 8**
Investment income	3	-	168 4
Net realised gains on financial assets	4	-	70 9
Net fair value loss on assets at fair value	5	-	(1 6)
Other operating income and expenses	6	-	14 9
Net income		-	**1,833 4**
Insurance claims and loss adjustment expenses	7	-	(1 200 0)
Insurance claims and loss adjustment expenses recovered from reinsurers	7	-	8 9
Net insurance claims		-	**(1,191 1)**
Commission refund	8	-	0 8
Expenses for marketing and administration	8	-	(343 3)
Expenses		-	**(342 5)**
Profit before tax		-	**299 8**
Tax charge	9	-	(81 4)
Profit for the year		-	**218 4**
Other comprehensive income			
Available-for-sale financial assets gain arising during the year	16	-	55 6
Less realised net gains on available-for-sale investments	16	-	(17 7)
		-	**37 9**
Tax charge on other comprehensive income	16	-	(10 0)
Other comprehensive income for the year		-	**27 9**
Total comprehensive income for the year		-	**246 3**

The total comprehensive income for the year was entirely attributable to equity shareholders of the Company and was derived from discontinued operations

The accompanying notes on pages 10 to 21 form an integral part of these financial statements

BALANCE SHEET
AS AT 31 DECEMBER 2012

	Notes	2012 £ Million	2011 £ Million
ASSETS			
Property, plant and equipment		-	-
Investment property		-	-
Insurance contracts			
Reinsurance assets		-	-
Deferred acquisition costs		-	-
Prepayments and accrued income		-	-
Financial investments		-	-
Loans and receivables		-	-
Current tax assets		-	-
Cash and cash equivalents		-	-
Total assets		-	-
EQUITY			
Share capital		-	-
Other reserves	16	-	-
Retained earnings	16	-	-
Total equity		-	-
LIABILITIES			
Insurance liabilities		-	-
Borrowings		-	-
Provisions for other liabilities and charges		-	-
Trade and other payables including insurance payables		-	-
Deferred tax liabilities		-	-
Total liabilities		-	-
Total equity and liabilities		-	-

The financial statements of Direct Line Insurance Limited, were approved by the Board of Directors on 20 August 2013 and signed on its behalf by

Darrell Evans
Director

The accompanying notes on pages 10 to 21 form an integral part of these financial statements

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2012

	Notes	Share capital £ Million	Other reserves £ Million	Retained earnings £ Million	Total £ Million
Balance as at 1 January 2011		**155 0**	**210 7**	**531 1**	**896 8**
Profit for the year		-	-	218 4	218 4
Other comprehensive income		-	27 9	-	27 9
Movement in claims equalisation reserves	16	-	9 4	(9 4)	-
Total comprehensive income		-	**37 3**	**209 0**	**246 3**
Share capital reduction		(155 0)	-	155 0	-
Release of capital contribution reserve	16	-	(160 0)	160 0	-
Release of claims equalisation reserve - business transfer	16	-	(48 9)	48 9	-
Release of available-for-sale reserve - business transfer	16	-	(53 2)	-	(53 2)
Release of available-for-sale deferred tax - business transfer	16	-	14 1	-	14 1
Dividends Paid during the year		-	-	(1 104 0)	(1,104 0)
At 31 December 2011		-	-	-	-
At 31 December 2012		-	-	-	-

The accompanying notes on pages 10 to 21 form an integral part of these financial statements

