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Financial summary

(Results from continuing operations)

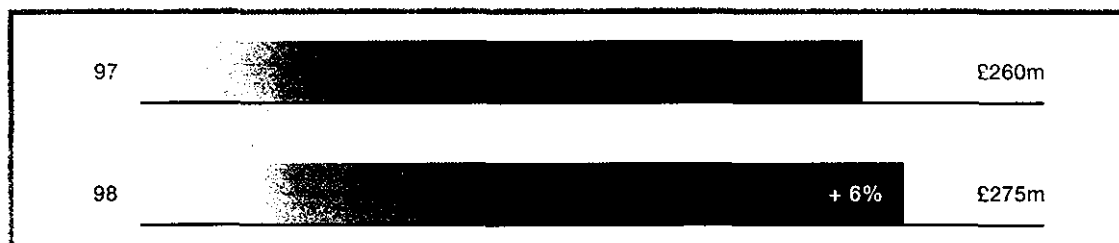


New business premiums*	£275 million	+6%
Total premium income**	£1,970 million	+10%
Funds under management	£20.8 billion	+12%
Pre-tax operating profit	£160 million	+27%

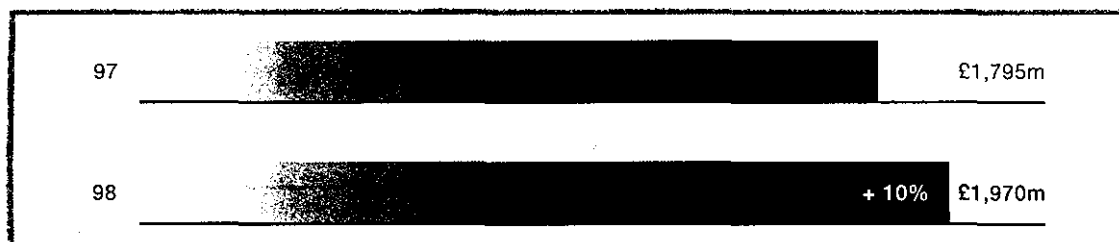
*New business premiums comprise new regular premiums and 10% of new single premiums and collective investment scheme sales.

**Total premium income includes sales of collective investment schemes.

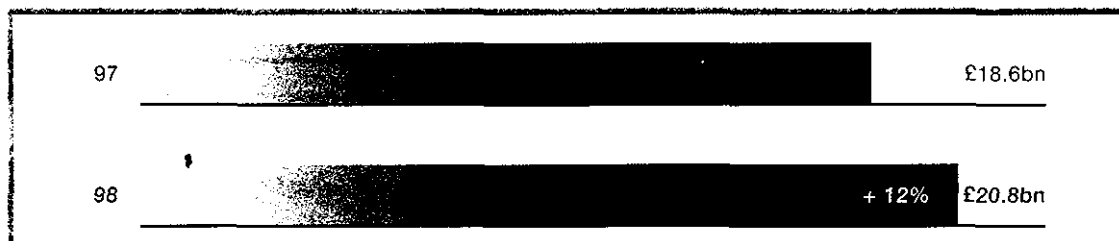
New business premiums* £m 1997 - 1998



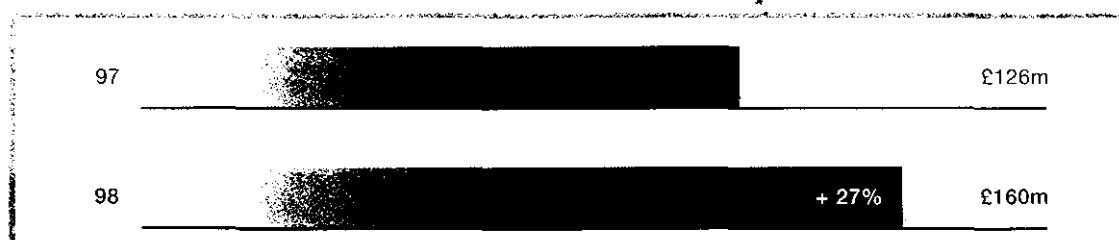
Total premium income** £m 1997 - 1998



Funds under management £bn 1997 - 1998



Pre-tax operating profit £m 1997 - 1998



Chairman's statement



"Allied Dunbar has made excellent progress in 1998."

Sandy Leitch Chairman

Allied Dunbar has made excellent progress in 1998, with good growth in new business, funds under management and operating profit.

On 7 September, the merger of B.A.T Industries' financial services business, including Allied Dunbar, with the Zurich Insurance Company was completed. The new group, Zurich Financial Services, is listed on the UK stock exchange through Allied Zurich p.l.c. and is also listed in Switzerland through Zurich Allied AG. Zurich Financial Services is one of the world's largest financial services groups with over 30 million customers in over 60 countries. Allied Dunbar is a leading member of Zurich Financial Services' UK, Ireland and South Africa region (UKISA) that, in the UK, also includes Eagle Star Insurance, Zurich Insurance Company UK, Eagle Star Life, Zurich Life and Sterling Assurance.

The merger provides us with the opportunity to invest in further profitable growth. In January 1999, we relaunched the Allied Dunbar Sales Force as the Allied Dunbar Franchise Network. The heart of the Franchise Network is a 'business to business' relationship between Advisers and Allied Dunbar. We are continuing to build this relationship by increasing our investment in the Franchise Network to drive Adviser productivity and earnings even higher. In addition, UKISA announced the creation of the Zurich IFA Group in September. This is a new marketing and services company totally dedicated to the IFA, which will provide Allied Dunbar with access to many more segments of the IFA market.

During 1998, I was delighted to be able to appoint Brian Thomas as Finance Director for the UKISA

region. As a result of his new appointment, Brian resigned from the board of Allied Dunbar in August. Shayne Deighton replaces Brian as Finance Director of Allied Dunbar. Shayne brings a wealth of experience, gained as a principal with a leading firm of consulting actuaries.

In October, Phil Smith stepped down as Chief Executive of the UK Life businesses and as a director of Allied Dunbar, to devote more time to his charitable interests. Phil's contribution to the development and success of Allied Dunbar over 26 years has been immense and I wish him and his family every happiness for the future. I would also like to thank Keith Davies, who retired at the end of 1998 and Paul Manduca, who resigned as director in February 1999, for their contribution to the company over many years.

