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AA Mutual International Insurance Company Limited

Financial Statements

Year ended 31 December 2003

AA MUTUAL INTERNATIONAL INSURANCE COMPANY LIMITED
DOING BUSINESS AS
UNDERWRITERS
ACT 1982

Company No: 1432586





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AA MUTUAL INTERNATIONAL INSURANCE COMPANY LIMITED



COMPANY INFORMATION

Directors

E. J. Kok
P. J. Elliott

Registered Office

Hampden House
Great Hampden
Great Missenden
Buckinghamshire
HP16 9RD

Secretary

Hampden Legal Plc
Hampden House
Great Hampden
Great Missenden
Buckinghamshire
HP16 9RD

Bankers

Barclays Bank Plc
London Customer Services Centre
PO Box 46116
London EC4N 8WB

Auditors

Seymour Taylor
57 London Road
High Wycombe
Buckinghamshire
HP11 1BS



REPORT OF THE DIRECTORS

The directors present their annual report and audited financial statements for the year ended 31 December 2003.

Directors' Responsibilities

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 of the profit or loss of the company for that period. In preparing those financial statements, the directors are required to:

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

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. 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.

Principal Activity

The company used to be authorised to underwrite all classes of non-life insurance business, but has been in run-off since the 4th December 1987 and Hampden Insurance Management Services Plc are acting as agent for the run-off. The directors continue to negotiate commutations with interested creditors to resolve outstanding liabilities.

AA Mutual Insurance Association

AA Mutual Insurance Association Limited (AAMA) was the company's former parent undertaking and major reinsurer. The short-term insurance business of AAMA was placed in liquidation on 24th June 1986, the liquidation of AAMA will be finalised during 2004, and the company has no more claims against AAMA (2002: £300,001).

During 2003 the company received a distribution from AAMA totalling £358,315.

Business Review

On 1 August 2003, following approval by the FSA, a group reorganisation was undertaken and the entire issued share capital of the company was transferred from Hampden Plc to Hampden Insurance Group Limited, a fellow subsidiary company. The ultimate holding company remained Hampden Holdings Limited.

Results and Dividends

The results for the year are shown in the profit and loss account on page 6. The directors do not recommend the payment of a dividend.

Directors

The names of the directors of the company during the year were:

Mr. E.J. Kok

Mr. P.J. Elliott

Mr. P.J. Elliott retires at the Annual General Meeting and offers himself for re-election.

Directors' Interests

Neither of the directors had any beneficial interest in the share capital of the company or of Hampden Holdings Limited at 1st January 2003 or 31st December 2003.



REPORT OF THE DIRECTORS (continued)

Auditors

Moore Stephens resigned as auditors of the company on 10 December 2003 and Seymour Taylor were appointed in their stead. A resolution confirming their appointment and authorising the directors to fix their remuneration will be submitted to the forthcoming Annual General Meeting.

This report was approved by the board on 15 March 2004

A handwritten signature in black ink, appearing to be 'JL' or similar, written in a cursive style.

HAMPDEN LEGAL PLC

Secretary

Hampden House
Great Missenden
Buckinghamshire
HP169RD



**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDER OF
AA MUTUAL INTERNATIONAL INSURANCE COMPANY LIMITED
YEAR ENDED 31 DECEMBER 2003**

We have audited the financial statements of AA Mutual International Insurance Company Limited for the year ended 31 December 2003, which comprise the Profit and Loss account, the Balance Sheet, the Cashflow Statement and the related notes numbered 1 to 13. These financial statements have been prepared under the historical cost convention as modified by the revaluation of certain assets and liabilities, and the accounting policies set out on page 9.

This report is made solely to the company's shareholder, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's shareholder those matters we are required to state to them in an auditors 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 shareholder, for our audit work, for this report, or for the opinions we have formed.

Respective Responsibilities of Directors and Auditors

As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

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 1985. 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 with the company is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it. Our responsibilities do not extend to any other information.