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2012

	Notes	2012 £ Million	2011 £ Million
Profit before tax		-	299 8
Adjustments for			
Investment revenues	3	-	(168 4)
Net fair value loss on assets at fair value through income	5	-	1 6
Profit on sale of available-for-sale equity investments	4	-	(3 7)
Profit on sale of available-for-sale debt securities	4	-	(67 2)
Interest received		-	169 0
Rental income received from investment properties		-	6 6
Dividends received from equity shares		-	5 9
Operating cash flows before movements in working capital		**-**	**243 6**
Movements in working capital			
Net increase in insurance net assets		-	(12 5)
Net decrease in reinsurance assets		-	36 1
Proceeds on disposal/maturity of available-for-sale equity investments		-	3 7
Proceeds on disposal/maturity of available-for-sale debt securities		-	2,189 3
Net decrease in investment balances held with credit institutions		-	30 0
Purchases of debt securities		-	(2,159 9)
Net increase in loans and receivables		-	(14 2)
Net decrease in other assets		-	39 6
Net decrease in related party balances		-	21 5
Net increase in other operating liabilities		-	(13 9)
Net cash inflow on transfer of business		-	152 6
Cash generated from operations		**-**	**515 9**
Taxes received		-	19 3
Net cash generated from operating activities		**-**	**535 2**
Cash flows from investing activities			
Proceeds on disposal of property, plant and equipment		-	0 2
Net cash generated from investing activities		**-**	**0 2**
Cash flow from financing activities			
Dividends paid		-	(1,104 0)
Net cash used by financing activities		**-**	**(1,104 0)**
Net decrease in cash and bank overdrafts		**-**	**(568 6)**
Cash and bank overdrafts at the beginning of the year		-	568 6
Cash and bank overdrafts at the end of the year		**-**	**-**

The Company classified the cash flows for the purchase and disposal of financial assets in its operating cash flows as the purchases were funded from the cash flows associated with the origination of insurance contracts, net of the cash flows from payment of insurance claims

The accompanying notes on pages 10 to 21 form an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

1 ACCOUNTING POLICIES

1 1 Presentation of accounts

The accounts have been prepared on an other than going concern basis (see page 2 of the Directors' Report) and in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board (IASB) and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB as adopted by the European Union (EU) (together IFRS)

The Company is incorporated in the United Kingdom and registered in England and Wales

The accounts were previously prepared on the historical cost basis except that available-for-sale financial assets and investment properties were stated at their fair value

The Company accounts are prepared in accordance with the Companies Act 2006

The Company had considerable financial resources and as a consequence, the directors believed the company was well placed to manage its business risks successfully despite the current uncertain economic climate As discussed in the Directors' Report the business was transferred to U K Insurance Limited The business is no longer considered a going concern and there is no material impact on either the 2012 or 2011 financial statements Accordingly the directors have not adopted the going concern basis in preparing the annual report and financial statements The Company has not traded in the year due to Part VII transfer as set out in the Activities and Business Review section of the Directors' Report on page 2

1 2 Foreign currencies

The Company's financial statements are presented in sterling which is the functional and presentation currency of the Company

Transactions in foreign currencies were translated into sterling at the foreign exchange rate ruling at the date of the transaction Monetary assets and liabilities denominated in foreign currencies were translated into sterling at the rates of exchange ruling at the balance sheet date Foreign exchange differences arising on translation were recognised in the income statement Non-monetary items denominated in foreign currencies that were stated at fair value were translated into sterling at foreign exchange rates ruling at the dates the values were determined

1 3 Insurance premium revenue

Insurance premiums comprised of the total premiums receivable for the whole period of cover provided by contracts incepted during the financial year adjusted by an unearned premium provision which represented the proportion of the premiums that related to periods of risk after the balance sheet date Unearned premiums were calculated on the basis of the estimated risk profile of the business written Insurance premiums exclude insurance premium tax

Estimates were included for premium not yet notified by the year end Insurance premiums were stated gross of commissions and exclusive of taxes and duties levied on premiums

1 4 Insurance claims and loss adjustment expenses

Insurance claims were recognised in the accounting period in which the loss occurred Provision was made for the full cost of settling outstanding claims at the balance sheet date including claims incurred but not yet reported at that date net of salvage and subrogation recoveries Outstanding claims provisions were not discounted for the time value of money except for claims to be settled by periodical payments orders (PPOs) established under the Courts Act 2003 A UK Court can award damages for future pecuniary loss in respect of personal injury or for other damages in respect of personal injury and may order that the damages are wholly or partly to take the form of PPOs