In Keith Baldwin, promoted to Chief Executive, and Phil Hodgkinson, who assumes the new role of Managing Director, Allied Dunbar has one of the most powerful leadership teams in the industry.

Distribution is the key competitive factor in today's Life and Investment market. The continued strength of Allied Dunbar's Franchise Network and our growth in the IFA market demonstrate that our strategy is the right one. In addition, our people have the necessary skills and determination to succeed in this highly competitive market.

Sandy Leitch

Sandy Leitch Chairman
20 April 1999

Annual review



"There can be no arguments, Allied Dunbar is the 'Franchise of Choice'."

Keith Baldwin Chief Executive

The Allied Dunbar Franchise has continued to produce outstanding results. Following a record-breaking year in 1997, 1998's performance was even better. New business premiums and individual Adviser productivity again hit all-time highs.

But surpassing even this, Allied Dunbar's Franchise was voted The Most Admired Large Direct Sales Force in the Industry, for the third consecutive year. Once was an achievement, twice was outstanding, three times and there can be no arguments, Allied Dunbar is the 'Franchise of Choice'.

The 'franchise of choice'

During 1998, a record number of industry professionals joined the Allied Dunbar Franchise. Over 600 new industry professionals joined, up 32 per cent on last year, helping grow the total franchise membership to 3,665. Adviser productivity continued to increase and new business from the Franchise for Allied Dunbar was up 5 per cent at £224 million. Total new business generated for UKISA by the Franchise was also up 5 per cent.

We continued to make improvements to the sales process aimed at making further increases in Adviser productivity. In April, we launched a new simplified client fact find. This enables Advisers to collect key information about their clients' financial affairs effectively and efficiently. We also introduced new application forms aimed at streamlining the application process. The new fact find and application

forms allow us to move further towards the introduction of a full electronic point of sale system.

1998 saw Dunbar Independent's first full year of operation. Dunbar Independent is an important addition to our overall offering to clients. It provides an in-house IFA service for clients whose needs cannot be satisfied fully by the Allied Dunbar product range alone.

We introduced a new focus on 'Professional Advice' in our television advertising campaign, to further emphasise Allied Dunbar's strategy of providing guaranteed face-to-face professional advice. We also continued our sponsorship of English professional rugby. Our first season of sponsorship has proved highly beneficial for both English rugby and Allied Dunbar. Through local and national marketing events it has provided us with valuable opportunities to reach new groups of potential clients.

Products and services

Allied Dunbar reinforced its position as the leading provider of personal life protection products with new business premiums up 11 per cent, at £93 million.

New Personal Pensions were up 1 per cent, new Pension Annuities were up 19 per cent and Pension Income Withdrawal Plans were 55 per cent higher.

However, overall Pensions business was down, reflecting delays in receipt of government rebates on personal pension plans.

Investment business was 19 per cent higher reflecting excellent growth in Distribution and International Bonds.

Allied Dunbar's Life and Pensions funds continued to demonstrate good investment performance under the management of Threadneedle Asset Management.

On 1 May the Government's new mortgage code came into effect. We welcomed this initiative. However, we are concerned that the new code does not yet go far enough in protecting consumers from poor advice. In particular, the new register of intermediaries makes no checks to ensure intermediaries are fit, proper and competent.

Allied Dunbar's Franchise is the UK's largest introducer of business to mortgage lenders. To ensure we provide consumers with genuine protection, we have introduced the new Allied Dunbar Mortgage Application Service (ADMAS). ADMAS is a service that goes beyond the mortgage sale. It provides consumers with professional advice on the Allied Dunbar products which clients can use to repay and protect residential mortgages, together with the facility to introduce clients to residential mortgage lending sources. The consumer benefits by receiving guaranteed advice from a trained and competent adviser who will provide documentation to support the advice given.

The Bank of Scotland and the Halifax joined our list of 'premier lenders' in January and, together with Alliance & Leicester, provided a range of exclusive mortgage offers. Total mortgage completions by our panel lenders in 1998, through our introduction service, exceeded £1.8 billion.

Dunbar Bank continued to enhance its reputation as a specialist lender in the commercial property market. Its loan book grew by 14 per cent and pre-tax profits increased by 25 per cent to £16 million.

The future

The UK financial services industry has changed enormously in recent years, but the future holds the prospect of yet more change. The government seems set to review the current system of polarisation amongst distributors. The reduction in state benefits also seems set to continue. As a result, the overall market for financial services will continue to grow. This provides Allied Dunbar with an opportunity to press home its advantage of providing guaranteed face-to-face professional advice and I expect to see continued growth in Adviser productivity and profitability. To support our plans for growth we will be investing further to build the Allied Dunbar Franchise Network, the most profitable financial services franchise in the UK.



Keith Baldwin Chief Executive

20 April 1999

Annual review



"Allied Dunbar delivered a strong financial performance in 1998."

Phil Hodgkinson Managing Director

Allied Dunbar delivered a strong financial performance in 1998, against a background of further rationalisation within the financial services industry. This was an even more creditable performance given the distractions of the merger with Zurich. New business again reached record levels, up 6 per cent at £275 million. Funds under management grew by 12 per cent to £20.8 billion, with total premium income at £1,970 million.

New business from the Allied Dunbar Franchise Network was up 5 per cent, while IFA new business increased by 11 per cent to a new high of £48 million. New regular premiums grew by 4 per cent, while new single premiums were up 11 per cent.

Operating profit from continuing operations, at £160 million was after an increase of £35 million in the provisions for the Financial Services Authority (FSA) review of pension transfers and opt-outs.

Pensions review

During 1998 the FSA set the industry challenging targets for completing Phase 1 of the review. We met the targets set for Allied Dunbar by achieving accepted offers of redress on all relevant priority one redressable cases.

In August, the FSA issued guidance on Phase 2 of the review. This requires us to write to certain classes of clients, not contacted in Phase 1, and invite them to

request a review of their case. These mailings are coupled with a high profile government television advertising campaign. In November and December, the FSA issued further guidance on Phase 2, which included a requirement for pension providers to rework some cases completed as part of Phase 1. As a result of this clarification from the FSA on Phase 2 and further experience from Phase 1, we have reviewed our provisions for redress and the expenses of performing the review and increased these by £35 million.

