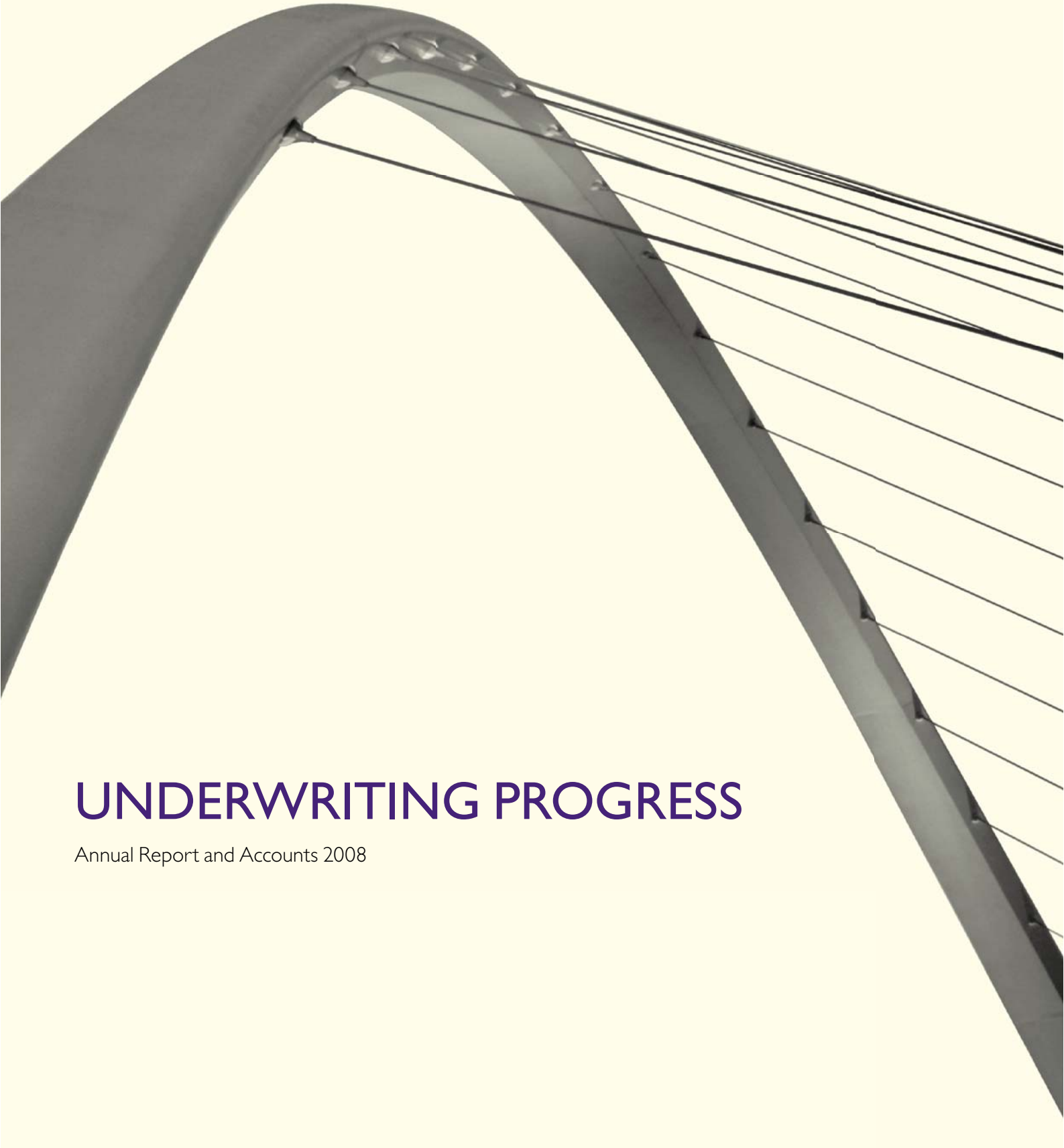
RSA



UNDERWRITING PROGRESS

Annual Report and Accounts 2008

CONTENTS

WE ARE A LEADING GENERAL INSURER DELIVERING SUSTAINABLE PROFITABLE PERFORMANCE.

WE OPERATE IN 33 COUNTRIES AND PROVIDE GENERAL INSURANCE PRODUCTS AND SERVICES IN OVER 130 COUNTRIES.

OUR PORTFOLIO OF BUSINESSES IS DIVERSE AND PROVIDES EXPOSURE TO MARKETS AT DIFFERENT POINTS IN THE INSURANCE CYCLE.

IN CHALLENGING TRADING CONDITIONS AND VOLATILE FINANCIAL MARKETS, 2008 HAS BEEN ANOTHER STRONG YEAR.

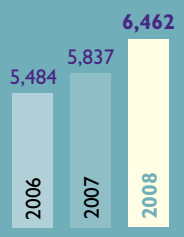
Visit **www.rsagroup.com** for more information. This Annual Report and Accounts contains forward looking statements as defined in the US Private Securities Litigation Reform Act of 1995. For a discussion of factors that could affect future results, reference should be made to the 'Important disclaimer' on the inside back cover. Pages 1 to 35 constitute the business review of RSA and are incorporated by reference into the directors' report set out on pages 41 to 43. The directors' report has been drawn up and presented in accordance with, and in reliance upon applicable English Company Law and the liabilities of the directors in connection with that report shall be subject to the limitations and restrictions provided by such law.

HIGHLIGHTS

2008 HAS BEEN ANOTHER STRONG YEAR.

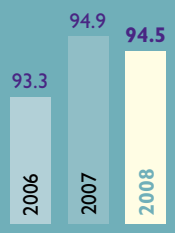
NET WRITTEN PREMIUMS
£6,462m

+11%



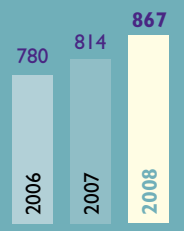
COMBINED OPERATING RATIO

94.5%



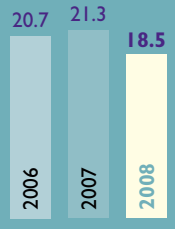
OPERATING RESULT
£867m

+7%



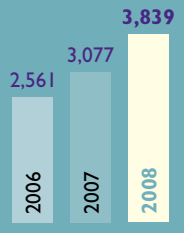
UNDERLYING RETURN ON EQUITY

18.5%



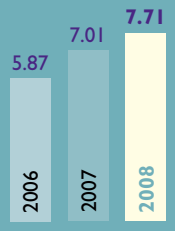
SHAREHOLDERS' FUNDS
£3,839m

+25%



DIVIDEND
7.71p

+10%



Combined operating ratio (COR): The ratio of claim costs and expenses (including commission) to premiums

RSA AT A GLANCE

OUR STRONG AND DIVERSIFIED PORTFOLIO IS BALANCED BETWEEN ATTRACTIVE MATURE MARKETS AND EMERGING MARKETS WITH HIGHER GROWTH POTENTIAL

INTERNATIONAL

INTERNATIONAL COMPRISES OUR BUSINESSES IN THE MATURE MARKETS OF SCANDINAVIA, CANADA, IRELAND AND ITALY.

Scandinavia represents 53% of the International portfolio and 25% of the RSA Group. Codan in Denmark and Trygg-Hansa in Sweden are the third largest insurers in their respective markets. We also have a growing presence in Norway and a Marine business in Finland.

In Canada, we are the sixth largest general insurer. Johnson, our direct business, is Canada's second largest affinity writer and we are well positioned in the Broker channel.

In Ireland, we are a pure intermediated business and a leading provider of Household insurance.

Our Italian business is focused primarily in the north of the country, distributing through a network of non-tied agents and brokers, and this year we continued to grow ahead of the market.

NET WRITTEN PREMIUMS
£m

£2,998m

1,602	SCANDINAVIA
884	CANADA
512	OTHER EUROPE

UK

WE ARE THE UK'S LARGEST COMMERCIAL INSURER AND THIRD LARGEST PERSONAL LINES INSURER.

Our Commercial business writes Property, Motor, Liability and Marine insurance. The business has a strong reputation for technical excellence. We are the UK's largest Property and second largest Liability and Motor insurer and a leading Marine underwriter.

Our Personal business is the third largest in the UK, and writes business through the broker, direct and affinity channels. MORE TH>N®, our direct business has around 2.6 million covers in place, providing Household, Motor, Travel and Pet insurance. We are the UK's second largest Household and fourth largest Motor insurer. Our affinity business provides a range of insurance products to the retail customers of our corporate partners.

NET WRITTEN PREMIUMS
£m

£2,711m

1,615	COMMERCIAL
1,096	PERSONAL

EMERGING MARKETS

EMERGING MARKETS OPERATES ACROSS 20 DEVELOPING INSURANCE MARKETS AND IS RSA'S FASTEST GROWING REGION.

Latin America is the largest business in Emerging Markets with operations in seven countries. The largest is in Chile, where we are the market leader, and we are also the largest private insurer in Uruguay.

We are the largest general insurer in the Baltics with leading market positions in Latvia and Lithuania.

We operate in four countries across the Middle East, and service the Asian region through commercial hubs in China, Hong Kong and Singapore and through our associate, Royal Sundaram in India.

Intouch, our business in Central and Eastern Europe has market leading direct operations in Poland, Russia and the Czech Republic.

NET WRITTEN PREMIUMS
£m

£738m

393	LATIN AMERICA
186	BALTICS
159	ASIA & MIDDLE EAST

Chairman's statement

A STRONG AND FOCUSED BUSINESS

WE ARE PLEASED WITH OUR 2008 RESULTS AND CONFIDENT OF A CONTINUING STRONG RELATIVE PERFORMANCE IN 2009.

I am pleased to report on another year of further improvement for our Company despite increasingly difficult market circumstances. In summary:

- a growth in net written premiums of 11%
- a 13% increase in pre-tax profits
- a combined operating ratio of 94.5%
- a strengthened balance sheet and robust capital position.

We have delivered on a statement made last year that we believed that we had "the experience and control processes to operate effectively in what we expected to continue to be difficult and demanding market environments" and that we could deliver "a relative increase in profit and strategically enhance our market positions where we choose to operate".

The main sources of profit growth were increased net written premiums up 11% with growth in all regions and continuing cost and efficiency gains. The largest contributors were International and Emerging Markets with strong growth helped by the relative currency changes. This reflects some of the strategic benefits of our geographically diverse Group.

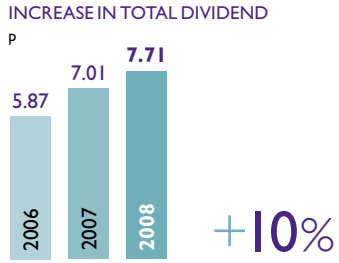
In all markets we continue to take the right action on rate and cost and delivered our planned expense savings target of £200m by mid 2008. We announced new targets with our preliminary results for further cost savings of £70m to ensure we can deliver competitively priced products and maintain our profitability in all markets where we choose to operate.

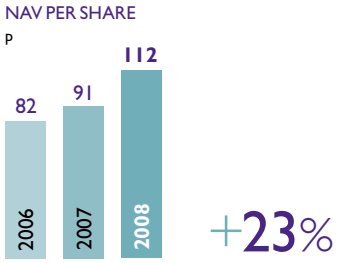
The common theme behind our results has not changed, namely management excellence in strategic, operational and financial performance in all our businesses. We continue to review and improve our control environment in the pricing of risk and underwriting disciplines with sustainable profitable performance linked to prudent reserving and a low risk investment strategy. This approach remains unchanged and will continue.

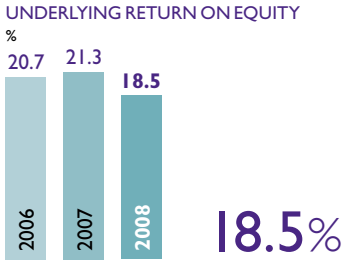
There have been understandable demands for increased regulation following the issues in the banking sector. This from time to time can give concerns about over generalised, untargeted and disproportionate responses. Our policy remains to seek to cooperate positively with all regulators in an open, joint way and help develop improved industry practice. There remain important external regulatory issues including agreement on Solvency II to ensure that any changes to the financial services arrangements are proportional and risk based as they relate to general insurance.

We did not get all our 2008 predictions right. The relatively large downward swing in interest rates, inflation and the relative weakness of Sterling was not forecast. The persistence of these trends has led us to go back to the original shareholder approved rate of return range for LTIP shares which we adjusted upwards on a voluntary basis last year. More generally, our philosophy of closely aligning management reward structures with the longer term interests of shareholders remains. The events of the past 12 months are certain to drive change in the structure and nature of reward for senior executives. Whatever these changes, we will maintain the strong link to performance and the focus on sustainability of results that underpin our existing culture.

The main variable moving forward is the likely impact of lower interest rates on predicted investment income. There are other less predictable trends in the rate of fall of economic growth in various economies. Our general response is to continue to seek management







excellence in what we do at all management levels and in all functions. We have an ongoing programme of review and continuous improvement in all our management disciplines. We continue to invest in operational and technical excellence and progress our extensive management development programmes, which are a key contributor to our progress.

There is no role for complacency in 2009. We continue to raise our management performance and plan to improve even further. It is an area of comparative strength for our Company and the best contingent action against any adverse circumstances. As a result we remain well positioned to take advantage of market opportunities as they rise.

In summary therefore we are pleased with our 2008 results and confident of a continuing strong relative performance in 2009 despite expecting some inevitable decline in the investment return. Against that background we are confident in recommending an increase in the final dividend to 7.71p, giving a total increase for 2008 of 10%.

I would like to take this opportunity to thank on behalf of shareholders, all our RSA colleagues, the management team ably led by our Chief Executive Andy Haste and my Board colleagues for their commitment, support and dedication on which all results depend. Finally I look forward to seeing as many of you as possible at the AGM and introducing a new RSA director, Johanna Waterous, who joined us in the year and has become an effective contributor to the RSA Board.

John Napier
Chairman

'THE COMMON THEME BEHIND OUR RESULTS HAS NOT CHANGED, NAMELY MANAGEMENT EXCELLENCE IN STRATEGIC, OPERATIONAL AND FINANCIAL PERFORMANCE IN ALL OUR BUSINESSES.'

John Napier
Chairman

Group CEO's review

CONTINUED DELIVERY

IN A YEAR OF CHALLENGING TRADING CONDITIONS AND VOLATILE INVESTMENT MARKETS, WE HAVE ONCE AGAIN DELIVERED STRONG RESULTS AND HAVE STRENGTHENED THE GROUP'S NET ASSET AND REGULATORY CAPITAL POSITION.

2008 has been another strong year for the Group. In a year of challenging trading conditions and volatile investment markets, we have again delivered a strong and profitable performance.

Across the Group we have continued to take the right action on rate and expenses. We have achieved good growth in shareholders' funds and our capital position remains healthy, with significant surpluses on both an economic and regulatory basis.

These results continue to demonstrate the positive impact of our tight operational and financial management and the benefit of the Group's strong and diversified portfolio.

STRONG PERFORMANCE IN CHALLENGING CONDITIONS

In 2008 we increased net written premiums by 11% to £6.5bn, reflecting our disciplined approach in the UK and continued growth in International and Emerging Markets.

The combined operating ratio (COR) for the Group was 94.5%. The underwriting result increased by 38% to £384m with the expected strong contribution from International.

The investment result was £594m (2007: £629m) and included an 11% increase in investment income to £654m, offset by a lower level of total gains (£32m compared with £119m in 2007). This is a good result and the Group continued to benefit from its low risk investment strategy.

Given the strong investment and underwriting performance, the operating result increased by 7% to £867m, while profit before tax increased by 13% to £759m.

Profit after tax was £586m. This compares with £628m last year which benefited from the release of £103m of deferred tax provisions in Codan.

Underlying return on equity remained strong at 18.5%. Net asset value per share increased by 23% to 112p, and by 15% to 101p excluding the pension fund surplus.

'WE REMAIN CONFIDENT OF CONTINUING TO DELIVER SUSTAINABLE PROFITABLE PERFORMANCE AND WE ARE WELL POSITIONED TO TAKE ADVANTAGE OF MARKET OPPORTUNITIES.'

Andy Haste
Group CEO

REGIONAL OVERVIEW

INTERNATIONAL

International again delivered a strong top and bottom line performance. Net written premiums increased by 19% to almost £3bn (6% on constant exchange) driven by growth in Canada, Scandinavia and Other Europe. We increased the underwriting profit by 27% to £262m, and the COR was 91.2%.

£m	2008	2007	2006
NET WRITTEN PREMIUMS	**6,462**	5,837	5,484
UNDERWRITING RESULT	**384**	278	310
OPERATING RESULT	**867**	814	780
COMBINED OPERATING RATIO (%)	**94.5**	94.9	93.3
UNDERLYING RETURN ON EQUITY (%)	**18.5**	21.3	20.7

In Scandinavia, it has been an outstanding year. The buyout of the minorities was the right thing to do and the business has performed strongly in attractive markets. Premiums were up by 16% to £1.6bn (3% at constant exchange) reflecting good growth in Commercial, particularly in Denmark and Norway.

In Denmark we grew our SME book by around 6%, Marine by 10%, and Renewable Energy by almost 60% (all figures on constant exchange). In Norway we signed a further 10 agents during the year and achieved strong growth with Commercial premiums up by 65% on constant exchange.

The underwriting result was up by 64% to £190m, with a COR of 88.3%, over 3 points better than last year. This was driven primarily by a strong performance from Sweden.

The rating environment across Scandinavia remains stable and we continue to put rate through the book with single digit increases across most lines.

In May 2008, we announced plans to double the Scandinavian expense savings to £50m and achieve an expense ratio of around 14% by mid 2010. As a result of the actions we have already taken, we are well on our way to achieving both targets.

In Canada, premiums increased 26% to around £900m (15% on constant exchange), driven by strong organic growth and the strong performance of CNS which was acquired in December 2007. The integration of CNS is on track. We have consolidated our product range and all new business is on the RSA platform. Broker loyalty remains high and customer retention was very good at 80%.

Johnson, our direct personal business, finished the year strongly with premiums increasing by 24% (14% on constant exchange), reflecting the acquisition of TJV in 2007 and good growth in affinity. We signed 35 new sponsorship groups during the year, giving us access to around 240,000 potential new customers.

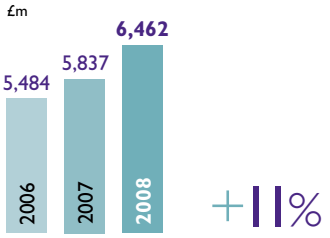
In Personal lines, we increased rate in Household by 7% and Motor by 4% and we have seen continued evidence that the market's hardening. In Commercial, we have maintained our discipline. Motor pricing is back in positive territory, with Property held flat and only minor reductions in Liability.

The underwriting profit of £57m and COR of 92.9% are good results and were achieved despite the severe winter storms and increased large losses.

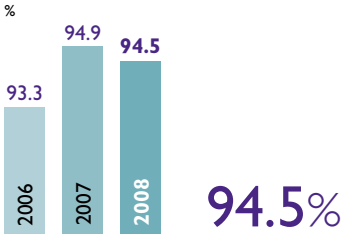
In Other Europe, premiums increased by 19% to £0.5bn (2% on constant exchange) and the COR was 97.1%. Italy continued to grow ahead of the market and premiums increased by 3% on constant exchange, driven by growth in Personal Motor. We also continued to build distribution, signing 37 new agents in 2008.

In Ireland, the market remained competitive and premiums were in line with 2007.

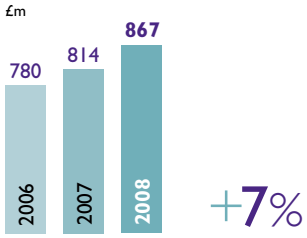
INCREASE IN NET WRITTEN PREMIUMS



COMBINED OPERATING RATIO



OPERATING RESULT



Group CEO's review continued

We withdrew capacity in areas such as Motor Fleet and Solicitors' Professional Indemnity and this was offset by growth in affinity and our recent acquisitions.

We have also taken action on rate, increasing it by 6% in Personal lines and between 2% and 7% across Commercial lines.

We also completed the domestication of our Irish business, establishing it as a separate legal entity. This company started writing Group business in 2009, taking advantage of Ireland's lower tax regime.