Basis of Audit Opinion

We conducted our audit in accordance with United Kingdom 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.

Fundamental Uncertainties

In forming our opinion, we have considered the adequacy of the disclosures made in the financial statements concerning the following matters:

a) Technical provisions

The balance sheet includes technical provisions for claims outstanding of £600,411 (2002 - £711,093) and reinsurers' share thereof of £102,223 (2002 - £131,485). As explained in note 4, the company has completed its sixteenth year of run-off and the directors believe incurred claims to be effectively fully developed. Nevertheless they acknowledge that unexpected future experience may show that adjustments are required to these amounts, particularly in respect of:

- i) Assumptions made in estimating claims provisions and in the potential for new sources or types of claim to emerge; and
- ii) Assumptions made in estimating the reinsurers' share of claims outstanding and the appropriate provision in respect of them.

Accordingly, technical provisions could be either overstated or understated with a corresponding impact on shareholders funds. In the event of adjustments to these amounts being required, they will be reflected in the financial statements for the period in which they arise.



**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDER OF
AA MUTUAL INTERNATIONAL INSURANCE COMPANY LIMITED
YEAR ENDED 31 DECEMBER 2003 (continued)**

b) Reinsurance creditors

As explained in note 9, the company has written back certain provisions in respect of reinsurance creditors to the technical account on the grounds that they are time-barred. At 31 December 2003 the cumulative amount of these items was £1,728,751 (2002 - £2,168,805), giving rise to a net charge of £252,110 (2002 - £179,313) in respect of such amounts for the year. Due to the inherent uncertainties in the legal process, it is impossible to confirm whether such treatment is appropriate unless all the creditors involved have their claims subsequently denied by the courts.

c) Going concern

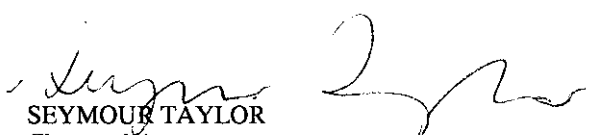
As explained in note 1, the financial statements have been prepared on a run-off basis which the directors believe to be appropriate given the company's circumstances. The company reported a (loss) / profit of £(256,707) (2002 - £19,647) for the year, which resulted in shareholders' funds of £285,585 (2002 - £542,292) at the year end. We have not received any current projections to establish whether or not the company can continue to meet its liabilities as they fall due over the next twelve months.

In the event of any significant adverse adjustments becoming necessary in relation to the matters explained in paragraphs a) and b) above, the future of the company might be uncertain.

In view of the possible significance of these issues, we consider that they should be brought to your attention. Our opinion is not qualified in these respects.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company at 31 December 2003 and of its loss for the year then ended, and have been properly prepared in accordance with the Companies Act 1985 applicable to insurance companies.


SEYMOUR TAYLOR
Chartered Accountants
Registered Auditors
57 London Road
High Wycombe
Buckinghamshire
HP11 1BS