Business developments

During 1998, we have worked with the other UKISA Life businesses in the UK to formulate an integrated common processing strategy. Within this strategy Allied Dunbar is continuing its programme to redesign radically our point-of-sale, policy set-up, client servicing and claim processes. However, this is now being pursued within a framework that will seek to identify opportunities to re-use and consolidate system developments across the UKISA Life business as a whole. This will help deliver consistency of technology infrastructure, reduced costs and flexibility.

Following a successful pilot of our new claims and maturities process in 1997, this service was launched to senior members of the Franchise during 1998. This service allows clients to invest the proceeds from Allied Dunbar and other policy maturities and

claims directly into a special deposit account operated by Dunbar Bank. Clients are able to earn a competitive rate of interest on their funds while deciding how to reinvest or otherwise use their policy proceeds.

Our Client Service Centre has been expanded during 1998 and a further investment in technology has been made. This represents the next step towards enabling Advisers to use the service centre as if it were an extension of their own office.

Year 2000 compliance

Allied Dunbar's programme to ensure that the Year 2000 date change does not disrupt our operations started in early 1996. During 1998, the programme has continued in line with our expectations. The programme is based on a detailed risk assessment that includes such areas as health and safety, continuity of supplied services and contingency planning as well as our individual computer systems. The overall cost of the programme is expected to be £7 million, incurred over 4 years.

Community involvement

During 1998, Allied Dunbar paid £1.7 million under a deed of covenant to the Zurich Financial Services (UKISA) Community Trust (formerly the British American Financial Services Community Trust). Most of these funds were earmarked for the Trust's major programmes on dementia and domestic violence and the ongoing programme in India. The India programme alone has provided over £200,000 in grants and 23 senior staff assignments since its launch in 1996.

In January 1998, the Allied Dunbar Foundation, which is funded and managed by members of the Allied Dunbar Franchise, launched a new theme, 'On the Road', concerned with mobility and accessibility. Under this theme, funds raised by members of the Allied Dunbar Franchise exceeded £1 million for the first time, a superb achievement.

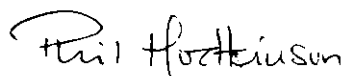
The Staff Charity Fund made grants of over £300,000 to charities in the Swindon area and more than 850 staff took up volunteering opportunities. This included a record number of volunteers for the 1998 Challenge event, which focused on projects helping disadvantaged children.

The ASPIRE National Training Centre, for which the Foundation and Allied Dunbar jointly provided over £2 million, was officially opened by HRH Duke of York in September. A new 'Seeing is Believing' programme was launched during 1998 to provide opportunities for directors and senior managers to visit community projects in the Swindon area to explore the social and personal impact of our community involvement activity.

People

Allied Dunbar's success is built on its people and I'd like to thank all our people for their continued commitment and enthusiasm during a year that presented many challenges and distractions.

As we look towards the start of the new millennium, I believe we have the people with the professionalism and qualities to continue Allied Dunbar's extraordinary success.



Phil Hodkinson Managing Director
20 April 1999

In the event of an existing employee becoming disabled, it is the policy of the Group to make every effort to ensure that they remain in employment and seek to find them suitable alternative employment where remaining in their current role is not possible. Financial provision is made for those who become unable to work because of permanent disability through the provision of disability pensions.

Employee involvement

During 1998 the Group continued to implement its policy to involve staff on matters of concern to them as employees and to achieve an awareness of the financial and economic factors affecting the performance of the Group. This involved communication and consultation mechanisms such as regular meetings with employee representatives, team meetings and newsletters which were supplemented by various additional communication initiatives.

There have been a number of employee roadshows where staff have had the opportunity to meet and discuss matters of general importance with senior management. A number of employee representatives also attended meetings of the European level B.A.T. Industries Employee Forum during 1998, although this will be replaced in 1999 by membership of the Zurich Financial Services Employee Forum.

The Group operates a number of performance related bonus and share participation schemes based on the results achieved by the Group.

Employee share schemes

The Board recognises the importance of the involvement of employees through share participation schemes, which encourage awareness of the Group's financial performance and participation and success of the Group. Upon the demerger of the B.A.T Industries' financial services business, including Allied Dunbar, from B.A.T Industries p.l.c., the B.A.T Industries p.l.c. savings related and executive options schemes had to be discontinued, and options were exercised by the

participants pursuant to the rules of each scheme. Since the completion of the merger of B.A.T Industries' financial services business, including Allied Dunbar, with the Zurich Insurance Company in September 1998, a Share Option Plan has been introduced under which all UK employees were awarded an option to acquire 160 shares in Allied Zurich p.l.c. at 625p per share, exercisable in normal circumstances in the six month period commencing with the third anniversary of the grant.

A new Share Save Option Scheme has recently been launched, under which employees can save up to £250 per month over a three or five year period which they can then use to acquire shares in Allied Zurich p.l.c. In February 1999, the option price of 690.8p was set, this being a 20% discount to the market price of Allied Zurich p.l.c. shares.

The environment

The Group follows positive environmental policies and aims to comply with current legislation and regulations. The overall objectives are to minimise any negative environmental impact because of our operations and to maximise opportunities to contribute to improving the environment.

Creditor payment policy

The Company aims to agree the terms of payment with its suppliers when agreeing the terms of each transaction. Normally these are within the supplier's own standard payment period. The Company aims to pay all of its suppliers within the agreed terms.

The value of trade creditors at 31 December 1998 can be represented as creditors outstanding for 2 days (1997 18 days).

For 1999 the Company's policy concerning the payment of its trade creditors is to follow the Confederation of British Industry's Prompt Payment Code for all suppliers. Information about the code may be obtained from the CBI, Centrepont, 103 New Oxford Street, London, WC1 1DN.

Donations

The Company paid £1.7 million gross of taxation (1997 £2.3 million) to Zurich Financial Services (UKISA) Community Trust Limited under a deed of covenant.

Auditors

Our auditors, Coopers and Lybrand, merged with Price Waterhouse on 1 July, following which Coopers and Lybrand resigned and the directors appointed the new firm, PricewaterhouseCoopers, as auditors. A resolution to re-appoint PricewaterhouseCoopers as auditors will be proposed at the Annual General Meeting.