1 5 Claims equalisation

A statutory claims equalisation reserve was included as a non-distributable reserve within Other Reserves in Equity This reserve was calculated in accordance with chapter 1 4 of the Prudential Sourcebook for Insurers (INS PRU)

1 6 Reinsurance

The Company ceded reinsurance in the normal course of business with retention limits varying by line of business Outwards reinsurance premiums were accounted for in the same accounting period as the premiums for the related direct business being reinsured Outward reinsurance recoveries were accounted for in the same accounting period as the direct claims to which they relate

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

1 ACCOUNTING POLICIES (Continued)

1 6 Reinsurance (Continued)

Reinsurance assets included balances due from reinsurance companies for ceded insurance liabilities Amounts that were recoverable from reinsurers estimated in a consistent manner with the outstanding claims provisions or settled claims associated with the reinsured policies and in accordance with the relevant reinsurance contract Recoveries in respect of periodical payment orders were discounted for the time value of money A reinsurance bad debt provision was assessed in respect of outstanding reinsurance claims to reflect the credit risk exposure to long-term reinsurance assets particularly in relation to Periodic Payment Orders

Where there was evidence to indicate that the reinsurance asset may not have been collected or where the reinsurer's credit rating had been downgraded significantly, the Company reduced the carrying value of the asset accordingly and the impairment loss was recognised in the statement of comprehensive statement

1 7 Deferred acquisition costs

Acquisition costs relating to new and renewing insurance policies were matched with the earning of the premiums to which they related

The principal acquisition costs so deferred were direct advertising expenditure and costs associated with telesales and underwriting staff

1 8 Revenue recognition

Interest income on financial assets that were classified as loans and receivables available-for-sale and interest expense on financial liabilities other than those at fair value through profit or loss were determined using the effective interest method The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or liabilities) and of allocating the interest income or interest expense over the expected life of the asset or liability The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount Calculation of the effective interest rate takes into account fees payable or receivable that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs All contractual terms of a financial instrument were considered when estimating future cash flows

Investment property - Rental income from investment property was recognised on a straight-line basis over the term of the lease Lease incentives granted were recognised as an integral part of the total rental income Any gain or loss arising from a change in fair value was recognised in the statement of comprehensive statement

1 9 Taxation

Provision was made for taxation at current enacted rates on taxable profits arising in income or in equity, taking into account relief for overseas taxation where appropriate

Deferred taxation was accounted for in full for all temporary differences between the carrying amount of an asset or liability for accounting purposes and its carrying amount for tax purposes except in relation to overseas earnings where remittance was controlled by the Group, and goodwill

Deferred tax assets were only recognised to the extent that it is probable that they will be recovered

1 10 Investment property

Investment property comprised freehold and long leasehold properties that were held to earn rentals or for capital appreciation or both It was not depreciated and was stated at fair value based on valuations by independent registered valuers Fair value was based on current prices in an active market for similar properties in the same location and condition Any gain or loss arising from a change in fair value was recognised in the statement of comprehensive statement

1 11 Property, plant and equipment

Items of property plant and equipment (except investment property - see accounting policy 1 10) were stated at historical cost less accumulated depreciation (see below) and impairment losses Where an item of property plant and equipment comprised major components having different useful lives, they were accounted for separately
Depreciation was charged to the statement of comprehensive statement on a straight-line basis so as to write off the depreciable amount of property plant and equipment (including assets owned and let on operating leases) over their estimated useful lives The depreciable amount was the cost of an asset less its residual value Land was not depreciated Estimated useful life was as follows

Freehold and long leasehold buildings	50 years or the period of the lease if shorter

The gain or loss arising from the derecognition of an item of property plant and equipment was determined as the difference between the disposal proceeds if any and the carrying amount of the item

1 ACCOUNTING POLICIES (Continued)

1 12 Impairment of property, plant and equipment

At each reporting date the company would assess whether there was any indication that its property plant and equipment were impaired If any such indication existed, the company estimated the recoverable amount of the asset and the impairment loss if any The recoverable amount of an asset was the higher of its fair value less costs to sell and its value in use Value in use was the present value of future cash flows from the asset discounted at a rate that reflects market interest rates adjusted for risks specific to the asset that have not been reflected in the estimation of future cash flows