15 March 2004

AA MUTUAL INTERNATIONAL INSURANCE COMPANY LIMITED

PROFIT AND LOSS ACCOUNT
For the year ended 31 December 2003

	Notes	£	2003	£	£	2002	£
TECHNICAL ACCOUNT							
General Business							
Wholly attributable to reinsurance operations							
Adjustments to gross premiums		27			1,084		
Adjustments to outward reinsurance premiums		—			<u>12,605</u>		
Refund of (earned premiums), net of reinsurance				(27)		11,521	
Gross claims paid or processed		(76,757)			388,309		
Reinsurers' share		<u>20,229</u>			<u>239,723</u>		
Net claims paid or processed		(96,986)			148,586		
Gross change in the provisions for claims		(82,365)			(763,705)		
Reinsurers' share		<u>29,262</u>			<u>238,833</u>		
Net deduction in the provision for claims		(53,103)			(524,872)		
Claims incurred net of reinsurance		(150,089)			(376,286)		
Administrative expenses	4	427,177			516,921		
Items arising from the run-off of the WF portfolio of business		(34,509)			56,039		
Time-barred reinsurance liabilities	9	252,110			179,313		
Change in provision for future claims handling costs		(225,000)			(250,000)		
(Decrease) / increase in provisions for doubtful debts		(21,696)			85,090		
Increase in amount anticipated from AAMA		<u>(58,314)</u>			<u>(300,000)</u>		
Total technical charges				189,679		(88,923)	
(Loss) / Profit on the technical account				<u>£ (189,652)</u>		£ <u>77,402</u>	
Non-Technical Account							
(Loss) / Profit on the technical account				(189,652)		77,402	
Investment income: Bank interest				19,000		41,005	
Exchange movements				<u>(86,055)</u>		<u>(98,760)</u>	
(Loss) / Profit on ordinary activities before taxation				(256,707)		19,647	
Tax on ordinary activities	5			—		—	
(Loss) / Profit on ordinary activities after taxation				(256,707)		19,647	
Retained loss brought forward				<u>(4,207,708)</u>		<u>(4,227,355)</u>	
Retained loss carried forward				<u>£ (4,464,415)</u>		£ <u>(4,207,708)</u>	

All operating income and expenditure is derived from run-off activities (note 3).

There are no recognised gains or losses other than those reported in the profit and loss account.

The notes on pages 9 to 12 form part of these financial statements.

AA MUTUAL INTERNATIONAL INSURANCE COMPANY LIMITED

BALANCE SHEET
As at 31 December 2003

	Notes	£	2003 £	£	2002 £
Assets					
Investments					
Other financial investments			1,286,995		2,002,087
Reinsurers' share of technical provisions					
Claims outstanding			102,223		131,485
Debtors					
Debtors arising out of reinsurance operations		41,017		49,868	
Other debtors		<u>559</u>		<u>300,001</u>	
			41,575		349,869
Other assets					
Cash at bank and in hand			<u>454,556</u>		<u>93,043</u>
Total Assets			<u>£ 1,885,349</u>		£ <u>2,576,484</u>
Liabilities					
Capital and reserves					
Called up share capital	6		4,750,000		4,750,000
Profit and loss account - retained loss			<u>(4,464,415)</u>		<u>(4,207,708)</u>
Shareholders' Funds Attributable to equity interests	7		285,585		542,292
Technical provisions					
Claims outstanding: Gross amount		600,411		711,093	
Provision for future claims handling costs		<u>225,000</u>		<u>450,000</u>	
			825,411		1,161,093
Creditors					
Creditors arising out of reinsurance operations		730,928		828,099	
Other creditors including taxation and social security		<u>43,425</u>		<u>45,000</u>	
			<u>774,353</u>		<u>873,099</u>
Total liabilities			<u>£1,885,349</u>		£ <u>2,576,484</u>

The financial statements on pages 6 to 12 were approved by the Board on 15 March 2004


E.J. Kok
Director

The notes on pages 9 to 12 form part of these financial statements.

**CASH FLOW STATEMENT**

For the year ended 31 December 2003

	Notes	2003 £	2002 £
Operating activities			
Funds (absorbed)/generated by operations	10	(168,529)	(1,279,903)
Returns on investments And servicing of finance			
Interest received		<u>19,000</u>	<u>41,005</u>
		(149,529)	(1,238,898)
Taxation			
Corporation tax paid		-	-
Management of liquid resources			
Cash withdrawn from deposits		<u>513,765</u>	<u>1,074,154</u>
(Decrease)/increase in cash	11	<u>£ 364,236</u>	£ (164,744)

The notes on pages 9 to 12 form part of these financial statements



NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2003

1 BASIS OF PREPARATION

The financial statements have been prepared on a run-off basis which the directors believe to be appropriate given the company's circumstances.

In the event of any significant adverse adjustments becoming necessary, the future of the company in the absence of other funding would be uncertain.