UK

The UK market remains competitive and we are maintaining our strategy of targeting profitable growth, putting rate through where required and withdrawing capacity where we cannot achieve our target returns.

Premiums increased by 1% to £2.7bn reflecting our disciplined approach to growth. The COR was 97.6%, with the benefit of improved weather offset by increased large losses.

In Personal, premiums were up 2% to £1.1bn. MORE TH>N® continued to perform well, with premium growth of 2%. New business sales increased by 10% while lower mortgage originations and new car sales continued to impact affinity volumes.

In Commercial, overall premiums were in line with 2007 at £1.6bn, with strong growth in specialty lines, including Risk Solutions which increased by 9%, Marine by 13% and targeted growth in Commercial Fleet. This offset the withdrawal of capacity in lines of business such as Liability and small and mid corporate Property where we could not achieve our target returns.

Overall retention remained strong at around 80%.

We continued to take action on rate, increasing Personal Motor rates by 6% and Household by 5%, and Commercial rates by 6% in Liability, 7% in Property and 8% in Motor. Across the market we are starting to see more consistent rating action from major competitors.

The underwriting result was £99m, with the expected lower level of prior year development and increased large losses partially offsetting the benefits of improved weather.

At our year end results, we announced a new £70m expense savings target for the UK to be delivered by mid 2010, primarily through a reduction in headcount of 1,200. There will be a one off cost of £80m to deliver this, which will be treated as a reorganisation cost in 2009 and will not be included in the Operating Result. The savings will be at full run rate by mid 2010 and together with other actions, we are targeting an expense ratio of around 14% by the end of 2012.

EMERGING MARKETS

In Emerging Markets, we again delivered strong growth. Premiums increased by 20% to over £0.7bn (7% at constant exchange) and increased by 26% (12% at constant exchange) after excluding Venezuela, which we sold in December 2007. The underwriting result increased by 28% to £23m with a COR of 96.4%, reflecting continued positive contributions from Asia and the Middle East, Latin America and the Baltics.

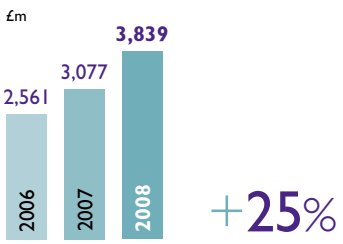
In terms of the economic outlook, as expected we have seen the impact of the economic downturn. We planned for it and have taken action on expenses to protect profitability, including reducing headcount by around 400 which represents around 10% of the Emerging Markets' workforce.

In the Baltics, premiums increased by 21% (4% at constant exchange) and while growth has slowed as a result of economic conditions, we have taken action to protect profitability.

In Asia and the Middle East, we delivered another excellent result. Premiums increased by 43% (30% on constant exchange) with strong growth in UAE Motor and Construction and Engineering.

We also achieved two significant regulatory milestones. In the Kingdom of Saudi Arabia, we were granted our Royal Decree so we can proceed with our IPO and in China we received approval to establish our branch in Beijing.

In Latin America, premiums increased by 22% (10% on constant exchange) with double digit increases across Chile, Brazil, Argentina and Colombia.



Our associates in India and Intouch in Eastern Europe maintained good momentum and premiums increased by 37% to £140m (25% on constant exchange). In India our business performed strongly. We have grown ahead of the market and expanded our agency network by around 2,700 new agents.

Intouch has market leading direct operations in Poland, the Czech Republic and Russia, and in February 2009, we announced plans to acquire the remaining 50% of the business.

Across the region, we are successfully implementing our affinity strategy and in 2008 we signed deals with 47 retailers and financial institutions.

These markets remain attractive with good growth potential, and we are on track to meet our target of increasing Emerging Markets' net written premiums to £1bn by the end of 2010.

STRONG FINANCIAL POSITION

We continue to benefit from our low risk investment strategy. 90% of the total investment portfolio is invested in high quality fixed income and cash assets. The fixed interest portfolio remains concentrated on high quality short dated assets, with 99% of the bond portfolio investment grade, and 83% rated AA or above. The bond holdings are well diversified geographically, with 74% invested in assets other than Sterling and 48% invested in non government bonds. During 2008, the investment portfolio increased by 11% to £14.7bn.

Our high quality investment portfolio and underwriting discipline have driven our strong capital position.

Shareholders' funds increased by 25% to £3.8bn, primarily reflecting after tax profits, foreign exchange and the increase in the pension fund surplus. The IGD surplus increased by 13% to £1.7bn, representing coverage of 2.5 times the requirement.

INDUSTRY OVERVIEW

IN WHAT WAS AN EXTREMELY CHALLENGING YEAR FOR FINANCIAL SERVICES, 2008 HIGHLIGHTED THE IMPORTANCE OF HAVING A FOCUSED BUSINESS MODEL, WITH HIGH LEVELS OF CONTROL AND TRANSPARENCY.

The economic environment deteriorated markedly in 2008. Growth decelerated sharply in most economies and unemployment began to rise. The speed and extent of the global slowdown prompted aggressive action from central banks and national governments. Interest rates were cut to historically low levels and substantial capital injections were provided to businesses regarded as essential to national economies. The banking sector, in particular, attracted considerable support. Despite these actions, expectations for global economic activity remain poor in the near term.

The rapidly weakening economy caused substantial downward pressure on financial markets with equity, corporate bond and property values falling sharply. Complex financial securities or structures were marked down particularly aggressively. Declining asset prices have weighed heavily on the insurance sector, particularly life companies, which have a high exposure to risk assets.

Against the backdrop of a weakening economy, RSA has performed strongly, due to the focused and geographically diversified nature of our business model, coupled with firm action taken on rate. Equally, the high quality and transparent nature of our investment portfolio has meant that we have not suffered unduly from market volatility.

Given the extent of the financial crisis and the high degree of government intervention which has resulted, policymakers are engaged in active debate over the appropriate nature of the future regulatory environment. We look forward to working with the European Union institutions on the follow up to the De Larosière high level group discussions on financial supervision which has considered the issues from an EU perspective.

It is critical that policymakers ensure that any future regulatory regime remains proportionate and supports sectors which continue to be healthy, such as general insurance. It is also important that the response to the banking crisis does not delay progress on important legislative proposals such as Solvency II, which presents significant opportunities for UK insurers that could help the future growth and stability of the industry.

RSA is keen for the EU governments to reach agreement on this legislation as soon as possible in order to end uncertainty and allow time for considered implementation. In the UK we will be monitoring the progress of the Banking Bill to ensure that the impact of changes to the Financial Services Compensation Scheme as regards general insurers is proportionate and risk-based.

Group CEO's review continued

TECHNICAL CAPABILITIES

We continue to build and expand our technical capabilities. We appointed Peter Jackson as our new Group Sales Director, responsible for building and managing RSA's relationships with key global brokers. As a global insurer, listening and working with our global broker partners and making it easier for them to do business with us is key to what we do and this appointment will strengthen that.

We also continue to focus on developing employees throughout the business and at all levels through our major initiatives:

- Our Technical Academy which we launched in 2006 to develop the next generation of talent, now has over 10,000 members across the Group in the core disciplines of claims, actuarial and underwriting
- The Executive Development Programme is now entering its fifth year, bringing together leaders from across the Group to work collaboratively on critical strategic issues
- Our Graduate and FastTrack programmes involved thirty new employees in 2008 providing structured support and career paths for new starters and high potential individuals.

We have continued our focus on employee engagement. 86% of employees participated in our revised Employee Survey and we will use the insights to generate ideas and clear action plans to make changes across our business.

CORPORATE RESPONSIBILITY

We take our impacts on society and the environment seriously, behaving ethically as individuals and as a company. As an insurer, we aim to ensure customers are protected from social and environmental risks, such as climate change.

We are committed to providing innovative ways of addressing those needs and emerging risks, including:

- The provision of energy performance management services for commercial customers, advising them how to reduce energy consumption, costs and CO_2 emissions; and
- Our Canadian home insurance, which provides supplementary coverage to help customers develop more eco-friendly homes.

We also remain focused on addressing our own internal impacts.

In 2008, our Irish business became carbon neutral for the first time, joining our UK business, with a newly constructed HQ designed to best practice construction and design standards.

We also launched our responsible procurement programme in the UK, assessing 96 of our suppliers on how they are tackling corporate responsibility issues and investigating how we can work together to address social and environmental issues in our supply chain.

Our employees also continued to participate actively in our corporate responsibility programme. During 2008, building on the success of the UK National Volunteer Week held in 2007, we launched similar programmes across Canada, Scandinavia and our Asia and Middle East businesses. For the first time employees were actively encouraged to help local communities during work hours with 7,250 volunteers taking part in Community activity across the Group. This approach ensures an engaged workforce, actively involved with our local communities.

In recognition of our progress, we were pleased to be nominated as a 'Gold' rated 'Times Top 100 Company that Counts', to be included in the ethical investor fund the Dow Jones Sustainability Index for the first time and to be awarded the Investor Relations Society award for Corporate Responsibility.

CONFIDENT OUTLOOK

We have once again delivered strong results in challenging conditions. With our strong balance sheet, our management actions and diversified portfolio, we are delivering sustainable profitable performance.

In 2009, we will continue to operate a high quality, low risk investment strategy. The investment result will be impacted by lower interest rates and continued investment market volatility, however we will continue to take action to mitigate this impact. These actions and the geographic diversification of the portfolio will limit the full impact of falling yields, and in 2009 we expect investment income to be around 2007 levels. Total gains will continue to be impacted by any further negative market movements in commercial property values as well as financial market volatility, and we are not anticipating a positive contribution from total gains in 2009.

We will maintain our focus on underwriting discipline and targeted profitable growth. We are seeing signs of economic downturn across the Group, however, we are also seeing rates beginning to harden in a number of our key markets and we continue to take action on rate and expenses. And as we announced with our full year results, we expect to deliver a combined operating ratio for 2009 of around 95%.

We remain confident about the outlook for the Group and we are well positioned to take advantage of market opportunities.

Andy Haste

Andy Haste
Group CEO

Group strategy

OUR STRATEGY

OUR STRATEGY IS BASED ON A DISCIPLINED APPROACH TO DELIVERING STRONG, SUSTAINABLE RETURNS AND OUR STRATEGIC PRIORITIES ARE:

STRONG ANNUAL EARNINGS	TARGETED PROFITABLE GROWTH	OPERATIONAL EXCELLENCE

OUR STRONG AND DIVERSIFIED PORTFOLIO AND FOCUS ON OPERATIONAL AND FINANCIAL MANAGEMENT ARE KEY TO DELIVERING THESE STRATEGIC PRIORITIES.

STRONG & DIVERSE PORTFOLIO

We derive real advantage from being a pure P&C insurer. Our focus on doing one thing and doing it well is evident in our attention to detail, rigorous control and our actions.

We have strong market positions in attractive markets and a balanced portfolio of businesses.

The shape of the portfolio is deliberate:

- Our geographic balance gives us exposure to markets at different points in the cycle and different stages of development
- It allows us to shift capacity to where we see the best opportunities
- In each of our markets there are opportunities for profitable growth.

TIGHT OPERATIONAL MANAGEMENT

We have a clearly defined risk appetite and have exited volatile lines.

We have strong underwriting controls, from ensuring that every one of our underwriters is licensed, through to quarterly in depth portfolio and reserve reviews. Together with our market leading technical skills, these controls ensure that we are taking the right risks at the right rate.

Our commitment to underwriting discipline and taking the right action on rate is clearly evident in our results.

We have a relentless focus on operational excellence and have a strong track record of delivering on our expense savings targets.

STRONG FINANCIAL MANAGEMENT

The sustainability of our earnings is underpinned by our strong financial management.

We maintain a conservative reinsurance programme to minimise volatility in our earnings from large losses and catastrophe events.

Our investment portfolio is well diversified, high quality and low risk. This is evidenced by the resilience of the portfolio during 2008, where, in spite of volatile financial markets the portfolio performed strongly and increased in value.

We have a prudent reserving policy and hold a significant margin over the best estimate of our liabilities. We therefore expect positive prior year reserve development to be an ongoing feature of our results.

Our balance sheet is strong, with shareholders' funds increasing by 25% in 2008. We hold strong regulatory and economic capital surpluses, as well as sufficient capital to maintain our financial strength ratings and pursue our bolt on acquisition strategy.

Group strategy continued

PROGRESS AGAINST STRATEGIC PRIORITIES

STRATEGIC PRIORITIES

STRONG ANNUAL EARNINGS

AREAS OF FOCUS

- Our strong portfolio allows us to shift capacity to where we see the best returns
- We have a tightly controlled risk appetite and underwriting process, and a conservative reinsurance policy
- We are committed to underwriting discipline and taking the right action on rate
- We have a prudent reserving policy, high quality investment portfolio and a strong balance sheet.

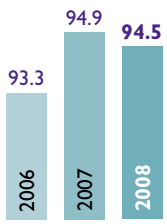
PROGRESS IN 2008

7% INCREASE IN OPERATING RESULT

In 2008, the Group delivered another strong performance with a 0.4pt improvement in the COR to 94.5% and, against the backdrop of volatile financial markets, a strong investment result. This result highlights the strength and diversity of our portfolio, our actions on rate and expenses, and the benefits of our high quality, low risk investment strategy.

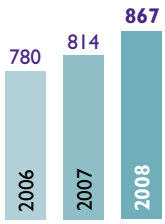
KEY PERFORMANCE INDICATORS

COMBINED OPERATING RATIO
%



94.5%

OPERATING RESULT
£m



£867m

2009 PRIORITIES

CONTINUE TO DELIVER SUSTAINABLE PROFITABLE PERFORMANCE

We expect to deliver a COR of around 95%. We are seeing signs of economic downturn, however alongside our rating and expense actions, we are seeing rates beginning to harden in our key markets. On investments we will benefit from geographic diversification and will continue to take action to mitigate against lower interest rates, and in 2009, expect to deliver investment income in line with 2007 levels.

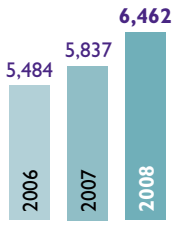
TARGETED PROFITABLE GROWTH

- We target growth in profitable lines of buiness and withdraw capacity from areas of the market where we cannot achieve our target returns
- We are using our strong customer focus to develop targeted propositions and maximise retention
- Our focus on customer differentiation for our partners and their customers is driving growth in our affinity business
- Across the Group, we have benefited from expanding distribution as well as targeted acquisitions.

4% GROWTH IN NET WRITTEN PREMIUMS

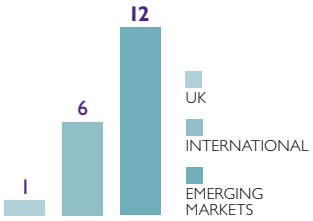
Net written premiums are up 4% on a constant exchange basis, reflecting 12% growth in Emerging Markets (adjusted for the sale of Venezuela), 6% growth in International, and 1% in the UK, our most competitive market. This growth reflects our positive rating action, organic growth in target segments and the benefits of the acquisitions made in 2007.

NET WRITTEN PREMIUMS
£m



£6,462m

GROWTH IN NET WRITTEN PREMIUMS (CONSTANT EXCHANGE)
%



4% growth

ALLOCATE CAPACITY TO TAKE ADVANTAGE OF POSITIVE RATING TRENDS

Our overriding focus remains taking the right action on rate and ensuring that we will only grow where it is profitable to do so. We will therefore continue to actively allocate capacity to maximise returns and look to take advantage of market opportunities in terms of positive rating trends and acquisitions.

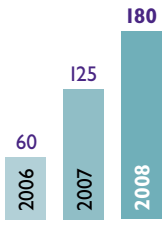
OPERATIONAL EXCELLENCE

- We maintain relentless focus on operational excellence and deliver on our expense savings targets
- Our technical skills are market leading and a source of real competitive advantage. We are investing in these skills through our Technical Academy and global development programmes
- We continue to attract top talent from both inside and outside the insurance industry. We have instilled a strong performance culture and over 90% of our employees have their pay linked to their performance.

£200M EXPENSE SAVINGS DELIVERED AHEAD OF SCHEDULE

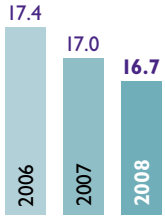
In mid 2008 we delivered our Group expense savings targets of £200m and have made good progress towards achieving the additional £25m expense savings target set in Scandinavia. These savings are to be achieved by mid 2010 and will double Scandinavia's expense savings to £50m and reduce the expense ratio to around 14%.

EXPENSE SAVINGS – IN YEAR P&L BENEFIT
£m



£180m

EXPENSE RATIO
%



16.7%

£70M ADDITIONAL SAVINGS TO BE DELIVERED IN THE UK BY MID 2010

In February 2009, we announced a new UK expense savings target of £70m to be delivered by mid 2010. This will be achieved primarily through a reduction in headcount of 1,200, and together with other actions, we are targeting a UK expense ratio of around 14% by the end of 2012.

Business review

INTERNATIONAL
CNS – BUILDING IN CANADA

The 2007 acquisition of CNS marked a £37 million investment in our Canadian broker business and made us the largest general insurer in British Columbia and the sixth largest in Canada.

Our focus has been to build on CNS' strong local service delivery and leverage RSA's technical expertise and capacity to strengthen our broker and customer propositions. As a result, we are well positioned to continue to grow profitably in the important British Columbian market.

The integration is progressing well. We have consolidated our product range and all new business is now processed on the RSA platform. The CNS brand has been updated and has a new, modern look and feel consistent with the RSA brand. Through these and other innovations we have positioned the business to continue delivering profitable growth.

In 2008 CNS contributed almost 10% of Canada's premiums and has helped the Canadian business continue to outperform the competition.

For more information visit www.cns.ca.

Business review

INTERNATIONAL

INTERNATIONAL HAS DELIVERED ANOTHER STRONG PERFORMANCE, WITH A 19% INCREASE IN NET WRITTEN PREMIUMS AND A 27% INCREASE IN THE UNDERWRITING RESULT.

£m	2008	2007
NET WRITTEN PREMIUMS	**2,998**	2,513
UNDERWRITING RESULT	**262**	206
COMBINED OPERATING RATIO (COR) (%)	**91.2**	91.3

BUSINESS OVERVIEW

International comprises the Group's operations in Scandinavia, Canada, Ireland and Italy. These businesses have strong positions in these attractive markets and we aim to outperform in terms of both growth and profitability.

KEY STRATEGIES

We are committed to delivering sustainable profitable performance. We are using three levers to drive the business forward and outperform the competition:

- Delivering profitable growth by focusing on profitable segments, expanding distribution and selected acquisitions
- Leveraging our market leading capabilities in underwriting and claims; and
- Driving continuous operational efficiencies across the business.

Our geographic spread and segmented approach enables us to target growth in profitable segments where our technical expertise gives us competitive advantage.

Customer focus is central to our propositions and we are optimising customer reach through our multi channel distribution strategy, with strong intermediary, affinity and direct propositions.

We delivered our increased target of £60m of annualised expense savings by mid 2008, and made good progress towards achieving the additional £25m expense savings target set for Scandinavia this year. These savings are to be achieved by mid 2010 and will double Scandinavia's expense savings to £50m and reduce the expense ratio to around 14%.

'WITH OUR STRONG TOP AND BOTTOM LINE PERFORMANCE, WE ARE CONTINUING TO DRIVE THE GROUP FORWARD.'

Simon Lee
Chief Executive, International businesses

PROGRESS AGAINST KEY STRATEGIES

International continues to drive the Group forward and has again delivered a strong top and bottom line performance. Net written premiums are up 19% to £2,998m (6% on constant exchange). International contributed the majority of the Group's underwriting result, with a 27% increase in underwriting profit to £262m and a COR of 91.2%.

SCANDINAVIA

Scandinavia represents over 50% of the International portfolio and 25% of the RSA Group. We are the third largest insurer in both Denmark and Sweden and are expanding our presence in Norway and Finland. In 2008, premiums increased by 16% to £1,602m (3% on constant exchange) and the COR improved by 3.1 points to 88.3% driven primarily by a strong performance in Sweden, particularly in Personal lines.