If the recoverable amount of an intangible or tangible asset was less than its carrying value, an impairment loss would have been recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss

Where an impairment loss subsequently reversed the carrying amount of the asset was increased to the revised estimate of its recoverable amount but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised as income immediately unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss was treated as a revaluation increase

1 13 Financial assets

On initial recognition financial assets were classified into available-for-sale financial assets or loans and receivables

Loans and receivables – Non-derivative financial assets with fixed or determinable repayments that were not quoted in an active market were classified as loans and receivables except those that were classified as available-for-sale Loans and receivables were initially recognised at fair value plus directly related transaction costs They were subsequently measured at amortised cost using the effective interest method (see accounting policy 1 8) less any impairment losses

Insurance receivables comprised outstanding insurance premiums where the policyholders had elected to pay in instalments or amounts due from third parties where they had collected the money from the policyholder

Available-for-sale – Financial assets that were not classified as loans and receivables were classified as available-for-sale Financial assets can be designated as available-for-sale on initial recognition Available-for-sale financial assets were initially recognised at fair value plus directly related transaction costs They were subsequently measured at fair value Impairment losses and exchange differences resulting from retranslating the amortised cost of foreign currency monetary available-for-sale financial assets were recognised in profit or loss together with interest calculated using the effective interest method (see accounting policy 1 8) Other changes in the fair value of available-for-sale financial assets were reported in a separate component of shareholders' equity until disposal when the cumulative gain or loss was recognised in profit or loss

A financial asset was regarded as quoted in an active market if quoted prices were readily and regularly available from an exchange dealer broker industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis The appropriate quoted market price for an asset held was usually the current bid price When current bid prices were unavailable the price of the most recent transaction provides evidence of the current fair value as long as there has not been a significant change in economic circumstances since the time of the transaction If conditions have changed since the time of the transaction (e g a change in the risk-free interest rate following the most recent price quote for a corporate bond) the fair value reflects the change in conditions by reference to current prices or rates for similar financial instruments, as appropriate

The valuation methodology described above uses observable market data

If the market for a financial asset was not active the Company establishes fair value by using a valuation technique Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties if available reference to the current fair value of another instrument that was substantially the same discounted cash flow analysis and option pricing models If there is a valuation technique commonly used by market participants to price the instrument and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions the Company used that technique

The fair value of investments in equity instruments that did not have a quoted market price in an active market and derivatives that were linked to and must be settled by delivery of such an unquoted equity instrument is reliably measurable if

(a) the variability in the range of reasonable fair value estimates was not significant for that instrument or
(b) the probabilities of the various estimates within the range could be reasonably assessed and used in estimating fair value

ACCOUNTING POLICIES (Continued)

Available-for sale – (Continued)

1 14 Impairment of financial assets

The company assessed at each balance sheet date whether there was any objective evidence that a financial asset or group of financial assets classified as available-for-sale or loans and receivables was impaired A financial asset or portfolio of financial assets was impaired and an impairment loss incurred if there was objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset

Available-for-sale – When a decline in the fair value of a financial asset classified as available-for-sale had been recognised directly in equity and there was objective evidence that the asset was impaired the cumulative loss was removed from equity and recognised in profit or loss The loss was measured as the difference between the amortised cost of the financial asset and its current fair value Impairment losses on available-for-sale equity instruments were not reversed through profit or loss but those on available-for-sale debt instruments were reversed if there was an increase in fair value that was objectively related to a subsequent event

Loans and receivables – If there was objective evidence that an impairment loss on a financial asset or group of financial assets classified as loans and receivables had been incurred the company measured the amount of the loss as the difference between the carrying amount of the asset or group of assets and the present value of estimated future cashflows from the asset or group of assets discounted at the effective interest rate of the instrument at initial recognition

Impairment losses were assessed individually where significant or collectively for assets that were not individually significant