Statement of directors' responsibilities

The following statement sets out the responsibilities of the directors in relation to these financial statements. The report of the auditors on page 12 sets out their responsibilities in relation to these financial statements.

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

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

- select appropriate accounting policies and apply them consistently, subject to any material departures being disclosed and explained;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed; and
- prepare the financial statements on a going concern basis, unless they consider that to be inappropriate.

The directors are responsible for ensuring that the Company keeps sufficient accounting records to disclose with reasonable accuracy the financial position of the Company and the Group and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for taking reasonable steps to safeguard the assets of the Company and the Group, and in that context to have proper regard to the establishment of appropriate systems of internal control with a view to the prevention and detection of fraud and other irregularities.

The directors are required to prepare the financial statements and to provide the auditors with every opportunity to take whatever steps and undertake whatever inspections they consider to be appropriate for the purpose of enabling them to give their audit report.

The directors consider that they have pursued the actions necessary to meet their responsibilities as set out in this statement.

On behalf of the Board,



Peter Howe Secretary
20 April 1999

Actuary's certificate

I certify that in my opinion the computation of the long term business provision has been prepared on the basis of recognised actuarial methods and with due regard to the actuarial principles laid down in the European Union Council Directive 92/96/EEC and that the long term business provision is sufficient to enable the Group to meet any liabilities arising out of insurance contracts as far as can be reasonably foreseen.

A handwritten signature in cursive script, reading "J.E. Bullimore".

J.E. Bullimore Appointed Actuary
20 April 1999

Auditors' report

Report of the auditors to the members of Allied Dunbar Assurance plc

We have audited the financial statements on pages 13 to 39, which have been prepared in accordance with the accounting policies set out on pages 13 to 15.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report, including as described on page 10, the financial statements. Our responsibilities as independent auditors are established by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any material misstatement or material inconsistencies with the financial statements.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group at 31 December 1998 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers
Chartered Accountants and
Registered Auditors London
20 April 1999

Accounting policies

1 Disclosure requirements

The accounts have been prepared in accordance with Section 255A of, and the special provisions relating to insurance companies of Schedule 9A to, the Companies Act 1985 (the 'Act'). The accounts have also been prepared in accordance with the Association of British Insurers' Statement of Recommended Practice on Accounting for Insurance Business dated December 1998.

The financial statements have been prepared in accordance with applicable accounting standards. Compliance with Statement of Standard Accounting Practice ('SSAP') 19 'Accounting for Investment Properties' requires departure from the requirements of the Companies Act 1985 relating to depreciation and an explanation of the departure is given in the accounting policy note relating to the valuation of investments below.

The Company and Group are exempt from the requirement to produce a cash flow statement under Financial Reporting Standard 1 (Revised) as the company is a subsidiary undertaking of Zurich Financial Services, which prepares a consolidated cash flow statement.

Accounting for investment gains by insurance companies, in accordance with the ABI SORP and generally accepted accounting principles, is not considered to give rise to differences from the historic cost convention. As there is no material difference between the results for the current year and the previous year as described in the profit and loss account and the results on an historic cost basis, no note on the historic cost profit and loss for the year is given.

2 Basis of consolidation

The Group accounts incorporate the assets and liabilities of the Company and its material subsidiary undertakings at 31 December and the results for the year ended on that date. The accounts of subsidiary undertakings constituted as open-ended investment companies are not consolidated as they are held as investments to cover linked liabilities and the directors are of the opinion that the effect of consolidating their results, assets and liabilities would be immaterial.

The results of subsidiary undertakings attributable to unit-linked and other long term business funds are included in the technical account. The results of all other subsidiary undertakings are included in the non-technical account.

3 Premiums

Premiums are included in the technical account when due. For unit linked business the due date is taken as the date that the associated technical provisions are established.

4 Investment income

Income from investments which are directly related to the carrying on of long term business is credited to the technical account. All other investment income is dealt with in the non-technical account.

Investment income is grossed up to include the relevant tax credits or associated income tax deducted at source.

5 Investment gains and losses

Realised gains and losses on investments are calculated as the difference between net sale proceeds and original cost.

Realised and unrealised gains and losses arising on assets directly related to the carrying on of long term business are included in the technical account.

The Company's unrealised gains and losses on investments in subsidiary undertakings that do not form part of the assets attributable to long term business, are taken to a revaluation reserve.

Realised and unrealised gains and losses on other investments are taken to the non-technical account.

6 Claims

Death claims are accounted for on notification of death. Annuities and maturities are included in the technical account when due for payment. Surrenders are accounted for at the earlier of the payment date or when the policy ceases to be included in the calculation of technical provisions.

Claims incurred include related claims handling costs.

7 Expenses

Expenses charged in the technical account comprise acquisition costs, administrative expenses, and investment expenses attributable to long term business for the year. All other expenses are charged to the non-technical account.

The costs of acquiring new business are deferred to the extent that they are recoverable from margins in future matching revenues. Such deferred costs are included in the balance sheet as an asset and are determined explicitly. Deferred acquisition costs are amortised over a period which is consistent with a prudent assessment of the expected pattern of receipt of future revenue margins for each product type.

Administrative expenses are charged in the profit and loss account when incurred.

8 Operating leases

Rentals under operating leases are charged to the profit and loss account on a straight line basis over the term of the lease.

9 Pension costs

Pension costs are charged to the profit and loss account on a systematic basis over the service lives of employees. Surpluses and deficits arising are allocated over the expected remaining service lives of current employees.

10 Taxation

The Company is liable to United Kingdom corporation tax on the basis applicable to a life assurance company and the provision for current taxation is charged in the profit and loss account.

The balance on the technical account is computed on an after tax basis reflecting the taxation applicable to long term business operations. In the non-technical account, the balance transferred from the technical account is grossed-up by the taxation attributable to shareholders' profits from long term business at the Company's effective rate of corporation tax.

Provision for deferred taxation is made on timing differences using the liability method to the extent that it is probable the liability will crystallise

11 Valuation of investments

Freehold and leasehold land and buildings, including properties held for the Group's own occupation, are valued on an open market basis as at 31 December by independent valuers.