Commercial performed strongly, delivering a 19% increase in net written premiums to £727m (5% on constant exchange). This reflects good growth in Norway, and in SME, Marine and Renewable Energy in Denmark.

In Personal lines, premiums are up 14% to £875m (1% on constant exchange) reflecting continued growth from WLI in Norway and good retention across the region.

CANADA

Canada has delivered another excellent performance, net written premiums are up 26% to £884m (15% on constant exchange), and the underwriting result is up 14% to £57m. Profitability remains strong with a COR of 92.9% (2007: 92.4%) despite adverse weather, with some of the worst winter storms in Ontario for almost 70 years.

Commercial net written premiums increased by 19% to £217m (9% on constant exchange) reflecting the CNS acquisition in December 2007 and continued strong retention. The integration of CNS is on track and the business is performing well, with 80% of business retained.

Personal net written premiums increased by 28% to £667m (18% on constant exchange). Growth in Personal Intermediated reflects positive rate, strong retention and the addition of CNS. Johnson is Canada's second largest affinity writer and represents 40% of our Canadian business. In 2008, Johnson continued to perform strongly, delivering 24% growth (14% on constant exchange), reflecting the benefit of the TJV acquisition in 2007 and the signing of 35 new sponsorship groups, giving us access to a potential 240,000 new customers.

OTHER EUROPE

In Other Europe, which comprises our operations in Ireland and Italy, premiums are up by 19% to £512m (2% on constant exchange). The COR of 97.1% (2007: 89.1%) reflects the impact of the floods in Ireland as well as the exceptional level of prior year development in 2007.

In Italy, we continue to grow ahead of the market with premiums up 3% on constant exchange reflecting growth in Personal Motor and increased distribution, with 37 new agents signed this year.

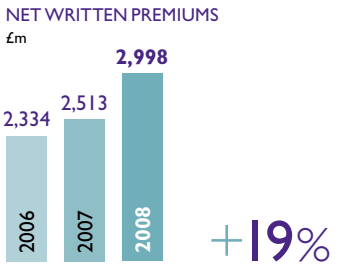
In Ireland, the market remains competitive and we are continuing to act on rate. Premiums are in line with last year, with growth in our affinity business and recent acquisitions offsetting the withdrawal of capacity in areas such as Fleet and Solicitors' Professional Indemnity. We also completed the domestication of our Irish business, establishing it as a separate legal entity. This company started writing Group business in 2009, taking advantage of Ireland's lower tax regime.

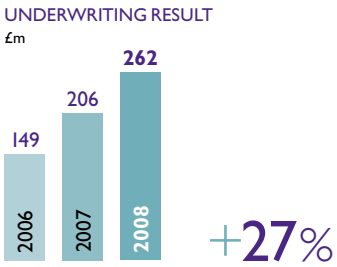
MARKET CONDITIONS

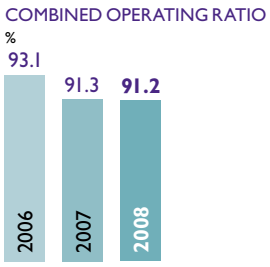
In Scandinavia, the rating environment remains stable and we continue to achieve single digit rate increases across most lines. In Canada, we are seeing continuing evidence that the Personal market is hardening, and although Commercial remains competitive, we are starting to see an improving trend. The Irish market remains competitive, while the Italian insurance market contracted over 2008 reflecting lower levels of economic activity.

OUTLOOK

We have built a track record of delivering strong top and bottom line performance. Although economic conditions will present some challenges in 2009, we are seeing positive rating trends in our markets, and with our ongoing actions on expenses and our strong portfolio, we are confident that we will continue to deliver sustainable profitable performance.







Business review

UK
TARGETED GROWTH IN MARINE INSURANCE

Marine insurance is an important part of RSA's heritage and one of our key specialty lines. We are one of the largest Marine underwriters in the UK and our market leading technical skills provide real competitive advantage.

We have been steadily expanding our Marine business with innovative products, such as New Aquaculture for the growing fishfarming industry, as well as bespoke solutions for Port & Terminal operators. We've also expanded geographically, establishing specialist insurance teams in Belgium, Brazil, China, Dubai, France, Germany, The Netherlands and Singapore.

With these initiatives and our investment in specialist teams, we have expanded our Marine business by more than 70% since 2003, with strong customer retention and a consistent track record, and have delivered more than 20 successive quarters of positive underwriting results.

Our performance has been recognised through a number of awards, such as the British Insurance Awards 'Underwriter of the Year' in 2005 and Lloyd's List Marine 'Insurer of the Year' in 2008.

Business review

UK

THE UK HAS DELIVERED ANOTHER STRONG PERFORMANCE IN A COMPETITIVE MARKET, WITH NET WRITTEN PREMIUMS OF £2.7BN AND AN UNDERWRITING RESULT OF £99M.

£m	2008	2007
NET WRITTEN PREMIUMS	2,711	2,688
UNDERWRITING RESULT	99	65
COMBINED OPERATING RATIO (COR) (%)	97.6	97.6

BUSINESS OVERVIEW

We are the UK's largest Commercial insurer. We are the largest in Commercial Property and the second largest in Motor and Liability and a leading Marine underwriter. We are the UK's third largest Personal lines insurer, with the number two position in Household and number four in Motor.

KEY STRATEGIES

We are committed to delivering sustainable profitable performance. We will only write business that is profitable and are driving growth in segments where we can achieve our target returns. We are committed to underwriting discipline and actively withdraw capacity in areas of the market where the rate, terms and conditions do not meet our underwriting criteria.

In Commercial we are focusing on specialist segments, such as Risk Solutions and Marine, and leveraging our technical expertise to develop innovative risk solutions and strengthen our broker proposition to deliver profitable growth and manage retention in our target markets.

In Personal, we are using increased customer segmentation and pricing sophistication to launch innovative products and marketing initiatives to acquire new customers and build retention. Our reputation for delivering quality affinity propositions for our partners and their retail customers is attracting new deals and helps us retain existing partnerships.

We achieved our target of £120m of annualised expense savings by mid 2008 and have committed to delivering a further £70m of savings by mid 2010. With these and other actions, we are targeting an expense ratio of around 14% by the end of 2012.

PROGRESS AGAINST KEY STRATEGIES

We are maintaining our strategy of targeting profitable growth, taking the right action on rate and selective capacity withdrawal. Total premiums are up 1% to £2,711m. Retention remains strong at around 80% across the portfolio. The underwriting result is £99m (2007: £65m), with the expected lower level of prior year development and increased large losses partially offsetting the benefits of improved weather.

COMMERCIAL

In Commercial, premiums are in line with last year at £1.6bn, with strong growth in specialty lines, including Risk Solutions which is up 9%, Marine up 13% and targeted growth in Commercial Fleet offsetting the withdrawal of capacity in lines of business such as Liability and small and mid corporate Property.

'WITH OUR CONTINUED ACTION ON RATE AND EXPENSES, WE ARE CONFIDENT THAT THE UK BUSINESS WILL CONTINUE TO DELIVER SUSTAINABLE PROFITABLE PERFORMANCE.'

Adrian Brown
UK Chief Executive

We have continued to take action on rate, achieving increases of 6% in Liability, 7% in Property and 8% in Motor.

The COR was 99.3% (2007: 95.9%), with adverse large loss experience and lower prior year development reducing the Property and Casualty results, however, this has been offset by good profitability in Marine and in our Legacy operations.

In 2008 we expanded our Risk Solutions European business and opened a new office in Munich. This was followed by the opening of our office in Madrid in February 2009, increasing the number of our European operations to six.

PERSONAL

In Personal, premiums are up by 2% at £1.1bn, reflecting a good performance from MORE TH>N® with 2% premium growth, while, as expected, affinity volumes continue to be impacted by lower new car sales and mortgage originations. The COR was 95.0% compared with the 2007 result of 100.6% which was impacted by the summer floods.

We have achieved consistent increases in rate, with Personal Motor rates up by 6% and Household by 5%.

We are continuing to build the MORE TH>N® brand with a series of marketing campaigns and new propositions. During the year, MORE TH>N® won Finaccord's 'Most Effective Brand' and was a finalist at the British Insurance Awards for E-business and Customer Care.

In affinity, we signed two new deals and retained four existing partnerships that renewed during the year.

TECHNICAL CAPABILITIES

Our technical skills are market leading and a real source of competitive advantage. In 2008, we won Insurer Innovation of the Year at the Insurance Times awards for our Energy Performance Management Proposition, which helps our customers meet Government requirements for Energy Performance Certificates. In addition, our rehabilitation programme, RSA Care, won the Rehabilitation Award at the British Insurance Awards.

MARKET CONDITIONS

The UK market remains competitive, however, we are now starting to see early signs of positive rating trends. While we are beginning to see the impact of the economic downturn on premium volume with a slowdown in business activity in Commercial and lower mortgage originations and new car sales in Personal, this is expected to be partially offset by higher rates.

In Commercial, we are increasingly seeing clients and brokers looking at the security and quality of companies where they place business and with our strong balance sheet and reputation for technical excellence, we are well positioned. There are also signs of the market showing a more disciplined approach to rate and greater resistance to high levels of broker commission.

The Personal market remains competitive, although we are now seeing some improving trends on rate and evidence of an increase in discipline from our major competitors. The influence of aggregators continues to grow and they are an increasing source of business for us. Our approach is to focus on working together with aggregators to create value over the long term. We also anticipate that the current economic environment may result in more affinity deals coming to the market.

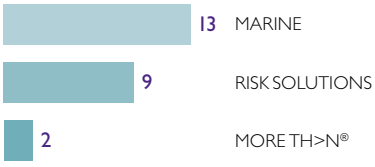
OUTLOOK

We are committed to maintaining underwriting discipline and targeted profitable growth. While the economic downturn is impacting premium volumes, we are seeing signs that rates are beginning to harden, which should partially mitigate this. In addition, with our continued action on rate and our programme to deliver an additional £70m of expense savings by mid 2010, we are confident that the UK business will continue to deliver sustainable profitable performance.

UK NET WRITTEN PREMIUM 2008
%

35	MOTOR	12	CASUALTY
21	HOUSEHOLD	8	MARINE
21	PROPERTY	3	OTHER

TARGETED PROFITABLE GROWTH
%



Business review

EMERGING MARKETS
GROWING IN AFFINITY

RSA Seguros is the market leader in Chile with 16% market share, employing over 500 people. In 2008 we grew by 16%, slightly faster than the market and achieved a combined operating ratio of 92.3%.

In 2008, Affinity was one of our key drivers of growth with premiums increasing by 12%. One of our most established relationships is with Falabella, a leading retail group and a powerful brand in Latin America.

In Chile, Falabella has over 400 outlets including supermarkets, department and home improvement stores and financial services retailers and has around three million active card holders.

We provide Falabella with a dedicated relationship manager and support team to ensure that we provide a high standard of service to them and their customers.

In October we launched a number of loyalty campaigns aimed at strengthening retention and, as a result, we've seen retention rates increase by 25% over average 2007 levels.

Business review

EMERGING MARKETS

EMERGING MARKETS IS OUR FASTEST GROWING REGION AND IN 2008 DELIVERED 20% GROWTH IN NET WRITTEN PREMIUMS. WE REMAIN ON TRACK TO DELIVER OUR TARGET OF INCREASING PREMIUMS TO £1BN BY THE END OF 2010.

£m	2008	2007
NET WRITTEN PREMIUMS	**738**	615
UNDERWRITING RESULT	**23**	18
COMBINED OPERATING RATIO (COR) (%)	**96.4**	95.3

BUSINESS OVERVIEW

Emerging Markets has operations in 20 countries across Latin America, the Baltics, Asia and the Middle East and Central and Eastern Europe. We are the number one insurer in Chile and in the Baltics, the largest private insurer in Uruguay and Intouch, our business in Central and Eastern Europe, has market leading direct operations in Poland, the Czech Republic and Russia.

KEY STRATEGIES

We are focused on delivering profitable growth through expanding distribution, disciplined underwriting and improving operational performance. Our strategy is to focus on markets where we can establish a meaningful presence, either in overall market share or in segments where we have a competitive advantage. We are committed to strong governance and control, as well as close co-operation across the region to develop customer solutions which can be replicated in relevant territories cost effectively.

We are focusing on Motor, Affinity, Large & Complex Risks and Small and Medium Enterprises (SME).

Motor is 45% of the portfolio and is a significant driver of growth and profitability. We are leveraging the Group's expertise to improve our pricing and claims capability to give us competitive advantage in the markets in which we operate.

Affinity is a significant opportunity given the scale of the populations in markets such as Brazil and India. It is a route to customers who have not previously been able to purchase

'THESE ARE ATTRACTIVE MARKETS, WITH GOOD LONG TERM POTENTIAL AND WE REMAIN ON TRACK TO DELIVER AN INCREASE IN EMERGING MARKETS' PREMIUMS TO £1BN BY THE END OF 2010.'

Paul Whittaker
CEO of Emerging Markets

insurance and can provide much needed simple, low cost products. We are working with utility companies, among others, to cost effectively access these large markets using their existing billing systems.

For Large & Complex risks, we have implemented a hub and spoke approach, where regional centres of excellence assist our smaller operations underwrite complex risks, combining RSA's global technical expertise with local knowledge. This has significant cost advantages over employing technical experts in all locations.

SMEs have historically been underserved by brokers due to the high cost to service small individual policies; however in countries such as India, this customer segment represents a significant opportunity. By offering simple, standard products with policies that can be issued after answering a handful of questions, we plan to simplify the broker sales process and access the potential of this market.

PROGRESS AGAINST KEY STRATEGIES

In Emerging Markets, premiums are up by 20% to £738m (7% on constant exchange) and up by 26% (12% on constant exchange) after excluding Venezuela, which we sold in December 2007. The underwriting result is up 28% to £23m and the COR was 96.4% (2007: 95.3%).

In the Baltics, premiums are up by 4% on constant exchange and, while growth has slowed as a result of economic conditions, we have taken action on rate and expenses to protect profitability.

Asia and the Middle East again performed strongly with a 43% increase in premiums (30% on constant exchange) with strong growth in UAE Motor and Construction and Engineering. We are making good progress on our expansion plans in China and recently received approval to establish a new branch in Beijing. We have also received our Royal Decree in the Kingdom of Saudi Arabia which enables us to proceed with the IPO of our Saudi business.

Latin America delivered a 22% increase in premiums (10% on constant exchange) after adjusting for the sale of Venezuela, reflecting good double digit growth across Chile, Brazil, Argentina and Colombia.

Our associates in India and Central and Eastern Europe continue to build momentum, and premiums are up by 37% to £140m (25% on constant exchange). In India, the business has performed strongly, growing ahead of the market and increasing the agent network by 2,700.

Across the region, we are successfully implementing our Affinity strategy and in 2008 we signed deals with 47 retailers and financial institutions.

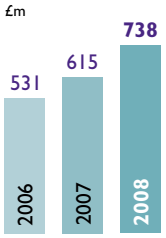
MARKET CONDITIONS

We are seeing the impact of economic downturn in a number of our markets and, in response, we have taken a number of actions on expenses to protect profitability, including reducing headcount by around 400 across the region, representing around 10% of the total Emerging Markets' workforce.

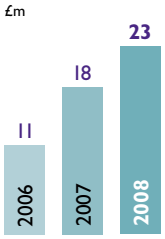
OUTLOOK

2009 will be a challenging year and we expect to see a continued slowdown in growth as a result of economic conditions across a number of our markets. However, we will continue to take action to protect profitability. As insurance penetration is low across our areas of strategic focus, there remain good opportunities for profitable growth. These are attractive markets, with good long term potential and we remain on track to increase Emerging Markets' premiums to £1bn by the end of 2010.

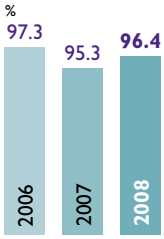
NET WRITTEN PREMIUMS



UNDERWRITING RESULT



COMBINED OPERATING RATIO



Financial review

ANOTHER STRONG YEAR

ANALYSIS OF RESULT
MANAGEMENT BASIS

£m	2008	2007	Movement* (%)
NET WRITTEN PREMIUMS	**6,462**	5,837	11
UNDERWRITING RESULT	**384**	278	38
INVESTMENT RESULT	**594**	629	(6)
INSURANCE RESULT	**978**	907	8
OTHER ACTIVITIES	**(111)**	(93)	(19)
OPERATING RESULT	**867**	814	7
OTHER MOVEMENTS	**(126)**	(122)	(3)
PROFIT/ (LOSS) ON DISPOSALS	**18**	(22)	182
PROFIT BEFORE TAX	**759**	670	13
TAX	**(173)**	(29)	(497)
PROFIT AFTER TAX FROM CONTINUING OPERATIONS	**586**	641	(9)
LOSS AFTER TAX FROM DISCONTINUED OPERATIONS	**–**	(13)	–
PROFIT AFTER TAX	**586**	628	(7)
COMBINED OPERATING RATIO (%)	**94.5**	94.9	0.4pts
SHAREHOLDERS' FUNDS	**3,839**	3,077	25

* Reported exchange rate

RESULTS OVERVIEW

In a year of challenging trading conditions and volatile investment markets, we have once again delivered strong results and have strengthened the Group's net asset and regulatory capital position. These results continue to demonstrate the positive impact of our tight operational and financial management and the benefit of the Group's strong and diversified portfolio.

NET WRITTEN PREMIUMS

Net written premiums are up 11% to £6.5bn (4% on constant exchange), representing good underlying growth and the benefits of foreign exchange in International and Emerging Markets, and a disciplined approach in the UK.

OPERATING RESULT

The operating result is £867m (2007: £814m), reflecting an improved underwriting result partially offset by a lower investment result, due to the expected reduced level of total gains.

UNDERWRITING RESULT

The underwriting result is up by 38% to £384m (2007: £278m) and represents another strong performance, with a current year underwriting profit of £93m (2007: underwriting loss £70m) and a prior year profit of £291m (2007: £348m). The improvement in the current year result

'OUR OBJECTIVE IS TO DELIVER SUSTAINABLE PROFITABLE PERFORMANCE AND THIS IS CLEARLY EVIDENT IN THE GROUP'S CONTINUED DELIVERY OF STRONG RESULTS.'

George Culmer
Chief Financial Officer

reflects the continued benefits of management actions, while improved weather (£155m better than 2007) was offset by adverse large loss experience (£110m worse than 2007), primarily in the UK. The strong prior year result reflects continued positive run off from all three regions.

The Group continues to adopt a prudent reserving policy for both current year and overall reserves and at 31 December 2008 reserves remain significantly to the right side of best estimate.

INVESTMENT RESULT (TABLE 1)

The Group continues to maintain a low risk investment strategy with the portfolio dominated by high quality fixed income and cash assets. The investment result is £594m (2007: £629m), and reflects increased investment income offset by the expected decrease in total gains from £119m in 2007 to £32m.

Investment income is up 11% to £654m, reflecting action taken to lock in higher bond yields as well as foreign exchange gains of £40m. The average underlying yield on the portfolio (excluding the yield on the ADC funds withheld account) was 4.6% (2007: 4.4%).

Total gains were £32m (2007: £119m) and comprise gains on the equity hedges of £141m and on equity and bond sales of £68m, offset by mark to market movements on commercial property of £98m, on CDO's of £12m and on other assets of £10m. Impairments totalled £61m and include £43m on equities and £18m on bonds.

In 2008, we took a number of actions to enhance yield on the bond portfolio, including selling low yielding government bonds and reinvesting at longer duration to take advantage of higher yields. In addition, we purchased a net £600m of high quality, well diversified non government securities. The net purchases of non government bonds were at an average credit rating of AA-, well diversified by sector and were spread over more than 100 names. These actions are consistent with our high quality, low risk investment strategy and we have maintained the overall high credit quality of the portfolio. In 2009, we will continue to be a cautious purchaser of high quality non government credit and selectively extend duration.

In addition, the portfolio benefits from being well diversified geographically, with over 70% of the bond portfolio invested in currencies other than Sterling. While most of these markets are also seeing interest rate reductions, this has been offset by foreign exchange gains.

Going forward, investment income will be impacted by lower interest rates. However, with the actions we are taking to lock in higher yields and the geographic diversification of the portfolio we expect to limit this, and in 2009, we expect investment income to be around 2007 levels.