Impairment losses were recognised in profit or loss and the carrying amount of the financial asset or group of financial assets was reduced by establishing an allowance for the impairment losses If in a subsequent period the amount of the impairment loss reduces and the reduction can be ascribed to an event after the impairment was recognised the previously recognised loss was reversed by adjusting the allowance

For debts due from policyholders the bad debt provision was calculated based upon prior loss experience For all balances outstanding in excess of three months a provision of 75% was made Where a policy was subsequently cancelled, the outstanding debt that was overdue was written off to profit or loss and the provision was written back to profit or loss

1 15 Financial liabilities

On initial recognition financial liabilities were classified into held-for-trading designated as at fair value through profit or loss or amortised cost

Amortised cost

Other than derivatives which were recognised and measured at fair value, all other financial liabilities were measured at amortised cost using the effective interest method (see accounting policy 1 8)

1 16 Derecognition

A financial asset was derecognised when it had been transferred and the transfer qualified for derecognition

1 17 Portfolio transfer

The charges associated with making portfolio claims' transfers from the Company were included as part of claims incurred Outstanding claims' liabilities covered by the portfolio transfer, are transferred off the balance sheet as at the date of transfer

Portfolio premiums payable are reflected as premiums for reinsurance and are included within net insurance premium revenue Unearned premium reserves in respect of premium covered by the portfolio transfer are transferred off the balance sheet as at the date of the transfer

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

2 NET INSURANCE PREMIUM REVENUE

Discontinued operations	2012 £ Million	2011 £ Million
Premium income from insurance contracts issued		
Premium receivables	-	1 635 7
Change in unearned premium provision	-	(17 5)
Transfer of business - portfolio premiums paid	-	(837 2)
Transfer of business - transfer of unearned premium off balance sheet	-	837 2
	-	1 618 2
Premium revenue ceded to reinsurers on insurance contracts issued		
Premium payables	-	(43 2)
Change in unearned premium provision	-	5 8
Transfer of business - portfolio premium income	-	23 6
Transfer of business - transfer of unearned premium off balance sheet	-	(23 6)
	-	(37 4)
Net insurance premium revenue	-	1 580 8

3 INVESTMENT INCOME

	2012 £ Million	2011 £ Million
Available-for-sale financial assets		
Dividends from equity shares	-	5 9
Interest income from debt securities	-	81 4
Interest income		
from policyholders	-	87 0
from loans to related parties (note 19)	-	0 2
from deposits with credit institutions	-	5 2
Net discount of premium on purchase of financial assets	-	(19 4)
Rental income from investment property	-	6 6
Income from other investments	-	1 5
	-	168 4

4 NET REALISED GAINS ON FINANCIAL ASSETS

	2012 £ Million	2011 £ Million
Net realised gains on financial assets - available-for-sale (note 16)		
Equity shares		
Release of available-for-sale reserve to comprehensive income	-	3 7
Debt securities	-	17 7
Release of available-for-sale reserve to comprehensive income	-	49 5
	-	70 9

5 NET FAIR VALUE LOSS ON ASSETS AT FAIR VALUE

	2012 £ Million	2011 £ Million
Net fair value loss on investment property (note 12)	-	(1 6)

Fair value losses in the prior year have arisen from the revaluation of financial assets at fair value through profit or loss property and the revaluation of non-hedged derivatives

6 OTHER OPERATING INCOME AND EXPENSES

	2012 £ Million	2011 £ Million
Other income	-	14 9

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

7 INSURANCE CLAIMS AND LOSS ADJUSTMENT EXPENSES

	2012		
	Gross £ Million	Reinsurance £ Million	Net £ Million
Current accident year claims paid	-	-	-
Prior accident years' claims paid	-	-	-
Movement in current accident year claims provision	-	-	-
Movement in prior accident years claims provision	-	-	-
	-	-	-