2 ACCOUNTING POLICIES

(a) Basis of accounting

The financial statements have been prepared on a run-off basis under the historical cost convention and in accordance with the provisions of Section 255 of and Schedule 9A to the Companies Act 1985. The financial statements have also been prepared in accordance with applicable accounting standards and to comply with the revised Statement of Recommended Practice issued by the Association of British Insurers.

(b) Investments & investment income

Investments are stated at market value. Investment income arising from deposits is accounted for on an accruals basis.

(c) Technical provisions

Gross claims outstanding comprise provisions for the estimated cost for settling all claims incurred, but unpaid at the balance sheet date, whether reported or not. The company has completed its sixteenth year of run-off and accordingly, the directors believe incurred claims to be effectively fully developed. The gross amount reserved represents outstanding claim amounts advised to the company by brokers on a claim by claim basis, together with a nominal provision for IBNR claims.

Reinsurers' share of technical provisions represents the amount of the company's gross claims outstanding that is recoverable from reinsurers, calculated by reference to event or cession codes attributable to individual inwards claims. The amount is calculated by reference to policy limits or cession percentages, adjusted as appropriate for commuted proportions and provisions for doubtful security.

(d) Foreign currencies

Assets and liabilities expressed in currencies other than sterling are translated to sterling at rates of exchange ruling at the year end, whilst revenue transactions are translated to sterling mainly at rates of exchange ruling at the year end. Realised and unrealised currency gains and losses are included in the non-technical profit and loss account.

(e) Interest receivable

Interest receivable is accounted for on an accruals basis and credited to the non-technical profit and loss account.

(f) Deferred taxation

Deferred tax is recognized in respect of all timing differences that have originated but not reversed at the balance sheet date. Timing differences are differences between taxable profits and the results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessment in periods different from those in which they are recognised in the financial statements.

A net deferred tax asset is regarded as recoverable, and therefore recognised, only when it can be regarded as a more likely than not there will be suitable taxable profits from which the future reversal of underlying timing differences can be deducted.

Deferred tax is measured on a non-discounted basis at the average rates that are expected to apply in the periods in which the timing differences are expected to reverse based on tax rates and laws enacted by the balance sheet date.



NOTES TO THE FINANCIAL STATEMENTS (continued)

For the year ended 31 December 2003

3. RUN- OFF

The company has been in run-off since 4th December 1987 and Hampden Insurance Management Services Plc are acting as agent for the run-off. The directors continue to negotiate commutations with interested creditors to resolve outstanding liabilities.

4. ADMINISTRATIVE EXPENSES

Administrative expenses include the following items, including attributable irrecoverable VAT:

Auditors' remuneration

in respect of audit services
in respect of other services

Fees charged by run-off agent

2003	2002
£	£

33,779	32,313
15,812	26,573

330,000	420,574
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The emoluments of the directors, were as follows:

Fees paid in respect of directors' services

-	-
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Employees

The company had no employees (2002 - none).

5. TAXATION ON (LOSS) / PROFIT ON ORDINARY ACTIVITIES

2003	2002
£	£

(a) Taxation

Tax on (loss) / profit on ordinary activities

£ -	£ -
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(b) Factors affecting current tax charge

The tax assessed for the year is lower than the standard rate of Corporation Tax in the UK of 30% (2002-30%), applied to the loss on ordinary activities before taxation. The differences are explained below.

(Loss)/Profit on ordinary activities before taxation

£ (256,707)	£ 19,647
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(Loss)/Profit on ordinary activities multiplied by the company's rate of corporation tax in the UK

-	5,894
---	-------

Effects of

Capital allowances in excess of depreciation

-	(13)
---	------

Expenses disallowed for tax purposes

-	(347,349)
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Current year tax losses not utilised

-	341,468
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Total current tax (Note 5(a))

£ -	£ -
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NOTES TO THE FINANCIAL STATEMENTS (continued)

For the year ended 31 December 2003

5. TAXATION ON (LOSS) / PROFIT ON ORDINARY ACTIVITIES (continued)

(c) Factors that may affect future tax charges

A deferred tax asset has not been recognised in respect of unrelieved tax losses.