Total gains will continue to be impacted by any further negative market movements in commercial property values as well as financial market volatility. If the FTSE 100 remains at around 4,000 throughout 2009, the value of the equity hedges is estimated to be £40m, while total impairments are estimated to be between £40m and £60m. The value of commercial property is expected to broadly track the IPD index, and as it stands today, we are not anticipating a positive contribution from total gains in 2009.

TABLE 1: ANALYSIS OF INVESTMENT RESULTS

	12 months 2008 £m	12 months 2007 £m	Movement %
BONDS	478	391	+22
EQUITIES	50	48	+4
CASH AND CASH EQUIVALENTS	57	83	(31)
LAND AND BUILDINGS	16	17	(6)
OTHER	53	52	+2
INVESTMENT INCOME	654	591	+11
REALISED GAINS	150	174	(14)
UNREALISED GAINS/(LOSSES), IMPAIRMENTS AND FOREIGN EXCHANGE	(118)	(55)	(115)
TOTAL GAINS	32	119	(73)
UNWIND OF DISCOUNT INCLUDING ADC	(92)	(81)	(14)
INVESTMENT RESULT	594	629	(6)

OTHER ACTIVITIES

Expenses from other activities for 2008 have increased by £18m to £111m and include £19m (2007: £4m) in respect of our investment in our associates in India and Central and Eastern Europe.

OTHER MOVEMENTS AND PROFIT ON DISPOSALS

Other movements comprises interest costs of £108m and amortisation of £18m. Interest costs are £108m, up from £104m, with the increase reflecting repo activity and the foreign exchange impact on interest payments on our Euro denominated bonds. Amortisation of £18m (2007: £18m) was charged in respect of renewal rights and on acquired claims provisions. Profit on disposal is £18m (2007: loss of £22m) and predominantly comprises the recycling of foreign exchange on the liquidation of a French subsidiary.

TAXATION

The tax charge is £173m compared with £29m in 2007, which included the release of £103m of deferred tax provisions in respect of the Scandinavian security funds. The 2008

Financial review continued

charge represents an effective tax rate of 23% and includes a 3% benefit from the transfer of a portion of the Swedish profits into the Swedish Security Fund.

PROFIT AFTER TAX

Profit after tax is £586m and the underlying Return on Equity remains very strong at 18.5%.

DIVIDEND

The directors will recommend at the Annual General Meeting, to be held on 18 May 2009, that a final ordinary dividend of 4.98p (2007: 4.53p) per share be paid. This, together with the interim dividend of 2.73p paid on 28 November 2008, will make the total distribution for the year 7.71p (2007: 7.01p).

CASHFLOW (TABLE 2)

The Group's operating cashflow has increased by 20% to £780m benefitting from strong operational cash flows and the disposal of Group occupied properties. Tax paid of £101m is £26m lower than 2007, primarily due to the timing of statutory instalments in Scandinavia and Canada. Interest paid increased by £15m to £107m, reflecting repo activity and the foreign exchange impact on the Euro bonds. Group dividends have increased by £70m to £181m, due to the dividend increase and the lower take up of scrip dividend in 2008. The pension funding payment of £37m is part of our pension scheme asset reallocation strategy. The issue of share capital and corporate activity in 2007 primarily related to the purchase of the Codan minorities. Corporate activity in 2008 of £101m includes a number of small acquisitions in the UK and International, further capital investment in our associates and the disposal of run off books in the UK and Scandinavia.

BALANCE SHEET

Our balance sheet and capital position are strong, and the Group has sufficient capital to meet its strategic objectives and financing commitments. In 2008, the Group's shareholders' funds increased by 25% to £3.8bn, primarily reflecting after tax profits, foreign exchange, and the increase in the pension fund surplus.

TABLE 2: CASHFLOW – MANAGEMENT BASIS

	12 months 2008 £m	12 months 2007 £m
OPERATING CASHFLOW	**780**	652
TAX PAID	**(101)**	(127)
INTEREST PAID	**(107)**	(92)
GROUP DIVIDENDS	**(181)**	(111)
DIVIDEND TO MINORITIES	**(8)**	(31)
NET CASHFLOW	**383**	291
ISSUE OF SHARE CAPITAL	**19**	304
PENSION ASSET REALLOCATION FUNDING	**(37)**	(86)
NET MOVEMENT OF DEBT	**(2)**	223
CORPORATE ACTIVITY	**(101)**	(888)
CASH MOVEMENT	**262**	(156)
REPRESENTED BY:		
DECREASE IN CASH AND CASH EQUIVALENTS	**(91)**	(352)
PURCHASE OF OTHER INVESTMENTS	**353**	196
	262	(156)

INVESTMENT PORTFOLIO (TABLE 3)

The investment portfolio increased by 11% to £14,727m over the year, with foreign exchange gains of £1,611m and other positive movements of £71m offset by mark to market movements of £233m. The foreign exchange benefit reflects the appreciation of the Canadian Dollar, the Euro, the Danish Krone and the Swedish Krona against Sterling. The mark to market movement on the bond portfolio is a positive £304m, and the movement on equities a negative £363m. The movement on equities is partially offset by the £141m gain on the equity hedges, which is recognised in total gains.

90% of the total investment portfolio is invested in high quality fixed income and cash assets. The fixed interest portfolio remains concentrated on high quality short dated assets, with 99% of the bond portfolio investment grade, and 83% rated AA or above. The bond holdings are well diversified, with 74% invested in currencies other than Sterling, and 48% invested in non government bonds (2007: 45%). The average duration is 2.7 years for the Group, and 2.0 years in the UK.

The non government bond portfolio of £5.6bn comprises £1.8bn of Scandinavian Mortgage Bonds, £2.2bn of other financials and £1.6bn of non financials. The Scandinavian Mortgage Bond portfolio comprises £1.2bn of Swedish bonds, which are all rated AAA, and £0.6bn of Danish bonds, which are principally rated Aaa. The average duration on the Scandinavian Mortgage Bond portfolio is 2.6 years with an average LTV of 50-60%. Within the £2.2bn of other financial exposure, £0.6bn is in supranational and sovereign backed entities, £0.3bn in other non bank financials and £1.3bn in banks. Of the £1.3bn in banks, just £320m of this is subordinated debt and only £90m is Tier 1, the vast majority of which is in Canadian banks with only £10m in the UK.

Equities (excluding preference shares and Collective Investment Vehicles backed by fixed income and cash) comprise 5% of the portfolio. We have hedged our equity exposure for the past 4 years and around 75%

TABLE 3: MOVEMENTS IN THE INVESTMENT PORTFOLIO OVER 2008

	Value 31/12/2007 £m	Foreign exchange £m	Mark to market £m	Other movements £m	Value 31/12/2008 £m
GOVERNMENT BONDS	5,333	743	261	(326)	6,011
NON GOVERNMENT BONDS	4,248	604	43	736	5,631
CASH	1,509	167	–	(62)	1,614
EQUITIES	1,132	32	(363)	(21)	780
PROPERTY	429	27	(98)	7	365
PREFS & CIVS	355	21	(78)	(138)	160
OTHER	272	17	2	(125)	166
TOTAL	13,278	1,611	(233)	71	14,727

of this exposure remains hedged with a rolling programme of put and call options, providing protection down to a FTSE level of 2,825.

The commercial property portfolio is only 2% of investment assets and comprises high quality commercial properties and does not include any development properties. The Group's CDO exposure is £81m, and includes £76m of CLOs which have experienced no downgrades.

At 31 December 2008, unrealised gains were £263m (31 December 2007: £461m).

CAPITAL POSITION

At 31 December 2008, the Group held an Insurance Group's Directive (IGD) surplus of £1.7bn, an increase of £0.2bn from 2007. The improvement in IGD surplus is mainly attributable to the profits for the year and positive foreign exchange movements, offset by the dividend, unrealised investment losses and an increase in the capital requirement in line with business growth. The coverage ratio remains very strong at 2.5 times (31 December 2007: 2.5 times). A further 30% fall in the FTSE from the year end level of around 4,400 would reduce the IGD surplus by an estimated £0.2bn.

At 31 December 2008, the Group had surplus economic capital of around £1.8bn, based on a risk tolerance consistent with Standard & Poor's (S&P) long term A rated bond default curve. This is equivalent to a probability of solvency over 1 year of 99.94%.

The Group calculates its economic capital position using a global multi year stochastic economic capital model and the 2008 surplus has been calculated to fully reflect current lower asset values and lower current and future investment returns. The model is a key decision making tool and is used for a range of strategic, operational and financial management purposes throughout the Group, and has also been the basis for the Group's Individual Capital Assessment (ICA) submissions to the FSA since 2004.

The ICA is a forward looking economic assessment of the capital requirements of the Group based on our assessment of the risks to which we are exposed. The Group has received its Individual Capital Guidance from the FSA, which at the request of the FSA remains confidential.

Our financing and liquidity position is strong. Our committed £455m senior facility remains undrawn and matures in 2013. The next call on external financing is on the €500m subordinated guaranteed bonds in October 2009.

RATING AGENCIES

S&P, AM Best and Moody's Investor Service provide insurance financial strength ratings for the Group and its principal subsidiaries.

The Group is currently rated A, stable outlook by S&P. The Group was upgraded by Moody's to A2 stable outlook in December 2008, and by AM Best to A (Excellent) in February 2009.

PENSION FUND

The surplus on the pension scheme as at 31 December 2008 is £363m compared with £116m at the start of the year. The movement is due to the increase in discount rate for the UK schemes from 5.6% to 6.2% (which includes an allowance for current pricing of financial corporate bonds) and the change in the inflation assumption from 3.2% to 2.8%.

The assets in the pension funds performed strongly over the year, reflecting the defensive asset mix, with only 22% invested in equities.

The Group uses medium cohort assumptions for mortality, using PFA92 and PMA92 tables. The life expectancy of a male pensioner aged 60 is assumed to be 25.8 years and 27.0 years for a female pensioner.

SUMMARY

Our objective is to deliver sustainable profitable performance and this is clearly evident in the Group's continued delivery of strong results.

Our strong balance sheet and tight management of the business, including our relentless action on rate and expenses and low risk investment strategy ensures that the Group is well positioned to continue to manage the competitive rating environment, challenging economic conditions and volatile investment markets.

We remain confident of the Group continuing to deliver sustainable profitable performance and this is reflected in the 10% increase in the 2008 final dividend and our expectation of delivering a COR of around 95% in 2009.

George Culmer
Chief Financial Officer

RISK FRAMEWORK

OVERALL RISK FRAMEWORK

The Group operates under an enterprise risk management framework that is designed to identify, assess, measure and manage exposure to risk. This process is subject to continuous review and development and further work was undertaken in 2008 to enhance the framework.

RISK MANAGEMENT

The Board is responsible for the Group's systems of risk management.

Executive management has the responsibility for establishing and implementing appropriate systems and controls in their own areas of remit. The Group Risk Management Framework provides the mechanism through which risk management and control is embedded throughout the Group. Each Group business is required to follow a consistent process to identify, assess, manage and monitor their key risks.

GROUP RISK APPETITE

The Group has a process for setting risk appetite at both Group and regional level and for monitoring compliance with this. The Group risk appetite sets business volumes for certain higher risk insurance classes, stipulates loss retention limits, reinsurance protection, targets for credit rating and solvency margins, and other appropriate measures.

There is a formal escalation process for potential or emerging risks that are outside the risk appetite.

RISK FRAMEWORK

The Group has continued to adopt the '3 lines of defence' governance model. The framework for the oversight and management of risk is as follows:

- Management – the first line of defence in setting strategy, performance measurement, establishment and maintenance of internal control and risk management in the business
- Risk assessment – the second line, operating a formal risk management framework within which the Group policies and minimum standards are set and objective oversight and challenge of risk management across the Group is achieved. This includes the Board Risk Committee, supported by the Group Risk functions, and a Group wide network of regional risk committees
- Independent assurance – the third line of defence, providing independent and objective assurance of the effectiveness of the Group's systems of internal control established by the first and second lines of defence. This is the Group Audit Committee, supported by Group Internal Audit.

GROUP RISK POLICY STATEMENTS

Group risk policy statements set out the minimum standards to be maintained by the Group's operations in order to manage their risks in a way that is consistent with the risk appetite. Business managers are responsible for complying with Group and local risk policies and for managing risk by taking mitigating actions where risks are outside the appetite. The Board Risk Committee's oversight and challenge role includes consideration of risk mitigation.

Compliance with policy statements is mandatory. Policies are subject to regular review in order to reflect changes in circumstances and the Group risk appetite.

RISK CATEGORIES

Within the Group the risk elements are viewed under headings that broadly correspond to those used in the Financial Services Authority's Prudential Sourcebook for Insurers (INSPRU), and Senior Management Arrangements, Systems and Controls (SYSC). Additional information is provided in the Risk Management section on page 79 to the financial statements. Details of some of the key current practices, tools and other arrangements for each risk category are set out below.

INSURANCE RISK

The Group's general insurance activities are primarily concerned with the pricing, acceptance and management of risks arising from our contracts with customers. The management of the underwriting and claims risks uses a number of key tools, including the review of the performance and management of all the individual insurance portfolios throughout the Group, and the investigation of potential emerging insurance risks.

Further work has been undertaken in 2008 to refine and improve the Portfolio Classification process, designed to provide a more effective method of evaluating portfolio performance. We are continuing to improve risk oversight and supporting tools to ensure that we remain in control of our insurance business and the risks within it.

Claims development and reserving levels are closely monitored by Reserve Committees. Each region's Reserve Committee determines a recommended level of outstanding claims reserves, in accordance with the Group Reserving Policy. The Group Reserving Committee considers the reasonableness of these recommendations. It then determines the level of aggregate outstanding claims reserves to be carried by the Group.

REINSURANCE RISK

The Group's reinsurance strategy and appetite are set and agreed by the Board Risk Committee and published and disseminated via the Group reinsurance policy statement. The Group Reinsurance Credit Committee oversees the implementation of the counterparty credit aspects of this strategy. The reinsurance team monitors and controls reinsurance activity throughout the Group and has responsibility for the purchase of the Group's worldwide programme of treaties. All major treaty purchases are analysed using various sophisticated modelling tools to ensure that the level of cover purchased is capital efficient and aligned with Group risk appetite and strategy.

OPERATIONAL RISK

Operational risk exists in every facet of the organisation, including those areas that are not viewed as 'operating units'. As such, all areas of the Group and its major outsourcing providers, are involved in addressing and controlling operational risk.

The Group uses a suite of risk tools to help manage operational risk using a common categorisation of risk. These tools include Risk and Control Self Assessments, Key Risk Indicators, Scenario Analyses, Incident Management and Loss Reporting.

A series of forward looking key risk indicators are used to assess potential future trends in operational risks, whilst data collected on actual operational risk incidents and 'near misses' captures past experiences. In addition, the use of scenario analyses enables the Group to assess whether certain operational events that have occurred elsewhere could manifest themselves within the Group. When taken together, the tools provide a complementary set of indicators of the Group's operational risk profile.

CREDIT, MARKET AND LIQUIDITY RISKS

The primary sources of credit risk within the Group are investment and treasury activities and reinsurance counterparty risk. Within the investment management and treasury activities, a range of bank counterparty concentration and credit quality limits, together with other controls, are in place to ensure that exposure is managed within the Group risk appetite. New reinsurance cover is placed with reinsurers that are authorised as Approved Reinsurance Counterparties recommended by the Group Reinsurance Credit Committee under criteria approved by the Board Risk Committee.

Market risk arises from the Group's investment portfolios. The Global Asset Management Committee is the management committee that oversees the Group's investment strategy under the oversight of the Investment Committee, and operating within risk limits set by the Board Risk Committee.

Liquidity risk is considered to be a low risk category. Group liquidity is managed by Group Treasury and each operation is required to maintain a minimum level of cash or cash equivalents or highly liquid assets that can be liquidated within a maximum stated period of time. Contingency funding plans are prepared and monitored to ensure that these minimum levels are met even in stress conditions.

REGULATORY RISK

The Group operates in a number of geographical locations with diverse regulatory requirements. Internationally, the regulatory environment has become more complex and demanding. The Group continues to respond to these developments through its arrangements for regulatory compliance and by ensuring that it maintains open and cooperative relationships with its regulators.

PRINCIPAL RISKS AND UNCERTAINTIES

In this section we set out the principal risks and uncertainties to delivering our strategy, together with the actions we are taking to minimise the likelihood that these will occur and any potential impact on the future performance of the business.

1. PROLONGED ECONOMIC DOWNTURN IN OUR KEY MARKETS NEGATIVELY IMPACTS PREMIUM GROWTH AND INCREASES CLAIMS FREQUENCY

We will maintain our focus on underwriting discipline and targeted profitable growth. In addition, the Group benefits from the actions taken to de-risk the underwriting portfolio over the past five years, and as a result, we have very limited exposure to economically triggered contracts. We have a suite of indicators in place to monitor for any emerging trends in claims frequency, which allow us to take early corrective action. These include early indicators of fraudulent claims and we have also strengthened resources in this area.

We have seen some impact on premiums as a result of lower levels of commercial and personal activity, including lower new car sales and mortgage originations, and have identified a limited number of contracts triggered by economic conditions. This impact is being partially offset by rates beginning to harden in a number of our key markets and an observed decline in claims inflation, for example, in rebuilding costs and replacement motor vehicles. In addition, we continue to take action on rate and expenses. We expect to deliver a combined operating ratio of around 95% in 2009.

2. ADVERSE FINANCIAL MARKETS AND LOWER INTEREST RATES IMPACT THE INVESTMENT PORTFOLIO AND INVESTMENT INCOME

The Group operates a low risk investment policy, with the investment portfolio dominated by short dated, high quality fixed income and cash assets. The prudent nature of the Group's investment strategy has been

Risk framework continued

evidenced by the resilience of the portfolio during 2008, where, in spite of increased market turbulence, the portfolio increased in value.

90% of the total investment portfolio is invested in high quality fixed income and cash assets. The fixed interest portfolio remains concentrated on high quality short dated assets, with 99% of the bond portfolio investment grade, and 83% rated AA or above. The bond holdings are well diversified, with 74% invested in currencies other than Sterling, and 48% invested in non government bonds and the average duration on the total bond portfolio is 2.7 years.

At the year end, only 5% of the portfolio was invested in equities (excluding preference shares and Collective Investment Vehicles backed by fixed income and cash). The equity exposure has been hedged for the past 4 years, and currently, around 75% of this exposure is hedged with a rolling programme of put and call options, providing protection down to a FTSE level of 2825. The commercial property portfolio is only 2% of investment assets and comprises high quality commercial properties and does not include any development properties.

The investment portfolio is routinely monitored to ensure compliance with counterparty concentration and credit limits and that all exposures are within the Group's risk appetite.

Investment income will be impacted by lower interest rates. In 2008, we took a number of actions to enhance yield on the bond portfolio, including selling low yielding government bonds and reinvesting at longer duration to take advantage of higher yields. In addition, we purchased a net £600m of high quality, well diversified non government securities. The net purchases of non government bonds were at an average credit rating of AA-, well diversified by sector and were spread over more than 100 names. These actions are consistent with our high quality, low risk investment strategy and we have maintained the overall high credit quality of the portfolio.

As noted above, the portfolio benefits from being well diversified geographically, with over 70% of bonds invested in currencies other than Sterling. While most of these markets are also seeing interest rate reductions, this has been offset by foreign exchange gains.

In 2009, we will continue to operate a high quality, low risk investment strategy. The investment result will be impacted by lower interest rates and continued investment market volatility, however, we will continue to take action to mitigate this impact. These actions and the geographic diversification of the portfolio will limit the full impact of falling yields, and in 2009 we expect investment income to be around 2007 levels. Total gains will continue to be impacted by any further negative market movements in commercial property values as well as financial market volatility, and we are not anticipating a positive contribution from total gains in 2009.

3. RATING ENVIRONMENT SOFTENS SIGNIFICANTLY IN KEY MARKETS

The Group's overriding objective is to deliver sustainable profitable performance. Our strong and diverse portfolio provides exposure to markets at different stages of development at different points in the insurance cycle. We actively use the portfolio to shift capacity to where we see the best returns.