	2011		
	Gross £ Million	Reinsurance £ Million	Net £ Million
Current accident year claims paid	524 3	-	524 3
Prior accident years claims paid	673 5	(45 0)	628 5
Movement in current accident year claims provision	748 1	(9 7)	738 4
Movement in prior accident years' claims provision	(745 9)	45 8	(700 1)
Transfer of business - portfolio claims paid	(2 358 8)	174 7	(2 184 1)
Transfer of business - claims liability	2 358 8	(174 7)	2 184 1
	1 200 0	**(8 9)**	**1 191 1**

Loss adjustment expenses for the year of £nil (2011 £112 5 million) have been included in the accident year claims figures above

8 EXPENSES

	2012 £ Million	2011 £ Million
a) Commission expenses		
Cost incurred for the acquisition of insurance contracts expensed in the year	-	11 2
Deferred acquisition costs	-	(12 0)
	-	**(0 8)**
b) Expenses for marketing and administration		
Marketing and administration expenses	-	**343 3**

9 TAX CHARGE

	2012 £ Million	2011 £ Million
Current taxation		
Charge for the year	-	90 4
Under provision in respect of prior periods	-	1 5
	-	91 9
Deferred taxation (note 14)		
Credit for the year	-	(10 5)
	-	(10 5)
Income tax charge for the year	-	**81 4**
Current tax	-	91 9
Deferred taxation (note 14)	-	(10 5)
Income tax charge for the year	-	**81 4**

The actual income tax charge differs from the expected income tax charge computed by applying the standard rate of UK corporation tax of 24 5% (2011 26 5%) as follows

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

9 TAX CHARGE (Continued)

	2012 £ Million	2011 £ Million
Expected income tax charge	-	79 4
Effects of		
Non-taxable items	-	0 6
Effect of the reduction in deferred tax rate to 23% (2011 25%)	-	(0 1)
Adjustments in respect of prior periods	-	1 5
Income tax charge	-	**81 4**

The aggregate current and deferred tax relating to items that were charged to equity is £nil (2011 £(4 3) million)

10 AUDITOR'S REMUNERATION

Fees for audit and non-audit services included within marketing and administration expenses were borne and recharged by a related party DL Insurance Services Limited

Fees paid to the auditors with respect to the statutory audit of the Company amount to £nil in 2012 (2011 £252 076)

Directors emoluments

	2012 £ Million	2011 £ Million
Other emoluments	-	1 5
Company pension contributions	-	0 1
	-	1 6

Fees paid to directors during the year amounted to £nil (2011 £24 525)

The directors of the Company are executives of the Group No directors who served during this or the previous financial year were remunerated by the Company All directors receive remuneration from DLIS as employees of that company and due to the non-executive nature of their services it is not appropriate to allocate their emoluments in respect of the Company

Emoluments excluding pension contributions paid to the highest paid directors amounted to £nil (2011 £588 205)

A contribution of £nil (2011 £10 859) to a money purchase scheme was made on behalf of the highest paid director Two directors (2011 Four directors) had retirement benefits accruing under defined pension schemes in respect of qualifying service One director (2011 Two directors) had benefits accruing under defined benefit pension schemes

During the year no directors exercised share options (2011 no directors)

11 PROPERTY, PLANT AND EQUIPMENT

	Land and buildings £ Million
Cost	
At 1 January 2011	0 2
Disposals	(0 2)
At 31 December 2011	-
At 31 December 2012	-
Net book value	
At 31 December 2011	-
At 31 December 2012	-

Depreciation charged during 2012 amounted to £nil (2011 £495)

The disposal related to a sale of property on 4 February 2011

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

12 INVESTMENT PROPERTY

	2012 £ Million	2011 £ Million
At 1 January	-	83 5
Change in fair value	-	(1 6)
Transfer of business	-	(81 9)
At 31 December 2011	-	-
At 31 December 2012	-	-

Investment property comprised of freehold property occupied by entities within The Royal Bank of Scotland Group on an operating lease A valuation was carried out at 10 December 2011 by CB Richard Ellis and this resulted in a decrease in the value of the property by £1 6 million CB Richard Ellis is a member of the Royal Institution of Chartered Surveyors and has appropriate qualifications and recent experience in the valuation of properties in the relevant location The decrease was debited to the income statement (note 5)