Depreciation is not provided on freehold and leasehold investment properties although the Act requires all properties to be depreciated. That requirement conflicts with Statement of Standard Accounting Practice ('SSAP') 19 which states that investment properties should not be subject to depreciation. The directors consider it is necessary to adopt SSAP 19 to give a true and fair view and, in their opinion, depreciation would not be significant because of expected future residual values.

Debt securities and other fixed income securities, shares (other than shares in subsidiary undertakings) and other variable yield securities, held as assets to cover linked liabilities, are valued at the lowest offered dealing price in compliance with the Company's policy conditions. All other listed investments together with holdings of shares in open ended investment companies are valued at middle market prices.

Loans secured by mortgages, other loans, unlisted investments, forward exchange and futures contracts and other investments are stated at the directors' estimate of likely realisable value.

The Company's interests in subsidiary undertakings are included at their net asset values.

12 Tangible assets

Tangible assets comprise leasehold improvements, plant and machinery, fixtures, fittings and equipment. Tangible assets are included at cost and are depreciated as follows:

■ Leasehold improvements, plant and machinery, fixtures, fittings and equipment.	Over a maximum period of five years
■ Other office furniture included in fixtures, fittings and equipment.	10 years
■ Specially designed computer facilities included in plant and machinery.	20 years

The depreciation charge is included in administrative expenses.

13 Foreign currencies

Assets and liabilities in foreign currencies are expressed in sterling at rates of exchange ruling at 31 December. Results of subsidiary undertakings reporting in foreign currencies are translated into sterling at average rates of exchange. For assets held to cover linked liabilities, surpluses and deficits on translation are included in the technical account.

14 Technical provisions

Technical provisions for linked liabilities are determined by reference to the value of assets held to provide linked benefits to the relevant policyholders.

The long term business provision is determined by the Company's Actuary in accordance with the actuarial principles laid down in the European Union Council Directive 92/96/EEC.

15 Goodwill

In accordance with Financial Reporting Standard 10, the treatment of goodwill has been changed to capitalise and systematically amortise purchased goodwill arising on acquisitions. Goodwill previously eliminated directly against reserves would have been fully written down in previous years and no prior year adjustment is necessary. There have been no acquisitions during the year and hence there is no impact on the 1998 financial statements.

Consolidated profit and loss account

For the year ended 31 December 1998

Technical account – long-term business

	Note	1998 £m	1997 as restated £m
Earned premiums, net of reinsurance	1	1,942	1,768
Investment income	2	1,506	1,397
Net unrealised gains on investments	2	1,049	826
Other technical income		17	27
Claims incurred, net of reinsurance	3	(1,507)	(1,358)
Change in long term business provision, net of reinsurance	4&5	(108)	(150)
Change in technical provisions for linked liabilities		(2,242)	(1,964)
Net operating expenses	4&6	(408)	(364)
Investment expenses and charges		(36)	(30)
Taxation attributable to long term business	4&9	(116)	(65)
Balance on the technical account – long term business	4	97	87

As described in note 4, the balance on the technical account – long term business for 1998 is after charging an exceptional item in relation to the Financial Services Authority (FSA) review of pension transfers and opt-outs of **£35 million** (1997 59 million).

All the above amounts in the technical account derive from continuing operations.

The accounting policies on pages 13 to 15 and the notes on pages 20 to 39 form part of these accounts

Consolidated profit and loss account

For the year ended 31 December 1998

Non-technical account.

	Note	1998 £m	1997 as restated £m
Balance on the technical account - long term business	4	97	87
Tax credit attributable to the balance on the long term business technical account	9	44	24
Profit from long term business before tax		141	111
Investment income	2	51	43
Investment expenses and charges		(32)	(26)
Collective investment scheme sales		19	98
Other income		30	33
Collective investment scheme creations and repurchases		(18)	(96)
Net operating expenses	6	(31)	(31)
Operating profit	10		
Continuing operations		160	126
Discontinued operations		-	6
		160	132
Profit on disposal of discontinued operations	10	-	71
Profit on ordinary activities before tax		160	203
Taxation on profit on ordinary activities	9	(51)	(28)
Profit for the financial year		109	175
Dividends	11	(217)	(126)
Retained (deficit)/profit		(108)	49

The Group has no recognised gains and losses in the period other than the profit for the period, therefore no statement of total recognised gains or losses has been included.

Collective investment scheme sales in 1997 include £79 million in respect of discontinued operations.

The accounting policies on pages 13 to 15 and the notes on pages 20 to 39 form part of these accounts

Balance sheets

as at 31 December 1998

Assets

	Note	Group		Company	
		1998	1997	1998	1997
		£m	£m	£m	£m
Investments					
Land and buildings	12	11	10	10	9
Investments in group undertakings	13	-	-	85	75
Other financial investments	14	1,805	1,681	1,337	1,267
		1,816	1,691	1,432	1,351
Assets held to cover linked liabilities	15	18,781	16,536	18,321	16,196
Reassurers' share of technical provisions	16	13	10	13	10
Debtors					
Debtors arising out of direct insurance operations	17	56	51	56	51
Amounts owed by group undertakings		33	25	88	74
Other debtors		46	48	16	22
		135	124	160	147
Other assets					
Tangible assets	18	43	37	38	34
Cash at bank and in hand		115	97	9	1
		158	134	47	35
Prepayments and accrued income					
Accrued interest and rent		36	28	36	27
Deferred acquisition costs		431	400	426	395
Other prepayments and accrued income		18	12	9	11
		485	440	471	433
Total assets		21,388	18,935	20,444	18,172

The accounting policies on pages 13 to 15 and the notes on pages 20 to 39 form part of these accounts

Balance sheets

as at 31 December 1998

Liabilities

		Group		Company	
	Note	1998	1997	1998	1997
		£m	£m	£m	£m
Capital and Reserves					
Called up share capital	19	124	1	124	1
Share premium account	20	75	75	75	75
Revaluation reserve	20	-	-	76	66
Capital redemption reserve	20	6	6	6	6
Profit and loss account	20	688	796	612	730
Shareholders' funds - equity interests	21	893	878	893	878
Technical provisions					
Long term business provision	22	960	851	959	851
Gross outstanding claims		66	64	66	64
		1,026	915	1,025	915
Technical provisions for linked liabilities	22	18,754	16,512	18,300	16,177
Provision for other risks and charges	23	78	57	73	57
Creditors					
Creditors arising out of direct insurance operations		24	20	24	20
Deposits by credit institutions and customer accounts of banking subsidiary undertakings	24	483	422	-	-
Amounts owed to credit institutions		28	26	30	26
Amounts owed to group undertakings		3	3	24	17
Dividends payable		10	28	10	28
Other creditors including tax and social security		65	53	49	34
		613	552	137	125
Accruals and deferred income	24	*	21	16	20
Total liabilities		21,388	18,935	20,444	18,172

The accounts were approved by the Board of Directors on 20 April 1999.