We are committed to underwriting discipline, with a relentless focus on profitability over volume and delivering on our expense savings targets.

We continue to invest in our technical skills and our sales and marketing capabilities. We target growth where it is profitable through specialist segmentation and focus on expanding in target trades and segments where our technical expertise gives us competitive advantage.

4. INSURANCE RISKS ARE ACCEPTED OUTSIDE THE GROUP'S RISK APPETITE OR BELOW TECHNICAL PRICE

The Group has strict underwriting limits in place to ensure that risk selection is within the Group's risk appetite. The Group's underwriters are licensed to only write risks within specified limits, based on the experience of each individual underwriter.

Quarterly portfolio reviews are carried out across the business, to assess the performance of each portfolio against key performance indicators. Key risk indicators are used to monitor emerging trends, opportunities and risks. Any portfolio that triggers a key risk indicator is flagged and investigated, with corrective measures implemented if required.

Quarterly audits of business won and lost ensure that risks accepted are priced to achieve target returns and that underwriting discipline is maintained.

5. ADVERSE LOSS EXPERIENCE THROUGH CATASTROPHIC LOSSES ARISING FROM AN INSURANCE EVENT OR SERIES OF EVENTS, INCREASING FREQUENCY AND SEVERITY OF LARGE LOSSES OR DETERIORATION IN LONG TAIL RESERVES

The Group's underwriting strategy is set centrally using risk aggregation models and limits to ensure that risks written are well diversified and are within the Group's risk appetite.

Quarterly portfolio reviews monitor underwriting performance, ensuring that risks accepted are within the Group's risk appetite and priced to achieve target returns. Emerging trends in large losses, frequency and severity are flagged and investigated.

The Group maintains a conservative reinsurance programme, which limits net losses to a specified amount each year.

In addition, the Group maintains a conservative reserving policy and claims reserves are set with the aim that, over the longer term, they will be more likely than not to result in positive prior year development.

CORPORATE RESPONSIBILITY

CORPORATE RESPONSIBILITY REMAINS FUNDAMENTAL TO THE WAY RSA CONDUCTS ITS BUSINESS AND THIS HAS BEEN PARTICULARLY IMPORTANT IN A YEAR OF TURBULENCE AND UNCERTAINTY FOR FINANCIAL SERVICES.

APPROACH AND GOVERNANCE

Behaving responsibly and ethically in the way we manage our business directly affects the environment, people and the communities in which we operate. We are committed to doing the right thing both as individuals and as a company.

We aim to make sure our approach is practical and focused on our main business impacts, delivering commercial benefits while recognising the value we add to society.

We focus on three key themes across the Group: the environment and climate change, safety and social inclusion. These issues have been identified as important by our customers, investors and employees. Forum for the Future, the sustainability charity who we ask to carry out an annual assessment, agree that we are focusing on the right issues.

The principles by which we operate the business and our brand beliefs underpin our commitments and our CR policies form an essential part of our broader risk and governance framework.

Responsibility for CR lies with the Group CEO, who chairs the bi-annual Group Executive Committee review of CR and annual review by the Board. Briefings and training on specific CR issues are given as they arise.

CR targets and objectives are included in CEO goals which are cascaded to direct reports and relevant business functions. All employees are assessed against the brand beliefs, which help to ensure that doing the right thing forms part of the performance and remuneration structure at RSA.

Our CR data, processes and external reporting are verified by the Corporate Citizenship Company (AA1000, GRI, ISAE3000) with an extra audit on the Group's carbon footprint forming part of our offsetting due diligence (GHG Protocol).

Our progress was recognised in 2008 by the award of the Investor Relations Society 'Best communication of CR', inclusion in the Dow Jones Sustainability Index (winner of 'Sector Mover') and being a 'Gold' rated 'Times Top 100 Company.'

Further information on our approach, governance and policies can be found at: **www.rsagroup.com/rsa/pages/responsibility/ourapproach**

CUSTOMERS

As an insurer, we play a vital role in helping people recover from sometimes catastrophic setback. Helping get their lives back on track is our first priority. Our response during the 2008 snowstorms, flooding and earthquake in China was to help our customers through our rapid claims response. Across RSA both employees and the business assisted others less fortunate through disaster relief.

Customer service is of critical importance to us and our Canadian business embodies this. Johnson is the leader out of 750 blue chip organisations around the world for the CMAT customer relationship management assessment. Our UK Personal Customer Management programme, provides customers with their own dedicated customer services manager, was pioneered in our Canadian business. It has now been rolled out to over 300,000 customers. This demonstrates our focus on the customer experience.

Product innovation is also key to our success and across the business we have created tailored and relevant products for specific customer groups. Social and environmental changes create new demands for insurance and we continue to develop insurance solutions that provide additional social or environmental benefits:

- In the UK, our Energy Performance Management Proposition won the Insurance Times insurer innovation category. The solution provides Energy Performance Certificates to support Government legislation to reduce CO_2 emissions
- We are the providers of a VanCity 'Purehome' insurance proposition through CNS in Canada. The policy provides supplemental coverage to upgrade your home with more environmentally sound alternatives for windows, heating systems, flooring, paints, energy efficient appliances and more
- RSA Marine in China is helping to provide solutions for the growing sector of aquaculture where 70% of world production is located.

We remain committed to clear and open communication with our customers, and to resolving any complaints promptly. This was reflected in our continued upper quartile performance in the Association of British

Insurers 2008 benchmark, which is 16% above the industry average.

BUSINESS PARTNERS

We work closely with our business partners and intermediaries to grow a successful business together while reducing our collective environmental and social impact. During 2008, in the UK we asked 96 of our suppliers about their management of these issues and engaged in active dialogue to improve standards.

In 2009, we will look to pilot this approach in Canada and Scandinavia building on our responsible procurement agenda and sector wide collaboration through the Financial Services Procurement Forum.

RESPONSIBLE INVESTMENT

The bulk of our UK equity assets continue to be managed by F&C Asset Management. F&C has one of the largest Governance and Sustainable Investment teams in Europe, enabling it to follow a policy of active engagement across its portfolios on environmental, social and governance issues. Last year F&C engaged with 902 companies on a wide range of issues from climate change to labour standards.

EMPLOYEES

A sustainable business needs to attract, develop and reward talented people, as well as giving responsibility and making them accountable for their actions. We continue to focus on developing employees throughout the business and at all levels through our major initiatives in 2008:

- Our Technical Academy now has over 10,000 members across the Group in the core disciplines of claims, actuarial and underwriting
- The Executive Development Programme is now entering its fifth year, bringing together leaders from across the Group to work collaboratively on critical strategic issues
- Our Graduate and FastTrack programmes supported thirty new employees in 2008 providing structured support and career paths for new starters and high potential individuals.

In 2008 we focused on employee engagement leveraging the insights from a revised Employee Survey. 86% of employees within RSA participated. The feedback obtained has been used to generate ideas and clear action plans to make changes across our business.

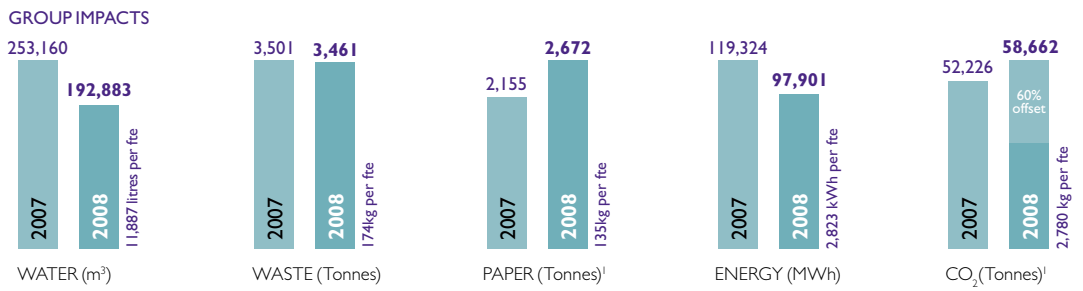
CLIMATE CHANGE & ENVIRONMENT

Climate change has continued to rise up the political agenda in 2008. As an insurer, any change in the intensity or frequency of extreme weather conditions is a significant issue.

We remain committed to engaging in the climate change debate and working closely with a range of forums; including in 2008 the insurance working group of the United Nations Environment Programme for Financial Institutions and the ABI ClimateWise initiative.

During 2008, we have focused on integrating our online environmental management system across our business. We achieved over 73% of our environmental targets across the Group for 2008. We will continue to set challenging targets and extend our approach across the Group.

Our Irish business became carbon neutral for the first time, joining our UK business in building on strong programmes of targets and operational energy efficiency improvements. All offsetting of equivalent emissions is made in renewable energy projects certified to the Voluntary Carbon Standard.



Note

Data covers 87.5% of RSA.

(1) Data includes additional Emerging Markets operations.

We are constantly improving and evolving our technology to assess risk for customers. Our flood risk assessment tool allows us to insure customers who might otherwise be excluded by assessing risk to the individual postcode level. We are partners in Eurotempest which allows a forecast of likely wind damage up to five days in advance of a storm.

We aim to make it more affordable for customers to make environmental choices through products and services such as our discounts for fuel efficient and alternative fuel vehicles and our customised environmental home insurance for the members of the UK charity the National Trust.

COMMUNITY

During 2008, building on the success of the UK National Volunteer Week held in 2007, we launched similar programmes across Canada, Scandinavia and our Asia & Middle East businesses. For the first time employees were actively encouraged to help local communities during work hours with 7,250 volunteers taking part in Community activity across the Group.

During 2009, we look forward to rolling out our volunteer programmes across our Latin American business to help local communities selected by employees.

Road safety continues to be a major issue for us as an insurer and we have continued to support road safety programmes around the world, most recently in Lithuania, Chile, Dubai and Sweden. In Denmark, we launched a new programme for children based on our successful programme in Sweden, donating over 2,000 reflective safety vests.

We donated over £2.2 million (2007: £2.3 million) in charitable donations in 2008, with over 13,039 volunteer hours donated. We also provided £1,000,026 in gifts in kind in the form of sports fields for three schools in London. Our focus continues to be helping issues which link to our business objectives and brand beliefs and where we are able to use our knowledge such as safety, environment and social inclusion to do the right thing.

For full details of progress please see the full Corporate Responsibility Report.

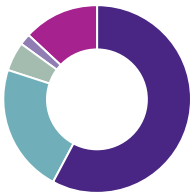
Environment targets 2009	% reduction
CO_2	
GROUP	1.5
UK	2.5
ENERGY	
UK (ELEC)	15
IRELAND (ELEC)	5
CANADA (ELEC)	3
TRAVEL	
DENMARK (AIR)	1[1]
DENMARK (CAR)	2[1]
SWEDEN (AIR)	1[1]
SWEDEN (CAR)	5[1]
IRELAND (AIR)	5
IRELAND (CAR)	5
UK (SHORT HAUL)	5[2]
WASTE & RECYCLING	
CANADA (WASTE DISPOSED)	2
CANADA (RECYCLING)	2
DENMARK (PAPER WASTE)	5[1]
IRELAND (WASTE DISPOSED)	10
UK (WASTE TO LANDFILL)	10
PAPER	
SWEDEN	5[1]
WATER	
UK	5

Note

All Canadian targets refer to RSA Canada only.

(1) For completion by 2010.
(2) For completion against a 2008 baseline.

CO_2 IMPACT
%



2	RAIL
13	AIR
58	ENERGY
22	ROAD
5	OTHER

CO_2 EMISSIONS BY REGION
%

12	EMERGING MARKETS
30	INTERNATIONAL
58	UK (INCLUDING CORPORATE CENTRE)

EXECUTIVE TEAM

ANDY HASTE
GROUP CHIEF EXECUTIVE

Andy was appointed Group Chief Executive in April 2003, following previous roles as Chief Executive of AXA Sun Life plc and director of AXA UK plc. He is currently a non-executive director of ITV plc. Previously Andy was President and Chief Executive Officer of Global Consumer Finance Europe at GE Capital UK, Western Europe and Eastern Europe, and is the former President of National Westminster Bank's US Consumer Credit Business.

GEORGE CULMER
CHIEF FINANCIAL OFFICER

George was appointed Chief Financial Officer and Group director in May 2004. He was previously Head of Capital Management at Zurich Financial Services and Chief Financial Officer of its UK operation. Before that George spent ten years with Prudential.

MARK CHAMBERS
GENERAL COUNSEL AND GROUP COMPANY SECRETARY

Mark Chambers joined as General Counsel and Group Company Secretary in October 2004. Prior to joining the Group, Mark led the legal team at American Express for Europe, Middle East and Africa. Before that he worked for GE holding a number of senior positions with the consumer finance and insurance businesses. Before moving in house, Mark worked for Slaughter and May, a leading international law firm, in London and New York. Mark is a non-executive director of the University of Westminster and a member of the Finance and Business Committee of WWF-UK.

ORLAGH HUNT
GROUP HUMAN RESOURCES DIRECTOR

Orlagh joined the Group as HR Director for International in September 2003 and was appointed Group Human Resources Director in October 2006. She was previously Head of Human Resources for AXA Sun Life and has previously worked at Walkers and Tesco in a variety of HR management roles.

TIMOTHY MITCHELL
GROUP UNDERWRITING AND CLAIMS DIRECTOR

Tim was appointed Group Underwriting & Claims Director in November 2007 when he joined the Group. Tim has over 30 years experience in the insurance industry.
He joined RSA from Zurich Financial Services where he held senior underwriting roles including three years as Global Chief Underwriting Officer for General Insurance. Tim has also held senior management roles at AIG and Continental Insurance.

SIMON LEE

CHIEF EXECUTIVE, INTERNATIONAL BUSINESSES

Simon has been Chief Executive of RSA's International business since April 2003. He is Chairman of the Codan Group and of Trygg-Hansa and is a director of RSA Canada. Previously he spent 17 years with the National Westminster Bank Group, in the UK and US including time as Chief Executive, NatWest Offshore and Head of US Retail Banking.

ADRIAN BROWN

UK CHIEF EXECUTIVE

Adrian Brown was appointed UK CEO in September 2008. Adrian is a qualified management accountant and has been with the RSA Group since 1989. Between 2006 and 2008, he was the UK's Chief Operating Officer with responsibility for Claims, Sales and Service, IT and Change across both Personal and Commercial lines. Prior to this, he was UK Director of Personal Lines, led the launch of MORE TH>N® and held a number of senior customer service and finance roles.

PAUL WHITTAKER

CEO OF EMERGING MARKETS

Paul was appointed CEO of Emerging Markets in 2006, having been RSA's Group HR Director since April 2003. He has over 20 years senior management experience in the financial services sector including three years at AXA and 10 years at GE Capital, including work in Asia and Eastern Europe on acquisition integration and business development.

DAVID WEYMOUTH

GROUP OPERATIONS AND IT DIRECTOR

David joined as Group Operations and IT Director in June 2007. David spent 27 years with the Barclays Group, where senior positions included Chief Operating Officer for Corporate Banking and Group Chief Information Officer and was part of the Group Executive Committee. He most recently spent two years consulting to a portfolio of blue chip and government organisations and acting as an independent Board Member at the DTI and for Chordiant Inc, the US Nasdaq quoted software business.

CLARE SHEIKH (NÉE SALMON)

GROUP STRATEGY, MARKETING AND CUSTOMER DIRECTOR

Clare joined as Group Strategy, Marketing and Customer Director in June 2007. Previously she was Director of Marketing & Commercial Strategy at ITV plc and a member of the Executive Management Board. Clare is also the former Managing Director of AA Financial Services and has held senior commercial roles at Prudential and British Gas. She is also a non-executive director of Alliance Trust plc.

ANNE JÆGER

GROUP CHIEF AUDITOR

Anne has been with the RSA Group since 2001. She was appointed Group Chief Auditor in September 2008. Prior to that she was Regional Chief Auditor, International, based in Denmark. She was part of the Codan Group Executive leadership team and the International Central leadership team. Anne was previously CFO at Maersk Data for two years and spent 13 years with KPMG as a State Authorised Public Accountant, where she was involved in work with public listed companies and M&A and restructuring.

BOARD OF DIRECTORS

JOHN NAPIER

Age 66. Director of the Group since January 2003 and Chairman of the Group since March 2003. Chairman of the Nomination Committee since March 2003. Member of the Remuneration Committee since January 2009. Non-executive Chairman of Aegis Group plc (media) since June 2008 and interim Chief Executive of Aegis Group plc (media) since December 2008. Former Non-executive Chairman and Executive Chairman of Kelda Group plc (water utility). Former Chairman of Booker plc (cash and carry). Former Managing Director of Hays plc (business services) from 1991 to 1998. Former Managing Director of AGB plc (international market research and information services). ●●●

ANDY HASTE

Age 47. Director and Group Chief Executive since April 2003. Non-executive Director of ITV plc (media) since August 2008. Former Chief Executive of AXA Sun Life plc and Director of AXA UK plc (life and pensions). Former President and Chief Executive Officer of Global Consumer Finance Europe at GE Capital UK, Western Europe and Eastern Europe (financial services). Former President of National Westminster Bank's US Consumer Credit Business (retail banking). ●●

GEORGE CULMER

Age 46. Chief Financial Officer and Director of the Group since May 2004. Previously Head of Capital Management Zurich Financial Services (insurance). ●●

NOEL HARWERTH

Age 61. Director of the Group since March 2004. Director of Logica CMG plc, Impellam Group plc (support services) and Harry Winston Diamond Corporation (mining and retail). Deputy Chairman of Sumitomo Mitsui Banking Corporation Europe Limited (finance). Former Chief Operating Officer of Citibank International plc (finance). ●●

EDWARD LEA

Age 67. Director of the Group since July 2003. Chairman of the Group Audit Committee since October 2003. Director of Redbourn Group Limited (property management and investment). Director of Powertraveller Limited. Director of MacIntyre Care (charity). Previously a Director of BUPA. ●●●

SIMON LEE

Age 47. Director of the Group since January 2007 having been Chief Executive of the International business since April 2003. Former Chief Executive, Natwest Offshore and Head of US Retail Banking at National Westminster Group. ●

MALCOLM LE MAY

Age 51. Director of the Group since March 2004 and Chairman of the Investment Committee. Non-executive Director of Pendragon plc (general retailers). Former Deputy Chief Executive of Morley Fund Management (Investment Fund Manager). Former Deputy CEO of ING-Barings (finance). ●●●

JOHN MAXWELL

Age 64. Director of the Group since July 2003. Chairman of the Remuneration Committee since October 2003. Director of Provident Financial plc (financial services). Director of Homeserve plc (support services). Director of the Royal Automobile Club Limited. Director of London Finance and Investment Group plc. Previously an executive director of Prudential Group plc. Former Chairman of DX Services plc (mail). Previously Director General (Chief Executive Officer) of The Automobile Association Limited. ●●●●

JOHANNA WATEROUS

Age 51. Director of the Group since May 2008. Director of the RBG Kew Foundation and Enterprises Limited. Chairman of Britt Lintner Limited. Director of the English National Opera. Former Chairman of Tate Enterprises and Director of McKinsey & Company. ●●

● Executive director
● Member of the Group Audit Committee
● Member of the Remuneration Committee
● Member of the Nomination Committee
● Member of the Investment Committee

CONTENTS

Directors' report

The directors of RSA Insurance Group plc (RSA) present their report and the audited financial statements of the Company for the year ended 31 December 2008.

Principal activity

The Company is the holding company of the RSA group of companies (the 'Group') whose principal activity is the transaction of personal and commercial general insurance business. The Group operates in 33 countries and provides general insurance products and services in over 130 countries.

Business review

The Companies Act 2006, section 417 requires the directors to present a business review in this report. The information that fulfils this requirement can be found in the sections below, which are incorporated by reference into this report:

- The Group CEO's review on pages 6 to 10
- The Group strategy on pages 11 to 13
- The regional business reviews on pages 14 to 25
- The financial review on pages 26 to 29
- The key performance indicators on pages 6 to 25
- The discussion of future developments of the business in the Group CEO's business review on pages 6 to 10 and in the regional business reviews on pages 14 to 25
- The discussion of principal risks and uncertainties facing the Group set out in the estimation techniques, risks, uncertainties and contingencies on pages 76 to 78, and in the risk framework on pages 30 to 32 and
- The corporate responsibility report on pages 33 to 35.