13 DEFERRED ACQUISITION COSTS

	2012 £ Million	2011 £ Million
At 1 January	-	59 8
Net credit to income statement	-	12 0
Transfer of business	-	(71 8)
At 31 December 2011	-	-
At 31 December 2012	-	-

14 DEFERRED TAXATION

The following were the deferred tax assets and liabilities recognised by the Company and the movements thereon during the current and prior reporting years

	Equalisation reserves £ Million	Fair value on financial assets £ Million	Total £ Million
At 1 January 2011	10 5	-	**10 5**
Credit to income statement	(10 5)	-	**(10 5)**
At 31 December 2011	-	-	-
At 31 December 2012	-	-	-

15 SHARE CAPITAL

	2012 £	2011 £
Issued and fully paid		
Equity shares		
100 ordinary shares of £1 each		
At 31 December 2011	**100 0**	**100 0**

On 14 December 2011 the issued share capital of the company was reduced from £155 million to £100

16 OTHER RESERVES AND RETAINED EARNINGS

The company received a capital injection of £160 million from its parent company Direct Line Group Limited in July 2010 The Capital contribution reserve was reduced to £nil in 2011

Movements in the revaluation reserve for available-for-sale investments were as follows

	Equity shares see note 1 1) £ Million	Debt securities see note 1 1) £ Million	Total £ Million
At 1 January 2011	**(2 1)**	**13 3**	**11 2**
Revaluation during the period - gross	6 6	49 0	**55 6**
Revaluation during the period - taxation	(1 8)	(12 9)	**(14 7)**
Net (gains) transferred to net profit on disposal and impairment - gross (note 4)	-	(17 7)	**(17 7)**
Net gains transferred to net profit on disposal and impairment - taxation	-	4 7	**4 7**
Release of available-for-sale reserve as a result of transfer of business	(3 7)	(49 5)	**(53 2)**
Release of available-for-sale deferred tax as a result of transfer of business	1 0	13 1	**14 1**
At 31 December 2011	-	-	-
At 31 December 2012	-	-	-

Movements in the claims equalisation reserve were as follows

	£ Million
At 1 January 2011	39 5
Transfer to retained earnings for movement in year	9 4
Release of claims equalisation reserves following transfer of business	(48 9)
At 31 December 2011	-
At 31 December 2012	-

17 INSURANCE LIABILITIES AND REINSURANCE ASSETS

Movements in insurance liabilities and reinsurance assets

(i) Claims and loss adjustment expenses

	Gross £ Million	Reinsurance £ Million	Net £ Million
Notified claims	1 414 0	(116 8)	1 297 2
Incurred but not reported	942 6	(94 0)	848 6
At 1 January 2011	**2 356 6**	**(210 8)**	**2,145 8**
Cash paid for claims settled in the year			
Current year	(524 3)	-	(524 3)
Prior year	(673 5)	45 0	(628 5)
Increase/(decrease) in liabilities			
- arising from current year claims	1 272 4	(9 7)	1 262 7
- arising from prior year claims	(72 4)	0 8	(71 6)
Transfer of business - claims liability	(2,358 8)	174 7	(2 184 1)
At 31 December 2011	-	-	-
There were no movements in insurance liabilities in the year			
At 31 December 2012	-	-	-
Notified claims	-	-	-
Incurred but not reported	-	-	-
At 31 December 2012	-	-	-

(ii) Provisions for unearned premiums

	Gross £ Million	Reinsurance £ Million	Net £ Million
Unearned premium provision			
At 1 January 2011	819 7	(17 7)	802 0
Net increase in the year	17 5	(5 9)	11 6
Transfer of business - unearned premium	(837 2)	23 6	(813 6)
At 31 December 2011	-	-	-
There were no movements in insurance liabilities in the year			
At 31 December 2012	-	-	-