K. R. Baldwin, Chief Executive P. A. Hodgkinson, Managing Director S. P. Deighton, Finance Director

The accounting policies on pages 13 to 15 and the notes on pages 20 to 39 form part of these accounts

Notes to the accounts

1 Earned premiums and new business

	1998 £m	1997 £m
Gross earned premiums:		
Life and health		
Single premiums	505	411
Regular premiums	516	477
Pensions and annuities		
Single premiums	334	338
Regular premiums	596	550
Total gross earned premiums	1,951	1,776
Outward reinsurance premiums	(9)	(8)
Earned premiums, net of reinsurance	1,942	1,768

Earned premiums mainly result from direct unit linked assurance business written in the United Kingdom. They include **£136 million** (1997 £98 million) in respect of business written in the Isle of Man.

New business

Total new business premiums for the year, comprising new regular premiums and 10% of new single premiums and collective investment scheme sales, were **£275 million** (1997 £268 million, of which £260 million were from continuing operations). New regular premiums were **£190 million** (1997 £183 million, all from continuing operations). New single premiums, including collective investment scheme sales, were **£853 million** (1997 £845 million, of which £766 million were from continuing operations).

Notes to the accounts

2 Investment return summary

	Non-technical		Technical	
	1998	1997 as restated	1998	1997 as restated
	£m	£m	£m	£m
Income from land and buildings	-	-	105	88
Income from other investments	51	43	646	604
	51	43	751	692
Gains net of losses on the realisation of investments	-	-	755	705
Total investment income	51	43	1,506	1,397
Net unrealised gains on investments	-	-	1,049	826
Investment expenses and charges	(32)	(26)	(36)	(30)
Net investment return	19	17	2,519	2,193

The net investment return relating to investments which are directly related to the carrying on of long term business is included in the technical account. The net investment return on other investments is included in the non-technical account.

The restatement of 1997 is in consequence of a change in accounting policy for shareholders' investment return following the publication of the ABI SORP. In 1997 the shareholders' net investment return of £24 million was recorded in the non-technical account.

3 Claims incurred, net of reinsurance

	1998	1997
	£m	£m
Gross claims paid	1,511	1,358
Reassurers' share	(3)	(4)
	1,508	1,354
Change in provision for outstanding claims	2	7
Reassurers' share	(3)	(3)
	(1)	4
Claims incurred, net of reinsurance	1,507	1,358

Notes to the accounts

4 Exceptional item

The change in the long term business provision and net operating expenses for 1998 and 1997, shown in the technical account, include amounts representing increases in the provisions for the expense of carrying out the FSA review of pensions transfers and opt-outs and the costs of providing redress to clients who may have been disadvantaged.

The effect in 1998 and 1997 on the balance on the technical account and on profit on ordinary activities before tax and profit for the financial year shown in the non technical account, is as follows:

	1998 £m	1997 £m
Technical account		
Change in long term business provision, net of reinsurance	8	68
Net operating expenses	27	14
Taxation attributable to long term business	-	(23)
Decrease in the balance on the technical account - long term business	35	59
Non-technical account	£m	£m
Decrease in profit on ordinary activities before tax	51	85
Tax credit attributable to the balance on the long term business technical account at 31% (1997 31.5%)	(16)	(26)
Decrease in profit for the financial year	35	59

5 Change in long term business provision, net of reinsurance

	1998 £m	1997 £m
Change in long term business provision	109	150
Reassurers' share	(1)	-
Change in long term business provision, net of reinsurance	108	150

Notes to the accounts

6 Net operating expenses

	1998 £m	1997 £m
Net operating expenses in the technical and non-technical accounts include:		
Depreciation	14	13
Interest payable and operating lease rentals		
Interest payable	2	2
Operating lease rentals - land and buildings for the Group's own occupation	20	21
	22	23

Auditors' remuneration

The remuneration of the auditors for audit of the Group was £766,000 (1997 £678,000), including £568,000 (1997 £482,000) for audit of the Company. In addition, £305,000 (1997 £182,000) was paid for regulatory, tax and consultancy work for the Company and its UK subsidiary undertakings to PricewaterhouseCoopers. This includes £179,000 paid to Coopers and Lybrand and £66,000 paid to Price Waterhouse prior to the date of appointment of PricewaterhouseCoopers as auditors. Non audit fees in 1997 comprise solely amounts paid to the previous auditors Coopers and Lybrand.

	1998 £m	1997 as restated £m
Net operating expenses in the technical account comprise:		
Acquisition costs arising in the year	281	252
Change in deferred acquisition costs	(31)	(21)
Administrative expenses	158	133
Net operating expenses	408	364

Commissions

Total commissions charged in the technical account in respect of direct insurance business for the year were £147 million (1997 £137 million).

Notes to the accounts

7 Staff costs

	1998 £m	1997 £m
Staff costs comprised:		
Wages and salaries	88	80
Social security costs	8	8
Other pension costs (note 29)	7	7
Total staff costs	103	95
The average number of employees of the Company and its subsidiary undertakings fell within the following categories:		
Sales and sales support	801	910
Client administration	1,233	1,194
Group services	764	974
	2,798	3,078

8 Emoluments of directors

	1998 £'000	1997 £'000
Emoluments of highest paid director	643	551
Other directors	1,405	2,356
Total aggregate emoluments	2,048	2,907
Compensation for loss of office	1,031	199
Total remuneration	3,079	3,106
Pension contributions to defined contribution scheme	40	21

Notes to the accounts

8 Emoluments of directors (*continued*)

Directors' emoluments (none of which were in respect of fees) include performance related pay, benefits, bonuses and an accrual in respect of deferred bonuses which may become payable in future years.