The amount that has not been recognised at 31 December 2003, when calculated at large companies rate of corporation tax in the UK of 30%, is £1,498,882 (2002 - £1,346,850). The deferred tax asset would be recoverable to the extent that future suitable taxable profits are generated enabling the tax losses to be relieved.

	2003 £	2002 £
6. SHARE CAPITAL		
Authorised		
Ordinary shares of £1 each	£ <u>5,000,000</u>	£ <u>5,000,000</u>
Called up		
Ordinary shares of £1 each	£ <u>4,750,000</u>	£ <u>4,750,000</u>

7. RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS FUNDS

1 January 2003	542,292	522,645
Retained profit (loss) for the year	(256,707)	19,647
31 December 2003	£ <u>285,585</u>	£ <u>542,292</u>

8. TECHNICAL PROVISIONS

The company has completed its sixteenth year of run-off and accordingly, the directors believe incurred claims to be effectively fully developed and estimates in respect of technical provisions to be fairly stated on the basis of information currently available to them. Nevertheless they acknowledge that unexpected future experience may show adjustments are required to the gross provision for claims outstanding and reinsurers' share thereof, particularly in respect of:

- assumptions made in estimating claims provisions and in the potential for new sources or types of claim to emerge; and
- assumptions made in estimating the reinsurers' share of claims outstanding and the appropriate provision in respect of them.

In the event of adjustments being required to these amounts, they will be reflected in the financial statements for the period in which they arise.

9. REINSURANCE CREDITORS

Provisions relating to reinsurance creditors identified as time-barred have been written back to the technical account. At 31st December 2003 the cumulative amount of such items was £1,728,751 (2002 - £2,168,805) giving rise to a net charge of £252,110 (2002 - £179,313).

The process of identifying time-barred liabilities was performed in compliance with established case law and written legal opinions obtained by Hampden Insurance Management Services Plc on behalf of the company.



NOTES TO THE FINANCIAL STATEMENTS (continued)

For the year ended 31 December 2003

	2003 £	2002 £
10. RECONCILIATION OF OPERATING (LOSS) / PROFIT TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES		
(Loss) / profit on ordinary activities before taxation	(256,707)	19,647
Less bank interest	(19,000)	(41,005)
Decrease in net technical provisions	(306,420)	(856,908)
Decrease in creditors	(98,746)	(702,028)
Increase / (decrease) in debtors	308,294	(56,956)
Exchange rate adjustments on cash and investments	204,050	357,347
Net cash outflow from operating activities	£ (168,529)	£ (1,279,903)

11. MOVEMENT IN CASH, PORTFOLIO INVESTMENTS AND FINANCING

	At 1 January <u>2003</u>	Cashflow	Changes to Market Value and Currencies	At 31 December <u>2003</u>
Cash in hand and at bank	93,043	364,236	(2,723)	454,556
Cash deposits	<u>2,002,087</u>	<u>(513,765)</u>	<u>(201,327)</u>	<u>1,286,995</u>
	£ 2,095,130	£ (149,529)	£ (204,050)	£ 1,741,551

12. RELATED PARTY TRANSACTIONS

Disclosure of transactions with entities that are part of the group are not required, as more than 90% of the voting rights of the company are controlled within the group. No other material related party transactions were undertaken during the year.

13. ULTIMATE PARENT UNDERTAKING

The immediate holding company is Hampden Insurance Group Limited, and the ultimate holding company is Hampden Holdings Limited. Both these companies are registered in England and Wales.

Copies of the financial statements of both these companies can be obtained from their registered office, the address of which is as follows:

Hampden House,
Great Hampden,
Great Missenden,
Buckinghamshire
HP16 9RD