18 PROVISIONS FOR OTHER LIABILITIES AND CHARGES

	Regulatory levies £ Million
At 1 January 2011	29 7
Charged to the statement of comprehensive income	
- additional provisions	23 5
Exchange differences	
Used during year	(27 8)
Transfer of business	(25 4)
At 31 December 2011	-
There were no movements in provisions for other liabilities and charges in the year	
At 31 December 2012	-

19 RELATED PARTIES

On 1 December 2008 the UK Government through HM Treasury became the ultimate controlling party of The Royal Bank of Scotland Group plc The UK Government's shareholding is managed by UK Financial Investments Limited a company wholly owned by the UK Government As a result the UK Government and UK Government controlled bodies became related parties of the Company

At 31 December 2012, Direct Line Insurance Limited ultimate holding company was The Royal Bank of Scotland Group plc which is incorporated in the United Kingdom and registered in Scotland On 13th March 2013, the ultimate holding company ceased to be The Royal Bank of Scotland Group plc and became Direct Line Insurance Group plc, which is also the immediate parent company and is incorporated in the United Kingdom and registered in England and Wales

The following transactions were carried out with other Group companies in the period 1 January to 31 December 2012 and are transacted on an arm's length basis

i Sales of insurance contracts and other services

	2012 £ Million	2011 £ Million
Sales of services		
Fellow subsidaries	-	0 2

	2012 £ Million	2011 £ Million
Interest received (note 3)		
Fellow subsidaries	-	0 2

Sales of services were provided between related parties on an arm s length basis

Interest income received from deposits held with related parties were at rates ranging from nil in 2012 (2011 0 40% to 0 77%)

ii Purchases of products and services and other purchases

	2012 £ Million	2011 £ Million
Purchase of services		
Fellow subsidaries	-	488 4

Purchases of services also includes payments made between companies determined by the level of business generated and as agreed between the parties on an arm's length basis

All employees were employed by DL Insurance Services Limited a fellow subsidiary company Total employee costs including directors' remuneration, recharged to the Company by DL Insurance Services Limited during the year were £nil (2011 £185 7 million)

Employee costs recharged by DL Insurance Services Limited included the full costs of key managers and other staff in respect of share-based payments The attribution among members of the RBS Group has regard to the needs of the Group as a whole

iii Compensation of key management

The aggregate remuneration of directors and other members of key management during the year was as follows

	2012 £ Million	2011 £ Million
Other emoluments	-	2 8
Company pension contributions	-	0 3
	-	3 1

Fees paid to directors during the year amounted to £nil (2011 £38,245)

19 RELATED PARTIES (Continued)

iv Year-end balances arising from sales/purchases of products/services

Receivables from related parties

Movements in receivables from related parties were as follows	2012 £ Million	2011 £ Million
At 1 January 2011	-	7 9
Transactions in the year	-	0 2
Settled in the year	-	(8 4)
Transferred as part of business transfer	-	0 3
At 31 December 2011	-	-
At 31 December 2012	-	-

Movements in receivables from Headrow Reinsurance Limited	2012 £ Million	2011 £ Million
At 1 January 2011	-	2 0
Transactions in the year	-	(2 0)
At 31 December 2011	-	-
At 31 December 2012	-	-

v Due to related parties

Movements due to related parties were as follows	2012 £ Million	2011 £ Million
At 1 January 2011	-	39 5
Transactions in the year	-	488 4
Settled in the year	-	(450 7)
Transferred as part of business transfer	-	(77 2)
At 31 December 2011	-	-
At 31 December 2012	-	-

vi Loans to related parties

Movements in loans to related parties were as follows	2012 £ Million	2011 £ Million
At 1 January 2011	-	15 6
Loans advanced during year	-	102 3
Loan repayments received	-	(78 2)
Interest received (note 3)	-	0 2
Transferred as part of business transfer	-	(39 9)
At 31 December 2011	-	-
At 31 December 2012	-	-

vii Reinsurance assets

Movements in reinsurance assets were as follows	2012 £ Million	2011 £ Million
At 1 January 2011	-	19 8
Movement in claims provision	-	(19 8)
At 31 December 2011	-	-
At 31 December 2012	-	-