The business review has been prepared to the best of the directors' knowledge in order to provide the Company's shareholders with a fair review of the development/performance of the position of the Company (and the Group as a whole), together with a description of the principal risks and uncertainties which may affect the Group. It may not be relied upon for any other purpose.

The Group uses Key Performance Indicators (KPIs) to provide a well balanced and comprehensive review of the Group's overall performance. KPIs are monitored in a number of areas including financial, employee, customer, strategic priorities and the environment and community. Financial KPIs include the Group's combined operating ratio, expense ratio, operating result and net written premium growth. Employee KPIs include the percentage of staff that have performance related pay, the percentage of staff taking part in the employee survey and the increase in overall employee engagement levels as measured by the survey. Customer KPIs include the levels of customer retention and the Group's position in the annual benchmarking survey on complaints handling by the Association of British Insurers. Environment and community KPIs include targets on energy, travel, waste and levels of CO_2 emissions and the amount of the Group's charitable donations. Financial KPIs are detailed in the Group CEO's review on pages 6 to 10, the Group strategy on pages 11 to 13 and the regional business reviews on pages 14 to 25.

The employee, customer and the environment and community KPIs are detailed in the regional business reviews on pages 14 to 25, the corporate responsibility report on pages 33 to 35 and in this report.

Dividends

The directors recommend a final dividend of 4.98p per ordinary share in respect of the year ended 31 December 2008 to be paid on 5 June 2009 to holders of ordinary shares on the register at the close of business on 6 March 2009, subject to shareholder approval. This, together with the interim dividend of 2.73p per ordinary share, will make a total dividend for the year of 7.71p per ordinary share.

The preferential dividend at the rate of 3.6875% for the period from 1 October 2008 to 31 March 2009 will be paid on 1 April 2009 to holders of preference shares on the register at the close of business on 6 March 2009.

Employment policy

The Group's employment policy reflects our belief that motivated and skilled employees are critical to our success.

We encourage equal opportunities and diversity across the Group. This involves recruiting, engaging, retaining, rewarding and developing people solely on the grounds of ability to do the job, and establishing and promoting a working environment which is free from discrimination.

The Group is committed to the promotion of equal opportunities for all employees including those with a disability. In order to do this, we shall ensure that any reasonable adjustment is made, where it is appropriate to do so, to provide equal opportunities to all in respect of recruitment, terms and conditions of employment, promotions, transfers, grievances, redundancies and vocational training. The Group is committed wherever possible, to supporting the rehabilitation and return to work of employees who become disabled during their career with us.

The Group is committed to fostering a constructive dialogue with recognised independent trade unions, ensuring a regular and open dialogue on business issues and early consultation on changes affecting the workforce. In the UK, Unite is formally recognised through a partnership agreement which covers collective consultation and bargaining on behalf of non management employees. The Management Association (TMA) represents managerial employees under a separate consultative agreement. The European Consultative Forum (ECF) is a cross European body created to enable information sharing and consultation on transnational issues with the European workforce. Since 2005, an amended constitution has been in place for the European workforce which enables streamlined consultation arrangements.

Our new Brand was launched externally and internally in March 2008 and following a successful roll out around the Group, our new Brand Beliefs were implemented to replace the people 'behaviours'. The Beliefs were embedded internally into our performance management process from July 2008.

Directors' report continued

The Group continues to focus on the development of employees in order to ensure they can deliver high levels of performance. We believe we can create real competitive advantage by building and maintaining a high performance culture across the Group.

In 2008, we have continued to deliver our leadership development programmes, integrating the new Brand Beliefs into each one. We have continued to accelerate the development of our in house executive talent through the Executive Development Programme which enters its fifth year in 2009. We have also introduced robust strategies to build capability and performance in the areas of sales, underwriting, claims and actuarial.

The Global Technical Graduate Programme continues into its second year, covering business and technical essentials, demonstrating our commitment to core insurance skills and personal development.

Our accelerated career programme, FastTrack, has continued in all regions. 30 individuals from 16 different countries joined the programme in 2008.

We have seen improvements in a number of key result areas in our global employee survey. In 2008 our focus was on employee engagement. Our new survey providers, Gallup, supported us in measuring employee engagement using the Gallup Q12© questions. With an overall response rate of 86%, our engagement levels represent a better than average result for first time clients. When comparing this year's scores with the equivalent from our previous supplier we have made good progress in all areas.

Our policy is to encourage employee share ownership. Employees from a number of our global businesses are encouraged to participate in Sharesave which is an Employee Sharesave Scheme (HM Revenue and Customs approved). This year saw a significant increase in the number of eligible employees participating in both the UK and overseas schemes.

We also encourage employees to participate in our employee discount schemes. Our Staff Saver Scheme in the UK currently has approximately 6,000 Staff Saver policies in force, an increase from approximately 500 policies in 2007.

Employees are kept well informed of the overall performance and objectives of the Group. Communications are regularly provided by email, intranet articles and staff publications. Key messages from our biannual Group Leaders Conferences are fed back to teams by local management.

The Group actively encourages employees to become involved in supporting their local communities. Further details are provided in the corporate responsibility report on pages 33 to 35.

Environmental programme

Details of our environmental programme can be found on our website at **www.rsagroup.com**.

Supplier payment policy

It is the Company's policy to agree appropriate terms and conditions in advance with its suppliers and to make payment in accordance with those terms and conditions, provided the supplier has complied with them. In most cases, agreements for the supply of goods or services are made under the Group's standard terms of contract that lay down payment terms. In the UK these are available on request from UK Procurement, Leadenhall Court, 1 Leadenhall Street, London EC3V 1PP.

The Company's outstanding indebtedness to trade creditors on 31 December 2008 amounted to £3.9m corresponding to 19 days' payment when averaged over the year.

Share capital

During the year, 24,707,235 ordinary shares of 27.5p each were issued in satisfaction of the exercise of employee share options for a total consideration of £19,436,726, and 51,770,891 ordinary shares of 27.5p each were issued under the Company's scrip dividend scheme for a total consideration of £64,803,178.

The Company can increase its share capital and authorise the directors to allot further securities by ordinary resolution. As at 31 December 2008, the directors had authority to allot securities up to a nominal amount of £358,884,692.

The Company may purchase any of its own shares (including any redeemable shares). An authority from shareholders for the Company to purchase up to 325,496,475 of its own ordinary shares (representing 10% of its issued share capital as at 20 March 2008) remained in force at 31 December 2008.

Further details on the share capital of the Company are incorporated into this report and are set out in note 18 on pages 103 to 104.

Rights and obligations attaching to shares

The rights attaching to the ordinary shares and preference shares are set out in the Articles of Association (the 'Articles'). Details of the rights and obligations attaching to shares as at 31 December 2008 are incorporated into this report by reference and are set out in note 18 on pages 103 to 104.

The Articles may be amended subject to shareholder approval by special resolution at a general meeting of the Company.

Employee Benefit Trusts

The Company operates the Royal & SunAlliance ESOP Trust, the Royal & SunAlliance ESOP Trust No 2 and the Royal & SunAlliance ESOP Trust No 3 (the 'Trusts'). In each case, the Trustee is Lloyds TSB Offshore Trust Company Limited. In respect of any shares held in the Trusts, the Trustee may vote in respect of those shares, but is not obliged to. In respect of the Royal & SunAlliance ESOP Trust No 3, the Trustee may have regard to the financial interests of the beneficiaries in exercising its voting rights over the Company's shares.

Substantial share interests

At the date of this report we have been notified, in accordance with the Disclosure and Transparency Rules, of the following interests in the ordinary share capital of the Company:

	Number of shares in which there is a direct interest	Number of shares in which there is an indirect interest	Interest in issued share capital
AXA S.A.	40,988,047	253,703,708	8.85%
Goldman Sachs Asset Management	–	192,491,038	5.78%
Standard Life Investments	111,042,332	63,001,930	5.23%
Legal & General Group plc	137,792,333	15,354,571	4.60%
Schroders plc	–	134,071,533	4.02%

Directors

The names of the directors, together with biographical details are set out on pages 38 and 39 and are incorporated into this report by reference.

Details of the directors' service contracts and terms of appointment, together with their interests in the Company's shares are shown in the remuneration report on pages 49 to 61 and are incorporated into this report by reference.

Details of directors' powers are set out in the corporate governance report on page 44 and are incorporated into this report by reference.

Directors' indemnity

Article 144 of the Company's Articles provides that, among other things and insofar as permitted by law, every director shall be indemnified by the Company against all costs, charges, expenses, losses or liabilities incurred in the execution and discharge of the directors' duties, power or office.

Since 12 July 2006, the Company has granted an indemnity to each of the directors pursuant to the power conferred by Article 144. The indemnities granted constitute qualifying third party indemnity provisions (as defined by section 234 of the Companies Act 2006). The Board of Directors (the 'Board') believes that it promotes the success of the Company to provide this indemnity to its directors in order to ensure that the Group attracts and retains high calibre directors through competitive terms of employment in line with market standards.

Directors and officers of the Company and its subsidiaries also have the benefit of an insurance policy which provides suitable cover in respect of legal actions brought against them.

None of the directors had any interest in any other contract with the Company or any of its subsidiaries during 2008.

Related party transactions

Related party transactions are set out in note 32 on page 121.

Significant relationships and essential contracts

The Company does not consider that it, or any of its subsidiaries, has any key dependency or essential contract that is fundamental to the success of the Company that is required to be disclosed pursuant to section 417 of the Companies Act 2006. However, the Group includes a number of regulated entities which rely on various licences to carry out their business. Accordingly, maintaining effective relationships with the Group's regulators is integral to the success of the Group's strategies and its long term value.

Charitable and political contributions

The Company and its subsidiaries worldwide made charitable donations of £2,245,273 during the year. The largest contribution of £330,852 was made for the Swedish life buoy programme promoting safety around water. There is a formal Group Policy currently in place which prohibits any donations to political parties.

Annual General Meeting

The AGM will be held at the Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE on Monday, 18 May 2009 at 11.00 am.

Enclosed with this report is a letter from the Chairman to shareholders. Attached to the letter is the Notice convening the AGM which will include items of ordinary and special business as detailed in the Notice.

Auditors

So far as each director is aware, there is no relevant audit information (as defined in section 234ZA(3) of the Companies Act 1985) of which the Company's auditors are unaware, and each director has taken all steps that he ought to have taken as a director in order to make himself aware of, and to establish that the auditors are aware of, any relevant audit information.

Deloitte LLP have confirmed their willingness to continue in office as auditors of the Company for the year ending 31 December 2009. A resolution for their reappointment will be proposed at the 2009 AGM.

Going concern

In considering the appropriateness of the going concern basis, the Board has reviewed the Group's ongoing financial commitments for the next 12 months and beyond. The Board's review included consideration of the Group's underwriting plans, strong regulatory capital surplus, diverse insurance risk profile, considerable undrawn financing facilities and highly liquid investment portfolio. As a result of this review the directors have satisfied themselves that it is appropriate to prepare these financial statements on a going concern basis.

By order of the Board
Mark R Chambers
General Counsel and Group Company Secretary
25 February 2009

Corporate governance

This report sets out the Company's approach to corporate governance in 2008. The report has been prepared in accordance with the Code of Best Practice set out in section 1 of the 2006 FRC Combined Code on Corporate Governance (the 'Combined Code') and sets out the extent of our compliance with the Code.

Compliance with the Combined Code

Throughout 2008 the Group has complied with the Principles and Provisions of the Combined Code except that the Group has not appointed a senior independent director. The non-executive directors consider each year formally whether a senior independent director is required and continue to have a unanimous view that the appointment of a senior independent director is not appropriate at this time. All non-executive directors are encouraged to communicate directly with executive directors and senior management outside of formal meetings and an active dialogue is maintained by the Board.

The Board

The Board is accountable to shareholders for the creation and delivery of strong sustainable performance and the creation of long term shareholder value. The Board meets regularly and is responsible for organising and directing the affairs of the Company and the Group in a manner that will promote the success of the Company and is consistent with good corporate governance practice, and for ensuring that in carrying out its duties the Company and the Group meet legal and regulatory requirements. The Board is also responsible to the Financial Services Authority (FSA) for ensuring compliance with the Group's UK regulatory obligations. In the first quarter of 2008 the FSA concluded an Advanced Risk Recognition Operating FrameWork review of both the Group and UK operations. During 2008 the FSA also conducted private meetings with several members of the Board and executive management, including Johanna Waterous, prior to her appointment as a director, as a part of their 'close and continuous' programme.

The business of the Company is managed by the directors, who may exercise all the power of the Company subject to the Articles, relevant law and any directions as may be given by the Company in general meeting by shareholder resolution. The directors may delegate any of their powers or discretions to committees.

A director must not vote in respect of any contract or other proposal in which he (or any person connected with him) has a material interest otherwise than by virtue of his interest in securities of the Company. However, a director shall be entitled to vote in certain limited circumstances which are set out in full in the Articles. The Articles of the Company were amended at the 2008 AGM to, amongst other matters, address the new statutory provisions regarding directors' duties in relation to conflicts of interest which came into force on 1 October 2008 under the Companies Act 2006. Following the aforementioned amendment the Company has put updated procedures in place to deal with conflicts of interest and these procedures have operated effectively throughout 2008.

The directors restrict the borrowings of the Company so that the aggregate amount, for the time being, remaining borrowed by the Group is not, without the previous sanction of an ordinary resolution of the Company, more than one and a half times the aggregate of:

- The amount paid up on the issued share capital of the Company and
- The total of the capital and revenue reserves of the Group (subject to certain adjustments).

The specific duties of the Board are clearly set out as a formal schedule of matters specifically reserved to it, which can only be amended by the Board itself and which is reviewed annually. Matters reserved to the Board include:

- Approval of the Group's long term objectives and commercial strategy
- Approval of changes to the Group's senior management structure
- Approval of the Group's overall risk appetite
- Annual review of the effectiveness of internal control arrangements
- Approval of the annual operating and capital budgets
- Changes to the Group's capital structure and
- Approval of the Group's financial results and any significant changes to accounting practices or policies.

The Board met 11 times during the year ended 31 December 2008. The attendance of directors at meetings of the Board and at board committees of which they were members during the year is set out below:

	Notes	Board meetings	Board Committee	Group Audit Committee	Nomination Committee	Remuneration Committee	Investment Committee	Board Risk Committee
Total number of meetings in the year	1	11	4	5	3	8	3	4
George Culmer		11	4				3	4*
Noel Harwerth		11		5			3	
Andy Haste		11	4				3	4
Edward Lea		11		5*		8	3	
Simon Lee		11						
Malcolm Le May		8			2	5	3*	
John Maxwell		11		5	3	8*	3	
Bridget McIntyre	2	8						
John Napier		11*			2*		3	
Johanna Waterous	3	6		2			1	

*Chairman of the Board or board committee

Notes:

1. In addition to attendance as above, Andy Haste and George Culmer regularly attend, by invitation, meetings of the Group Audit Committee (GAC). Andy Haste regularly attends meetings of the Remuneration Committee.
2. Bridget McIntyre resigned as UK CEO on 2 September 2008 and as a director on 31 December 2008.
3. Johanna Waterous was appointed as a non-executive director with effect from 20 May 2008.

Board balance and independence

Details of the directors who served during the year can be found on pages 38 and 39.

At all times during the year, at least half of the Board, excluding the Chairman, comprised non-executive directors. All non-executive directors have been determined by the Board to be independent. The Chairman meets regularly with the non-executive directors both individually and collectively without the executive directors being present. The Chairman met the independence criteria of the Combined Code on his appointment in 2003 and continues to meet the criteria set out in the Code. There have been no changes to his external commitments since then which might affect his responsibilities to the Group. Andy Haste was appointed as a non-executive director of ITV plc on 11 August 2008 at which time ITV plc was a constituent of the FTSE 100. ITV plc is currently a member of the FTSE 250. No other executive director served on the board of a FTSE 100 company during the year.

Directors have access to the services and advice of the General Counsel and Group Company Secretary and in addition may take independent professional advice at the expense of the Company in furtherance of their duties.

Appointments to the Board

The directors and the Company (by ordinary resolution) may appoint a person who is willing to be a director either to fill a casual vacancy or as an additional director. A director who is appointed by the directors shall retire at the following AGM and will put himself forward to be elected by the shareholders. In accordance with the Company's Articles and the Combined Code, the directors submit themselves for reappointment at the first AGM after their appointment and for re-election every three years thereafter. Johanna Waterous will therefore be proposed for reappointment at the forthcoming AGM and the directors proposed for re-election are Andy Haste and John Napier. The Company may (by ordinary resolution of which special notice has been given) remove any director before the expiration of his period of office.

Pursuant to his appointment on 9 January 2003, John Napier has completed a six year term as a non-executive director and Chairman and his appointment has been extended for a further three year term which will expire on 31 December 2011. This reappointment was considered in detail by the Board, with particular consideration given to the commitment shown by John Napier to his role during his term of appointment and the requirement for the progressive refreshment of the Board.

Nomination Committee

During the year the Nomination Committee was chaired by John Napier. The other members of the Committee were John Maxwell and Malcolm Le May. The attendance record of directors during 2008 is shown in the table above. The Committee met three times during 2008.

The Nomination Committee's principal duties are to review the structure, size and composition of the Board and to evaluate the directors' skills, knowledge and experience. When appointing new directors, regard is given to the size of the Board and the balance of executive and non-executive directors as well as the skills and experience already represented by the existing Board members, and those which would be desirable on the Board going forward. The Committee has access to external recruitment consultants in order to help fill any vacancies. The Committee considers the leadership needs and succession planning of the Board when making decisions on new appointments. Resolutions to reappoint directors at the AGM are

Corporate governance continued

subject to the approval of the Board, taking into account the recommendations of the Nomination Committee.

Induction and professional development

On appointment, directors undertake an induction programme and receive a range of information about the Company when they join the Board. This includes background information on the Group and details of board procedures, governance issues and directors' responsibilities. The induction programme also includes a series of meetings with members of the Board and executive management, together with various briefings and presentations regarding the business and regulatory matters from executives.

Development and training for the directors is an ongoing process which includes briefings on legislative changes and on corporate governance issues. Directors also receive regular presentations about the Company's operations and there are regular discussions on strategy, customer marketing and employee satisfaction and environmental, social and governance matters. Opportunity is also created for non-executive directors to make informal visits to different parts of the Group and to meet with local management.

Performance evaluation

In 2008 the Board undertook an annual evaluation of its performance to assess how well the Board, its committees and the directors were performing. The review included the use of a comprehensive questionnaire. Responses from the questionnaire were collated and subsequently discussed by the Board. Some of the outcomes achieved in 2008 following the review included:

- A continued commitment to site visits and on the non-executive directors meeting emerging talent from the business
- Continued improvement of agenda management for Board meetings to ensure that adequate time is made for the debate and exchange of ideas and
- A programme of regular investment updates for the whole Board, in addition to continued comprehensive reviews at the Investment Committee.

The non-executive directors are responsible for the evaluation of the Chairman's performance and take into account the views of the executive directors in their evaluation. As part of the ongoing performance evaluation process the Chairman has regular one to one meetings with all the non-executive directors.

Chairman and Chief Executive Officer (CEO)

The roles of the Chairman and the Group CEO are separate, with responsibilities clearly divided between them. This separation of responsibilities is formalised in role statements which have been approved by the Board.

The Chairman is responsible for leading the Board, liaising as necessary with the Group CEO on developments between Board meetings and ensuring that both the Group CEO and his executive management team have appropriate objectives and that their performance against those objectives is reviewed. The Group CEO is responsible to the Board for the executive management of the Group and for liaising with the Chairman and keeping him informed on all material matters.

Remuneration

Details of the directors' remuneration and the Group's policies on remuneration are set out in the remuneration report on pages 49 to 61.

Financial reporting

The directors are required to ensure that adequate accounting records are maintained so as to disclose at any time, and with reasonable accuracy, the financial position of the Group. They are also responsible for taking reasonable steps to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The directors must present financial statements for each financial year, in accordance with applicable law, accounting standards and regulations, which give a true and fair view of the state of affairs of the assets, liabilities, financial position and the profit or loss and cashflows for the Company (and the Group as a whole) for that period. Financial statements for the Group are prepared in accordance with International Financial Reporting Standards (IFRS), the Companies Acts 1985 and 2006 and Article 4 of the IAS Regulations.