The emoluments of 2 directors (1997 1 director), which were paid directly by a fellow subsidiary, are included to the extent that they are charged as an expense to the Company.

The emoluments of 2 directors (1997 nil directors), which were paid directly by the parent company, are included to the extent that they are charged as an expense to the Company.

The emoluments of 4 directors (1997 2 directors) are net of amounts recharged to fellow subsidiaries.

9 directors (1997 5 directors) exercised options to subscribe for shares in B.A.T Industries p.l.c., the ultimate holding company until 8 September 1998, during the year.

10 directors, who served during the year, (1997 9 directors) are members of the defined benefit scheme.

6 directors (1997 6 directors) are members of the defined contribution scheme. The value of the highest paid director's accrued annual pension benefits at 31 December 1998 was **£50,055** (1997 £33,000).

9 Taxation

	Non-technical		Technical	
	1998	1997 as restated	1998	1997 as restated
	£m	£m	£m	£m
Tax credit attributable to the balance on the long term business technical account	44	24	-	-
Corporation tax on income for the year at 31% (1997 31.5%)	3	4	60	54
Tax attributable to UK dividends received	-	-	35	31
Overseas taxation	-	-	2	2
Amount payable to holding company in respect of ACT surrendered	4	-	21	-
Amount payable to fellow group undertaking in respect of Group relief surrendered	-	-	1	-
Prior year adjustments	-	-	(3)	(1)
Current taxation	51	28	116	86
Deferred taxation	-	-	-	(21)
Taxation charge	51	28	116	65

Notes to the accounts

9 Taxation (*continued*)

The balance on the technical account is computed on an after tax basis, reflecting the taxation applicable to long term business operations. In the non-technical account, the balance transferred from the technical account has been grossed-up, in accordance with the accounting policy described on page 14, at the corporation tax rate of 31% (1997 31.5%, adjusted to reflect surplus ACT surrendered by the Company's ultimate holding company for no charge).

The corporation tax on income for the year in the technical account has been reduced by **£21 million** (1997 £11 million) in respect of surplus ACT surrendered by the Company's ultimate holding company for a consideration of **£21 million** (1997 £Nil).

The corporation tax on income for the year in the non-technical account has been reduced by **£4 million** (1997 £3 million) in respect of surplus ACT surrendered by the Company's ultimate holding company for a consideration of **£4 million** (1997 £Nil).

The corporation tax on income for the year in the technical account has been reduced by **£1 million** (1997 £Nil) in respect of group relief surrendered by a fellow group undertaking for a consideration of **£1 million** (1997 £Nil).

The Company, in common with other Life Offices, is no longer able to recover tax credits attaching to dividends received from UK companies, in relation to Pensions business. In accordance with the accounting policy described on page 13, such dividend income has been grossed up to include the relevant tax credits and the unrecovered tax credits have been included in the taxation charge in the technical account.

Notes to the accounts

10 Sale of subsidiary

On 1 July 1997 the Group disposed of its subsidiary, Allied Dunbar Unit Trusts p.l.c., for a profit of £71 million. Goodwill attributable to the interest in the subsidiary of £3 million, previously written off through reserves, was charged to the profit and loss account in calculating the profit on disposal.

All of 1998 operating profit relates to continuing operations. The elements of 1997 operating profit relating to continuing and discontinued operations are as follows:

	Continuing as restated £m	1997 Discontinued £m	Total as restated £m
Profit from long term business before tax	111	-	111
Investment income	43	-	43
Investment expenses and charges	(26)	-	(26)
Collective investment scheme sales	19	79	98
Other income	21	12	33
Collective investment scheme creations and repurchases	(18)	(78)	(96)
Net operating expenses	(24)	(7)	(31)
Operating profit	126	6	132

11 Dividends

	1998 £m	1997 £m
<i>The Company's dividends are:</i>		
Interims paid	207	98
Final proposed	10	28
	217	126

Notes to the accounts

12 Land and buildings

	Group		Company	
	1998	1997	1998	1997
	£m	£m	£m	£m
At open market value:				
Freeholds	8	7	7	6
Long leaseholds	3	3	3	3
Total land and buildings at open market value	11	10	10	9
Total land and buildings at cost	26	25	24	23

Land and buildings comprise freehold and leasehold properties acquired by the Group for its own occupation and have been valued by independent valuers Jones Lang Wootton.

13 Investments in group undertakings

Investments in group undertakings comprise shares in subsidiary undertakings, other than subsidiary undertakings held as assets to cover linked liabilities, with an original cost of **£11 million** (1997 £11 million).

The Company's principal subsidiary undertakings are shown on page 39. Subsidiary undertakings are all wholly owned except for Allied Dunbar International Specialist Funds plc (ADISF) where the percentage of equity shares held is 99.7%. ADISF is an open-ended investment company and the Group's investment is held as an asset to cover linked liabilities. The results and assets and liabilities of ADISF have not been consolidated in the Group accounts, as the directors are of the opinion that the effect would be immaterial.

The Company's investments are all in ordinary shares. A complete list of investments in subsidiary undertakings will be attached to the Company's Annual Return made to the Registrar of Companies.

Notes to the accounts

14 Other financial investments

	Group		Company	
	1998	1997	1998	1997
	£m	£m	£m	£m
At market value				
Shares and other variable yield securities	125	152	123	152
Debt securities and other fixed income securities	647	368	647	368
Loans secured by mortgages	663	638	247	272
Other loans:				
Secured on policies	36	42	36	42
Other	6	6	-	-
Deposits with credit institutions	328	475	284	433
Total other financial investments at market value	1,805	1,681	1,337	1,267
At cost				
Shares and other variable yield securities	118	146	118	146
Debt securities and other fixed income securities	569	343	569	343
Loans secured by mortgages	676	649	252	277
Other loans:				
Secured on policies	36	42	36	42
Other	6	6	-	-
Deposits with credit institutions	328	475	284	433
Total other financial investments at cost	1,733	1,661	1,259	1,241
Listed investments included above at market value are:				
Shares and other variable yield securities	117	152	117	152
Debt securities and other fixed income securities	647	368	647	368
Total listed investments at market value	764	520	764	520

Loans secured by mortgages include loans and advances to customers of Dunbar Bank plc and Allied Dunbar Bank International Limited amounting to **£416 million** (1997 £367 million).