In preparing such financial statements the directors are required to:

- Select suitable accounting policies and apply them on a consistent basis using reasonable and prudent judgement
- State whether or not applicable accounting standards have been followed and explain any material departures
- State whether the Group financial statements have been prepared in accordance with IFRS and
- Use the going concern basis unless it is inappropriate to do so.

The directors confirm that they have complied with the above requirements in preparing the financial statements.

Internal control

The Board has overall responsibility for the Group's internal control systems and for monitoring effectiveness. Implementation and maintenance of the internal control systems are the responsibility of the executive directors and senior management. The performance of internal control systems is reviewed regularly by the Group Audit Committee (GAC).

The Board reviews annually the effectiveness of the Group's systems of internal control in order to safeguard the Group's assets and shareholders' investment. This system includes governance, financial controls, the risk management framework and the process to deliver regulatory and compliance requirements. The systems are designed to

identify and mitigate, rather than eliminate, the potential risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material financial misstatement or loss. Following the review of the internal control systems, the Board confirms that the actions it considers necessary to rectify any significant failings or weaknesses identified as a result of the review have been, or are being, taken.

The Board, through the GAC, receives reports from the Group Chief Auditor and her team on the integrity of the control environment and also receives reports from the external auditors based upon their audit work. The GAC also receives reports on the adequacy of the Group's arrangements for ensuring regulatory compliance from the Group Head of Regulatory Risk and Compliance. The Board, through the Board Risk Committee (BRC), considers reports from risk specialists to the Group, and reviews Group level risk management information.

Each quarter there is a self certification process completed by business managers across the Group to confirm the adequacy of controls and their compliance with Company policies, laws, rules and regulations.

The Board considers that the current reporting framework delivers sufficient information to monitor the systems of internal control and to review their effectiveness as required by the Combined Code. The Board therefore considers that an ongoing process for identifying, evaluating and managing the significant risks faced by the Group has been in place during 2008 and up to the date of approval of the Annual Report and Accounts. This process is regularly reviewed by the Board and accords with the Turnbull Guidance on the Combined Code.

Further detail on the overall risk framework is set out on pages 30 to 32.

Group Audit Committee

The GAC is chaired by Edward Lea who has been Chairman of the Committee since October 2003. The other members of the Committee are Noel Harwerth, John Maxwell and Johanna Waterous, who joined the Committee on her appointment to the Board on 20 May 2008. In 2008, the Committee met five times. The attendance record of directors in 2008 is shown in the table on page 45. The Committee is comprised of independent non-executive directors who have recent and relevant financial experience. The Group CEO, Chief Financial Officer, Group Chief Auditor and Group Head of Regulatory Risk and Compliance are regular attendees. The Chairman and other members of executive management are also invited to attend from time to time. The outcomes of meetings are reported to the Board and the Board receives the minutes of all GAC meetings.

The GAC's principal duties are as follows:

- To coordinate and have oversight of the Group's financial reporting process
- To monitor compliance
- To have oversight of internal and external audit functions
- To manage the systems of internal controls
- To review the Group's financial performance
- To review all matters relating to the legal integrity of the Group and
- To provide assurance on the effectiveness of the Group's risk management.

The GAC has unrestricted access to Company documents and information, as well as to employees of the Company and the external auditors.

The GAC meets regularly with internal and external auditors without management present. The partner of the Group's external auditors, who is responsible for the external audit, attends meetings regularly. Each year, the GAC considers the performance of the external auditors prior to a resolution on their reappointment and remuneration at the AGM.

It is the GAC's responsibility to keep the procedures laid out in the Group whistleblowing policy under review. This policy deals with employees who wish to raise serious concerns in good faith, and either do not feel comfortable raising the matter with local management or are not satisfied with the local management response. They can raise their concerns with the Group Chief Auditor, who will either investigate or arrange for an investigation of the matter. Employees are offered such safeguards and support as may be necessary to protect their personal integrity and, where possible, identity.

External auditors

During the year, Deloitte LLP were, on a number of occasions, engaged as advisors. In order to maintain their independence, such appointments are only made in accordance with a protocol developed by the GAC. This gives guidance to businesses within the Group on the appropriateness of engaging the Group's external auditors as advisors and sets down the procedures to be followed to authorise such an engagement. The GAC is satisfied that this protocol has been followed and there are no matters that would compromise the independence of the auditors or affect the performance of their statutory duties.

The Board has accepted the GAC's recommendation that a resolution be put to the 2009 AGM for the reappointment of Deloitte LLP as external auditors.

Key features of the current internal control systems of the Group include:

Internal audit

The Group has an internal audit function, whose activities and effectiveness are monitored and reviewed by the GAC. The GAC is responsible for ensuring that adequate access to information and resource is given to the Group Chief Auditor and for approving the appointment to, and removal of the holder from, that position.

Corporate governance continued

The Board Risk Committee

The BRC, which meets at least quarterly, is currently chaired by George Culmer, Chief Financial Officer. The BRC also comprises the Group CEO and other members of executive management. It is intended that in 2009 Noel Harwerth will join the Committee and become Chairman and Malcolm Le May will also join the Committee. The Committee is authorised by the Board under its terms of reference to manage all risks faced by the Group. The Committee's principal duties include:

- Defining the Group's risk appetite prior to approval by the Board by reference to policies, control limits and other mechanisms
- Approval of policy and minimum standards that are consistent with the risk appetite
- Ensuring that risks that are outside the appetite are identified and mitigated in an appropriate manner and
- Overseeing and challenging the Group's risk management processes.

Investment Committee

The Investment Committee is chaired by Malcolm Le May and comprises all of the non-executive directors, the Group CEO and the Chief Financial Officer. The Committee met three times during 2008. Due to the unprecedented activity in the financial markets in 2008 the Board also received regular investment updates from the Group Investments Director. The Committee assists the Board in setting the Group's investment strategy and monitors the execution of that strategy and the Group's investment performance.

Financial control framework

In 2006 the Company voluntarily delisted from the New York Stock Exchange and terminated its American Depository Receipt (ADR) programme. In January 2007 the Company suspended its US SEC registration and its reporting obligations to the SEC also ceased at that time. The registration was permanently terminated on 31 December 2007. As a result of the SEC deregistration, the Company is no longer required to be compliant with the US Sarbanes Oxley Act 2002. However, the elements of Sarbanes Oxley compliance which have added value have been carried forward in the Group's financial control framework.

Corporate governance framework

The Group's corporate governance framework describes and prescribes how the Group is directed and managed by setting out the matters reserved for the Board, the terms of reference of the Board and management committees, role statements, policies, systems, procedures and controls.

The terms of reference for key committees of the Board explaining their role and the authority delegated to them are available on the Company's website **www.rsagroup.com** or on request from the General Counsel and Group Company Secretary.

Delegated authorities

The Group operates a Delegated Authority Policy which specifies how executive authority is delegated from the Board to the Group CEO and on to other executives in the Group. Individual executive licences set out specific limits of authority in terms of entering into financial, underwriting and other business commitments. Each executive is responsible for ensuring a similar process of delegation is in place within his or her area of responsibility.

Dialogue with institutional shareholders

The Board attaches considerable importance to its relationships and communication with shareholders. Senior management meet principal institutional shareholders on a regular basis and small shareholder groups on request and non-executive directors are available to meet with institutional shareholders as required. In addition, investor relations events are held during the year to increase shareholders' understanding of the business.

Constructive use of the Annual General Meeting

All shareholders are invited to attend the Company's AGM. The AGM Notice is despatched to shareholders at least 20 working days before the meeting and contains separate resolutions on each substantive issue including a resolution to adopt the Annual Report and Accounts. All directors are requested to attend each AGM. The Chairman and the chairmen of the Group Audit, Nomination and Remuneration Committees make themselves available to take questions from shareholders at and after the AGM.

Any form of proxy sent by the Company to shareholders in relation to any general meeting must be delivered to the Company, whether in written form or in electronic form, not less than 48 hours before the time for holding the meeting (or in the case of a poll taken otherwise than at or on the same day as the meeting, not less than 24 hours before the time appointed for the taking of the poll).

At any general meeting every shareholder present shall have one vote on a show of hands, and on a poll every shareholder present in person or by proxy shall have one vote for each share of which he is the holder. In the case of an equality of votes, whether on a show of hands or on a poll, the chairman of the meeting shall be entitled to a casting vote. All resolutions were put to a poll at the AGM in 2008. Voting at the AGM is conducted electronically, with the results being announced to the London Stock Exchange and on the Company's website.

By order of the Board
Mark R Chambers
General Counsel and Group Company Secretary
25 February 2009

Remuneration report

The following report by the Remuneration Committee has been approved by the Board for submission to the shareholders at the 2009 AGM.

Deloitte LLP have audited the following items stipulated in law for their review:

- The table of directors' remuneration and associated footnotes on page 57 and the disclosure of the items comprising benefits in kind
- The tables of defined benefit and defined contribution pensions on pages 57 to 58 and associated footnotes
- The table of disclosure of directors' share options and share awards on pages 58 to 61 and associated footnotes.

In constitution and operation the Committee complies fully with the Combined Code as appended to the Listing Rules of the UK Listing Authority and as described in the corporate governance section of this report, on page 44.

Principal duties of the Remuneration Committee

The Committee is a formal committee of the Board and is accountable to shareholders through its annual remuneration report, which is voted on at the AGM, and remains committed to reflecting the best interests of shareholders and to the pursuit of best practice in remuneration policy.

The Committee's principal duties are as follows:

- The determination of the terms and conditions and remuneration of the Chairman of the Board and the executive directors
- Overseeing the operation of the Company's share based long term incentive schemes, including approving the value and timing of awards and overseeing the operation of performance conditions
- Consideration of, and advice to the Board on, the Group's broader remuneration policy in relation to senior executives reporting to the Group CEO (the Executive Team).

The Committee presents a summary of its principal activities to shareholders through this report, and the Committee Chairman attends the AGM to answer questions from shareholders on the activities of the Committee and its remuneration policies.

The Committee's responsibilities are set out in its terms of reference which are available to shareholders on request and on our website at **www.rsagroup.com**. The Committee welcomes ongoing dialogue with shareholders on remuneration policy.

Membership of the Remuneration Committee

During the year the directors who served on the Committee were John Maxwell (Chairman), Edward Lea and Malcolm Le May.

All of the non-executive directors on the Committee were determined by the Board to be independent. The attendance of members in 2008 is shown in the table on page 45.

Members of the Committee have no personal financial interest, other than as shareholders, in the Committee's decisions and they have no conflict of interest arising from cross directorships. Fees for serving as a committee member and chairing committees of the Board are described in the non-executive directors section of this report on page 56.

Advisors to the Remuneration Committee

During the first half of 2008, the Committee obtained its principal advice from Hewitt New Bridge Street, who were appointed by the Committee and provided no other services to the Company during the year. In July, the Committee reviewed the appointment of its advisers and, after presentations to the Committee, appointed Towers Perrin LLP as its principal advisers. In addition to providing independent advice to the Committee, Towers Perrin LLP provide broad reward advice to the Company and will continue to do so in 2009.

The terms of engagement for the remuneration consultants are available to shareholders on request and on our website at **www.rsagroup.com**.

The Group CEO is invited to attend all meetings of the Committee to provide context and advice to the Committee on Group strategy and performance and senior executive pay strategy. The Group Human Resources Director and the Group Director, Reward and Recognition normally attend meetings to provide information on wider remuneration strategy and practice within the Group. In 2008 the Chairman was invited to attend meetings as appropriate and became a member of the Committee with effect from 1 January 2009. The General Counsel and Group Company Secretary acts as secretary to the Committee. None of the non Committee attendees are present as of right, and do not attend when their own remuneration is discussed.

Activities of the Remuneration Committee

The continuing focus of the Committee is the maintenance of a strong link between performance and reward. It is the Committee's view that the interests of shareholders are best served by ensuring a remuneration structure which has a significant element of performance related pay, and reinforces the culture of high performance and accountability that applies at all levels throughout the Group.

The Committee is required by its Terms of Reference to meet at least twice each year, but meets as often as necessary throughout the year to ensure that it is able to fully report to the Board and shareholders on all relevant matters. In 2008, the Committee met eight times and discussed, amongst other things, the issues described below.

In February, the Committee approved the 2007 remuneration report, determined the outcome of annual bonuses for 2007 in the light of actual performance against agreed goals and objectives, and reviewed the proposed annual objectives and performance goals for executive directors in 2008. They also reviewed the effectiveness of the Remuneration Committee. At its meeting in April, the Remuneration Committee reviewed the base salaries of the executive directors and reviewed a forecast of share usage

Remuneration report continued

for Long Term Incentive Plan (LTIP) awards in 2008. When the Committee met in July it approved LTIP awards to be granted in September 2008 and approved the grant of Sharesave awards for 2008. It also received presentations from independent advisers and resolved to appoint Towers Perrin LLP as independent adviser to the Committee. In September the Committee reviewed the fees for the Chairman of the Board. In October the members of the Committee received an update on market movements in executive director remuneration. At its December meeting the Committee gave its approval to work being undertaken on share plans.

Remuneration policy principles

The Committee's remuneration policy is consistent with the high performance culture across the Group. The key principles which underpin the remuneration policy are:

- Total remuneration is set at a level which enables the recruitment, retention and motivation of high quality executive talent
- There is a strong and visible link between remuneration and performance
- Executive remuneration and shareholder interests are strongly aligned. This is reflected in the design of the LTIP, which provides a co-investment opportunity
- The observation of existing share ownership guidelines to further enhance the alignment of shareholder interests with those of executive directors
- Incentive arrangements are leveraged so that only exceptional performance attracts the highest levels of award
- A balance of short and long term performance is used, incorporating measures of financial performance, delivery of shareholder value and a robust assessment of personal contribution
- Remuneration policy and practice is transparent to shareholders
- That, where relevant, there is consideration of environmental, social and governance risks when determining remuneration for executive directors and senior managers to ensure that positive behaviours are reinforced.

Remuneration review

The Committee wishes to ensure that the structure of remuneration for the senior executives is sufficiently compelling and aligned with practice in the organisations with which we compete for talent. The Committee has reviewed variable remuneration for the executive directors, the Executive Team and senior management and believes that adjusting our variable pay policy is appropriate and timely because:

- The financial performance of the Group has been sustained and strong for a number of years, and the Group continues to deliver excellent results. The Committee believes that performance linked variable pay should be capable of delivering outstanding reward for consistently outstanding performance
- Reward opportunities with a strong performance link are critical to retain our top executives in the current challenging business environment and
- Following a review of the market, it was clear that the variable pay opportunities at the Company were lower than those in comparator companies and the Committee has approved a number of changes to improve the Company's alignment with those companies.

The Committee has therefore resolved to:

- Increase the on target and maximum cash bonus opportunity for the executive directors (the first increase in the annual bonus opportunity for over five years)
- Enhance the element of the bonus paid in the form of deferred shares, from 25% of the total bonus to 33% of the total bonus
- Increase the maximum value of Performance Shares granted under the LTIP for executive directors, but remaining within the limits approved by shareholders when the LTIP was introduced in 2006 and
- Improve the robustness of the guidelines for executives' shareholdings.

Additionally, the performance conditions applying to share awards granted under the LTIP were reviewed and the Committee resolved to adjust the ratio of shares subject to the return on equity (ROE) and total shareholder return (TSR) performance conditions.

Further details on each of the above changes is set out in the relevant section of this report.

Elements of remuneration

Remuneration for executive directors in 2009 will consist of the four principal elements described in the table below, of which only base salary is pensionable:

Remuneration	Purpose	Delivery	Policy detail
Base salary	To reflect the market value of the role and the skills and experience of the individual	• Cash • Monthly • Pensionable	• Reviewed annually, changes effective from 1 April • Benchmarked against equivalent roles in similar companies and with reference to the sustained performance of the executive
Annual performance bonus	To incentivise the delivery of annual goals at Group, business area and individual levels	• Maximum opportunity of 180% of base salary • One third of the annual bonus received is to be in the form of compulsory Deferred Shares under the LTIP • Annual • Non pensionable	• Financial targets are measured against combined operating ratio for Group and business areas • Individual targets are approved by the Remuneration Committee • Up to a further 33% of net cash bonus paid may be reinvested in voluntarily Deferred Shares under the LTIP
LTIP	To reward the creation of sustained growth in shareholder value	• Performance Shares subject to stretching performance conditions • Matching Shares awarded linked to Deferred Shares, also subject to performance conditions • Annual awards that may vest after three years • Non pensionable	• Discretionary awards • Participation reviewed annually • ROE measure, together with TSR performance measured against a peer group of companies • Full details of performance measures and vesting described on page 61
Pension	To provide appropriate and competitive post retirement benefits	• Deferred income • Paid monthly	• Defined benefit scheme or defined contribution scheme, and/or cash allowance in lieu of pension contributions

This structure is replicated for other members of the Executive Team.

As an indication of the balance of remuneration, including long term incentives (LTIs), the following charts illustrate the remuneration attributable to the continuing executive directors over the year (excluding allowances and pension provision):

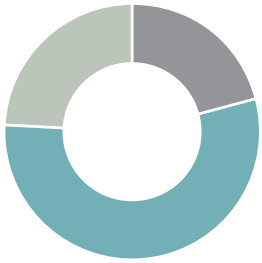
Andy Haste

24% SALARY
48% LTIs
28% BONUS

George Culmer

25% SALARY
46% LTIs
29% BONUS

Simon Lee



21% SALARY
55% LTIs
24% BONUS

For the purposes of the charts, the bonus value is based on the cash bonus plus the fair value of the compulsory Deferred Shares. The LTI value is based on the fair value of awards of Performance Shares and half of the maximum potential number of Matching Shares that may vest (subject to performance) relating to voluntary and compulsory Deferred Shares under the LTIP. Details of how the fair values have been calculated are set out in note 27 on page 118.

Remuneration report continued

Base salary

Policy: Base salary is set with reference to equivalent roles in similar companies and the sustained performance of the executive.

Base salaries for executive directors and members of the Executive Team are set on appointment with reference to market data.

To enable the Group to compete for the most talented executives, the Committee relates base salary levels to the median level for equivalent roles in similar companies facing similar levels of complexity and challenge in the UK and internationally. In the UK, the comparator group most frequently used is a selected group of financial services companies within the FTSE 100. The Committee also has regard to levels of base pay within European and international companies.

The Committee is alert to market concerns surrounding base pay increases and closely monitors basic pay (and total remuneration) for executive directors in the light of both the market and individual and corporate performance, as well as the levels of pay increases available for all employees. The Committee is confident that the structures and processes in place for reviewing annual salary increases are robust.

In 2008, base salaries were primarily reviewed on the basis of market movements. The Committee analysed the remuneration details of a comparator group comprising 14 FTSE 100 financial services companies and awards salary increases with reference to the median position for equivalent roles in that group.

The 2008 salary review process resulted in the following increases, effective from 1 April 2008, for the continuing executive directors (as at 31 December 2008):

	Position	Increase	Base salary
Andy Haste	Group CEO	6.4%	£910,000
George Culmer	Chief Financial Officer	10.4%	£530,000
Simon Lee	International CEO	9.9%	£408,000

The increase in base salary reflected movement in the relevant executive pay market at that time and the performance of the individual.

The following table sets out the base salaries of UK based executives below Board level on a banded basis as at 31 December 2008. No such executive received a base salary in excess of £360,000.

Base salary range	Number of employees
£250,001 and over	15
£200,001 - £250,000	11
£150,001 - £200,000	38

Annual performance bonus

Policy: Bonus payments are related to stretching performance targets and are capped at 180% of base salary. For maximum bonuses to be achieved outstanding performance must be demonstrated.

As part of the review of total remuneration, the Committee reviewed the on target and maximum bonus opportunities for executive directors. After a detailed review of the market, the Committee considered that the previous level of bonus provision was considerably below the median levels of opportunity provided to executive directors in the FTSE 100. Consequently, the Committee decided that, from 2009 the on target and maximum annual bonus opportunity would be increased from 66.5% of base salary at on target level, and 133% of base salary at a maximum level, to 90% of base salary at the on target level, and 180% of base salary as a maximum.