The Group held **£3,268 million** (1997 £2,703 million) of investments in collective investment schemes, managed by group and fellow subsidiary undertakings.

Notes to the accounts

15 Assets held to cover linked liabilities

The cost of investments, including investments in group undertakings, held to cover linked liabilities was **£13,717 million** (1997 £12,477 million).

16 Reassurers' share of technical provisions

	Group		Company	
	1998	1997	1998	1997
	£m	£m	£m	£m
Long term business provision	6	5	6	5
Claims outstanding	7	5	7	5
Reassurers' share of technical provisions	13	10	13	10

17 Debtors

	Group		Company	
	1998	1997	1998	1997
	£m	£m	£m	£m
Debtors arising out of direct insurance operations				
comprise amounts due from:				
Policyholders	1	2	1	2
Intermediaries	55	49	55	49
Total debtors arising out of direct insurance operations	56	51	56	51
All amounts fall due within one year.				

Notes to the accounts

18 Tangible assets

	Leasehold improvements plant and machinery £m	Fixtures fittings and equipment £m	Total £m
Movements in tangible assets for the year are:			
Group			
Cost, at 1 January 1998	20	85	105
Additions	1	22	23
Disposals	-	(11)	(11)
Cost, at 31 December 1998	21	96	117
Accumulated depreciation, at 1 January 1998	11	57	68
Charge for year	2	12	14
Disposals	(1)	(7)	(8)
Accumulated depreciation, at 31 December 1998	12	62	74
Net book value, at 31 December 1997	9	28	37
Net book value, at 31 December 1998	9	34	43
Company			
Cost, at 1 January 1998	19	72	91
Additions	1	18	19
Disposals	-	(9)	(9)
Cost, at 31 December 1998	20	81	101
Accumulated depreciation, at 1 January 1998	10	47	57
Charge for year	2	10	12
Disposals	-	(6)	(6)
Accumulated depreciation, at 31 December 1998	12	51	63
Net book value, at 31 December 1997	9	25	34
Net book value, at 31 December 1998	8*	30	38

Notes to the accounts

23 Provision for other risks and charges

	Expenses of FSA pensions review £m	Other provisions £m	Total £m
Movements in provisions for the year are:			
Group			
Provision, at 1 January 1998	23	34	57
Transfer of provisions to other Group undertakings	-	(1)	(1)
Provided in respect of the year	27	16	43
Utilised in the year	(12)	(9)	(21)
Provision, at 31 December 1998	38	40	78
Company			
Provision, at 1 January 1998	23	34	57
Transfer of provisions to other Group undertakings	-	(4)	(4)
Provided in respect of the year	27	14	41
Utilised in the year	(12)	(9)	(21)
Provision, at 31 December 1998	38	35	73
The provision for the expenses of the FSA pension review is in respect of the estimated cost of carrying out the Financial Services Authority's review of pension transfers and opt-outs.			
	1998 £m	1997 £m	
Group and Company			
Deferred taxation provided comprises:			
Deferred acquisition costs	44	44	
Excess of depreciation over capital allowances	(6)	(3)	
Losses available for set off against future taxable profits	(40)	(35)	
Other timing differences	2	(6)	
Provision, at 31 December	-	-	
In addition, £309 million (1997 £283 million) has been provided in respect of unrealised gains on assets held to cover linked liabilities and is included in technical provisions for linked liabilities.			

Notes to the accounts

24 Creditors

Deposits by credit institutions and customer accounts of banking subsidiary undertakings includes **£303 million** (1997 £262 million) falling due after more than one year.

25 Ultimate holding company

The Company's ultimate parent company is Zurich Financial Services, which is incorporated in Switzerland. Zurich Financial Services is owned as to 57% by Zurich Allied AG, incorporated in Switzerland and as to 43% by Allied Zurich p.l.c., incorporated in England and Wales.

Copies of the consolidated financial statements of Zurich Financial Services can be obtained from:

The Secretary

Allied Zurich p.l.c.

22 Arlington Street

London

SW1A 1RW

The Company's immediate parent company is Zurich Financial Services (UKISA) Limited, which is incorporated in England and Wales. Copies of the consolidated financial statements of Zurich Financial Services (UKISA) Limited can be obtained from:

The Secretary

Zurich Financial Services (UKISA) Limited

22 Arlington Street

London

SW1A 1RW

Notes to the accounts

29 Group pension arrangements

The Group operates two funded defined benefit schemes for staff based on final pay and two defined contribution schemes for sales managers and other staff.

The most recent valuations for the UK and Isle of Man defined benefit schemes, carried out triennially by independent actuaries, were at 31 December 1996 and 31 December 1997 respectively.

The valuations showed that the actuarial value of the schemes' assets were **£174 million** and that this represented 126% of the value of the benefits that had accrued to members, after allowing for expected future increases in earnings. The assumptions used by the actuaries in their valuations, and which have the most significant effect on the results of the valuations, are a rate of return on investments of 9%, dividend increases of 4.5% and rates of increase in salaries and pensions of 7% and 4.5% respectively.

Contributions are determined on the basis of the triennial valuations using the projected unit method, which makes allowance for the expected flow of new entrants. On the recommendation of the actuaries, contributions have been suspended to the UK scheme until the results of the next valuation, due no later than 31 December 1999, are known. As a result of this suspension a pension provision of **£11 million** (1997 £6 million) is held.

The total pension cost for the year was **£7 million** (1997 £7 million).

Principal subsidiary undertakings

Dunbar Bank plc

The provision of banking and related services in the UK.

Allied Dunbar Healthcare Marketing Limited*

Arranging private medical and long term care insurance in the UK.

Dunbar Independent Limited*

The provision of broking services in the UK.

These companies are registered in England and Wales.

Allied Dunbar International Assurance Limited*

The provision of long term assurance in the Isle of Man.

Allied Dunbar Bank International Limited

The provision of banking services in the Isle of Man.

Allied Dunbar International Fund Managers Limited*

The management of international investment funds in the Isle of Man.

These companies are incorporated in the Isle of Man.

Those holdings marked by an asterisk (*) are owned directly by the Company.