Deferred shares remain an important element of the total bonus and the proportion of deferred shares is to be increased from 25% of the total bonus payable, to 33% of the total bonus. If the stretching targets required to achieve on target level are achieved, executive directors receive a cash bonus of up to 60% of base salary and Deferred Shares worth up to 30% of base salary. For outstanding performance, a cash bonus of up to 120% of base salary and Deferred Shares worth up to 60% of base salary are achievable. Deferred Shares are described in the section headed share based long term incentive awards below.

The targets used for determining the amount of bonus payable are a combination of stretching business performance targets and the results of a structured assessment of each executive's performance against detailed and specific personal objectives.

Financial targets are measured against combined operating ratio (COR) targets which are the preferred measures for the Group. COR is the single indicator which most fully captures the underlying strength and performance of an insurance business. To achieve focused incentivisation, for each executive director financial targets are weighted towards the area of the business for which they have primary responsibility.

The financial targets that apply to the annual performance bonus for Andy Haste and George Culmer are a combination of targets relating to the overall Group COR result and the COR results of the regional operating businesses. The financial targets for Simon Lee's annual performance bonus are weighted towards the International business while also retaining a target for the Group COR result as a whole.

Personal targets are reviewed and approved by the Committee early in the financial year. The Group CEO's performance is assessed annually by the Chairman of the Board and members of the Committee. The Group CEO carries out a similar assessment for each of his direct reports, subject to review and sign off by the Committee in the case of executive directors. Assessments also take account of appropriate leadership style and each executive receives a performance rating against the standard scale used at all levels in the business.

Bonuses paid to executive directors in respect of the performance year 2008 are included in the table of directors' emoluments on page 57. The Remuneration Committee is satisfied that the bonus payments made in respect of 2008 reflect the consistently strong COR results across the Group throughout 2008, and the contribution made by each executive director.

UK based executives who are members of the Top 100 participate in a bonus plan which is structured in the same way and measured using the same metrics as the plan described above. For outstanding performance a cash bonus of up to 80% of base salary and Deferred Shares worth up to 33% of the cash bonus are achievable.

Executives are also offered the opportunity to voluntarily invest up to 33% of the cash element of their bonus into Deferred Shares.

In 2008 (under the LTIP) an award of Matching Shares was made on a pro rata basis to the Deferred Shares. Matching Shares may vest subject to the performance conditions described on page 61 of this report.

The Committee reserves the right to reduce the permissible investment below this level. However, the LTIP will continue to operate on the same terms in 2009.

Share based long term incentive awards

Policy: To provide annual share awards to executives to ensure alignment with shareholder interests solely through the LTIP. Except in exceptional circumstances, no other discretionary share plan will be used to make awards.

Prior to the approval of the LTIP, two share incentive plans were operated:

- The 2004 Share Matching Plan, which was designed to operate for two years. The final awards under this plan were made in 2005
- The Executive Share Option Scheme (ESOS). Regular awards under the ESOS were discontinued from 2006. The ESOS plan rules expire in 2009. It is proposed that a renewed Executive Share Option Scheme will be put to shareholders at the 2009 AGM. As with the ESOS, it is intended that the new plan will initially be used only in exceptional circumstances, such as executive recruitment. Performance conditions will attach to all options granted under the new ESOS, and will be determined by the Committee at the appropriate time.

The primary long term incentive is the LTIP, the key features of which (and associated policies) are summarised in the sections below.

Awards under the LTIP will be funded through a combination of new issues and shares purchased in the market.

Conditional awards of Performance Shares

Participants may receive a conditional award of shares with the grant level and performance condition determined by the Committee prior to each grant. Executive directors, members of the Executive Team and the Top 100 will be eligible for awards of Performance Shares. As part of the review of total remuneration, the Committee considered the value of Performance Shares that are granted annually to executive directors. After a review of the market, the Committee decided to revise its policy of capping Performance Share awards for executive directors at 100% of base salary, and will now permit awards of Performance Shares of up to 150% of base salary, for outstanding personal performance, as approved by shareholders when the LTIP was introduced in 2006.

Account will be taken of personal performance in determining the scale of the award to each executive director and members of the Executive Team. For executives below this level, awards are made based on a formula which relates the size of award to performance and potential, as measured through the annual performance appraisal process.

In any year, the face value of Performance Shares granted to any individual will be limited to 150% of base salary in normal circumstances subject to an overriding cap of 250% of base salary in exceptional circumstances such as an executive recruitment.

Performance Shares will vest after three years subject to the performance condition (see below) and provided the individual remains in employment with the Group (other than in exceptional circumstances such as death or retirement at normal retirement age).

Deferred Shares

As described in the annual performance bonus section on page 52, executive directors, members of the Executive Team and the Top 100 may be granted Deferred Shares as part of the annual bonus. These Deferred Shares may not be withdrawn and will normally vest three years from the date of grant subject to continued employment with the Group.

In addition executives may invest an additional portion of bonus in Deferred Shares on a voluntary basis. Voluntary Deferred Shares are not at risk of forfeiture and may be withdrawn at any time (but the right to Matching Shares would lapse on those Deferred Shares withdrawn).

Conditional awards of Matching Shares

Executives may receive a conditional award of Matching Shares pro rata to the number of Deferred Shares held. At threshold performance the matching ratio will be 0.625:1. The maximum matching ratio for Matching Shares:Deferred Shares will be 2.5:1, calculated on the gross value of the bonus invested in Deferred Shares. Details of the performance condition used are described below.

Executive directors, members of the Executive Team and the Top 100 will be eligible for awards of Matching Shares.

Matching Shares will vest after three years subject to the performance condition (see below) and provided the individual remains in employment with the Group (other than in exceptional circumstances such as death or retirement at normal retirement age).

Performance conditions

The Committee will determine the performance condition for each grant of Performance Shares and Matching Shares, with performance measured over a single period of three years with no provision to retest. In 2009 grants of Performance Shares and Matching Shares related to

Remuneration report continued

non voluntarily Deferred Shares will be subject to a performance condition consisting of a combination of ROE and TSR targets.

While the ROE and TSR performance measures will continue to be used, the weighting of performance measures for long term incentive awards granted in 2009 is to be amended. ROE will be given greater prominence than relative TSR, to underline our commitment to improving the returns that we generate on our balance sheet. The vesting of 70% of the LTIP awards will be based on ROE performance and 30% on relative TSR performance (with the exception of Matching Shares attaching to voluntarily Deferred Shares, the vesting of which will remain dependent solely on the ROE performance condition).

- 70% of the shares comprising the award will vest according to ROE performance. In 2008, the Remuneration Committee approved an increase in the ROE performance targets for awards made in that year, so that if underlying average annual ROE over three years commencing with the financial year of grant is below 12% (10% for awards made in 2006 and 2007), no part of the award subject to the ROE performance condition will vest. If underlying average annual ROE over three years is 12% (10% for awards made in 2006 and 2007), 25% of the award will vest. If underlying average annual ROE over three years is 18% (16% for awards made in 2006 and 2007), 100% of the award will vest. Vesting will be on a straight line basis in between. Underlying ROE will exclude items of an exceptional nature which in the view of the Committee do not reflect the underlying performance of the business.

  For awards to be made in 2009, the ROE target range will return to that previously approved by shareholders of 10% to 16%. If the average annual ROE over three years is 10%, 25% of that element of the award will vest. If underlying average ROE over three years is 16% or more, all of this portion of the award will vest. There will be a straight line vesting scale between these two points.

- 30% of the shares comprising the award will vest according to TSR performance against a comparator group of UK and international financial services companies. Below median performance, no part of the award subject to the TSR performance condition will vest. At median performance, 25% of the award will vest. At upper quintile (top 20%), 100% of the award will vest. Vesting will be on a straight line basis in between.
- Additionally, before any shares subject to the TSR condition vests, the Committee must be satisfied that the Company's TSR performance is reflective of underlying financial performance.

The TSR comparator group will consist of the following companies:

Comparator companies	
Aegon	AXA
Alleanza	Allianz
AVIVA	Baloise
Generali	Legal & General
Munich Re	QBE
Swiss Re	Zurich Financial Services

During 2008, trading in Fortis shares was suspended and the Committee resolved to remove Fortis from the comparator group for the purpose of measuring TSR performance for awards made in 2006, 2007 and 2008. The Committee reviews, on an ongoing basis, the composition of the comparator group and will consider adding companies for future awards in the event that the number of constituent companies drops below an acceptable level.

The Group's TSR will be independently calculated and verified by the Committee for the purposes of awards made in 2009 under the LTIP.

The vesting of Matching Shares related to voluntarily Deferred Shares will be determined solely by the ROE performance condition.

ROE has been selected as the measure of financial performance as it is one of the key measures of overall business performance and is visible externally to shareholders.

The TSR performance condition has been designed to provide alignment between executive remuneration and shareholder interests and to ensure that an element of the package is linked directly to share price performance. The comparator group has been selected to ensure that performance is compared fairly against a group of similar companies operating in a similar competitive environment. The use of ROE and TSR in combination provides a balanced approach to the measurement of Company performance over the longer term.

Dilution

Dilution levels for all schemes are held strictly within the Association of British Insurers (ABI) limits (10% over 10 years for all schemes and 5% for discretionary schemes). The dilution levels compared to ABI limits as at 31 December 2008 were:

ABI limit	RSA dilution
10% over 10 years for all share schemes	5.10%
5% over 10 years for discretionary schemes	3.09%

Share ownership guidelines

Strengthened share ownership guidelines were introduced in 2004 for executive directors and members of the Executive Team. As part of the review of remuneration, the Committee resolved to increase the shareholding requirements for executive directors and members of the Executive Team.

The Group CEO is required to build and maintain a minimum shareholding in the Company equivalent to 200% of base salary (previously 150% of base salary). The other executive directors have a target of 150% of base salary (previously 100% of base salary) and other members of the Executive Team have a target of 75% of base salary (previously 50% of base salary). In order to ensure that progress is made towards this target, executives are required to retain shares to a value of 50% of the net of tax gain under all executive schemes until the relevant guideline is attained. This requirement will apply to awards under the LTIP and will continue to apply to awards under all existing long term incentive plans.

The following table shows the number of shares (including voluntary Deferred Shares held under the LTIP) held by each executive director at 31 December 2008 and the increase in shareholding over the year.

	Shares held	Increase	Salary*
Andy Haste	1,480,103	38%	225%
George Culmer	325,423	33%	85%
Simon Lee	477,458	170%	161%

* Assuming share price of 138.10p (the closing middle market price on the last dealing day of the year).

Pension provision and other benefits

Policy: Reasonable provision in line with arrangements made in similar companies will be made to allow executives to plan effectively for their retirement but the Committee will not compensate executives affected by the tax limits effective 6 April 2006.

Andy Haste is a member of the SAL Pension Scheme (SAL), a contributory defined benefit occupational pension scheme. In common with all other members of the Group's defined benefit occupational pension schemes, from 1 January 2006 Andy Haste's future benefits within SAL will accrue on a career average revalued earnings basis rather than on a final salary basis. The Group retains a cap within its defined benefits and Andy Haste's benefit accrual is calculated with reference to a capped salary (£117,600 for the tax year commencing 6 April 2008). In addition to his benefits within SAL, Andy Haste receives an age related taxable cash allowance to enable him to make his own provision for retirement above the cap. In 2009 he will be paid an allowance of 29% of base salary for this purpose.

George Culmer is a member of the Royal & SunAlliance Stakeholder Pension Plan which is a contributory defined contribution occupational pension scheme. In 2009, as in 2008, he will receive employer contributions worth 15% of base salary, subject to an employee contribution of 5% of base salary up to the HM Revenue and Customs annual allowance as applicable. Additionally, George Culmer receives a taxable cash allowance of 15% of base salary, in order to bring his overall pension provision closer to the market median.

Simon Lee elected not to join a Group pension plan on appointment, and receives a taxable cash allowance of 17.5% of base salary instead.

In addition, the executive directors participate in a number of benefits available to other senior managers including life assurance at the rate of four times base salary together with a spouse/dependant annuity, sickness and ill health early retirement benefits and private medical insurance. They also have a choice between a company car and a monthly cash car allowance. In common with other employees, the executive directors are eligible to participate in the Royal & SunAlliance Sharesave plan.

Service contracts

The Committee's policy on service contracts is that they should be subject to a maximum notice period of one year. Generally in the event of termination and in all cases of termination on performance grounds the Committee's policy would be to seek and apply mitigation. None of the executive directors have current terms in their service contracts which allow them additional rights or payment in the event of a reconstruction or amalgamation of the Group.

Director	Effective date of contract	Notice period
Andy Haste	2 April 2003	12 months
George Culmer	1 May 2004	12 months
Simon Lee	30 April 2003	12 months
Bridget McIntyre*	1 November 2005	12 months

* Bridget McIntyre's contract was terminated by mutual consent on 31 December 2008.

Andy Haste's service contract expires under normal circumstances in January 2024. The service contracts for George Culmer and Simon Lee terminate under normal circumstances in October 2024 and March 2023 respectively. These service contracts may all be terminated earlier by the Company, or the individual, on 12 months' notice.

Bridget McIntyre's termination arrangements

Bridget McIntyre's contract of employment was terminated by mutual consent, effective from 31 December 2008, when she stood down from the Board. The Committee approved termination payments that comprised an amount payable in lieu of notice, in line with the contractual entitlement, equivalent to one year's base salary and bonus for 2008. No amount is payable in respect of a bonus for 2009. Awards made under ESOS and SMP vested prior to termination, and may be exercised within the time periods set out in the rules of the plans as they relate to leavers. Matching Share awards and Performance Share awards made under the LTIP will vest on a time pro rated basis (to 31 December 2008) on the normal vesting date, and remain subject to further pro rating for performance to the end of the relevant performance periods. All awards of voluntary and compulsory Deferred Shares will vest on the normal vesting date. An amount equivalent to 30% of base salary is payable in respect of pension contributions for the notice period. The balance comprises other contractual benefits.

The sums payable in respect of base salary, pension and benefits are subject to mitigation. They will be paid in 12 monthly instalments during 2009 and are subject to reduction, in whole or in part, by any amount received as remuneration or fees from employment, consultancy or any other arrangement until the final payment is made. The sum payable in respect of bonus for 2008 will be paid in March 2009.

External directorships

Where appropriate, the Group encourages directors and other senior managers to accept, subject to the approval of the Chairman and the Group CEO, an invitation to join the Board of another company in a non-executive capacity, recognising the value of such wider experience. In these circumstances, they are permitted to retain any remuneration from the non-executive appointment. For executive directors and other members of the Executive Team, external appointments are limited to one.

Remuneration report continued

On 11 August 2008 Andy Haste was appointed to the Board of ITV plc as a non-executive director. During the year he received a fee of £23,878. At the date of this report Simon Lee and Mark Chambers held directorships in not for profit organisations.

Non-executive directors

Under the Company's Articles, the remuneration paid to non-executive directors is determined by the Board, within limits set by shareholders. The fee structure for non-executive directors is shown below:

	£
Base fee	45,000
Plus:	
Chairman of Group Audit Committee	20,000
Chairman of Remuneration Committee	12,500
Chairman of Investment Committee	12,500
Additional fee for sitting on more than one committee but not acting as chair of any committee	5,000

Non-executive directors are not entitled to bonus payments or pension arrangements, nor do they participate in the Group's long term incentive plans.

The Committee determines the Chairman's remuneration. The fee payable to John Napier in respect of his appointment as Chairman of the Board was £325,000 p.a. until the end of his previous term of appointment which ended on 31 December 2008, and was not increased for three years. In 2009, the fee payable to John Napier is £400,000 for the first year of his current appointment and will be subject to annual review by the Committee. The appointment may be terminated by the Chairman on three months' notice to the Company.

Non-executive directors do not have service contracts but each has a letter of appointment. The letters of appointment all request a period of one month's notice should the non-executive director wish to resign.

Non-executive director	Effective date of letter of appointment
Edward Lea	10 July 2003
John Maxwell	10 July 2003
Noel Harwerth	30 March 2004
Malcolm Le May	30 March 2004
Johanna Waterous	20 May 2008

All non-executive directors (including the Chairman) are subject to a three year rolling period of appointment in accordance with the Company's Articles.

John Napier's initial letter of appointment was effective 9 January 2003 and the term of his appointment was three years. At the beginning of 2006 it was extended until 31 December 2008, and was extended again at the beginning of 2009, until 31 December 2011.

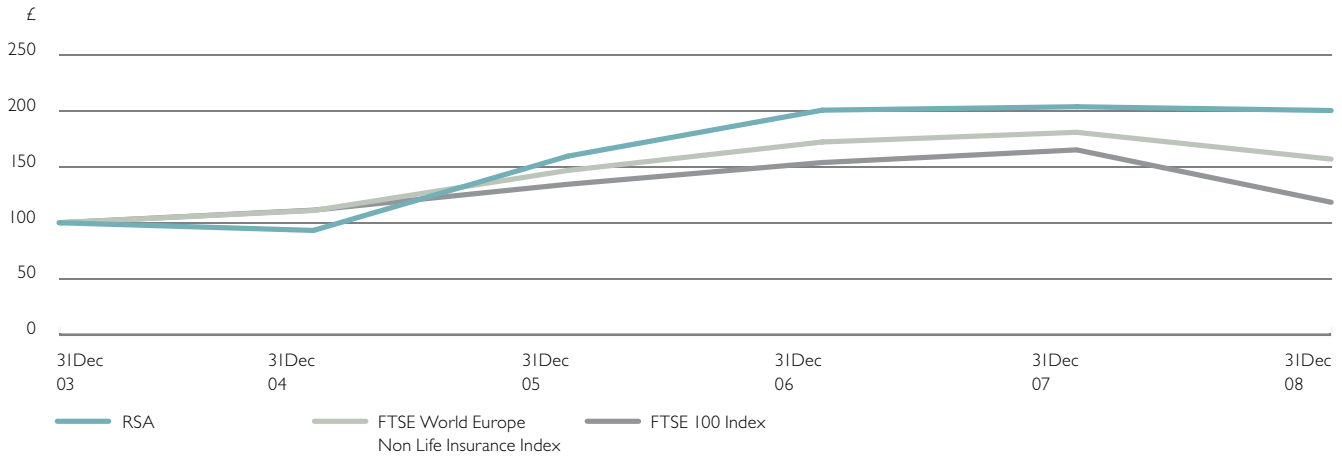
Historical TSR performance

The graph below is included in the report of the Committee as a requirement of Schedule 7A to the Companies Act 1985.

The graph shows the TSR of the Group with reference to the FTSE World Europe Non Life Insurance Index and the FTSE 100 Index. The FTSE World Europe Non Life Insurance Index comprises the range of European insurance businesses which most closely match our competitor group, and the TSR comparator group selected for awards under the LTIP. The FTSE 100 Index comprises the 100 most highly capitalised companies of the UK market. TSR performance relative to the indices is shown over the five years from 31 December 2003 to 31 December 2008.

TSR reflects the change in value of ordinary shares in a company over time, as represented by the evolution of a notional initial investment of £100 in the shares and including any distribution of dividends.

Total shareholder return for RSA and FTSE World Europe Non Life Insurance Index and FTSE 100 Index



Directors' emoluments and interests

Directors' emoluments (audited part)

Remuneration for the year ended 31 December was as follows:

	Notes	Base salary and fees £000	Allowances and benefits £000	Bonuses £000	Total 2008 £000	Total 2007 £000
Executive directors	1					
George Culmer	2	517	105	490	1,112	1,010
Andy Haste	3	896	300	841	2,037	1,912
Simon Lee	4	399	87	367	853	800
Bridget McIntyre	5	408	102	326	836	757
Non-executive directors						
Noel Harwerth		50	–	–	50	50
Edward Lea		65	–	–	65	65
Malcolm Le May		58	–	–	58	58
John Maxwell		58	–	–	58	58
John Napier		325	–	–	325	325
Johanna Waterous		28	–	–	28	–

Notes:

1. 2008 bonuses were calculated as described in the remuneration report on page 52. In 2008 a maximum cash bonus of 100% of salary was achievable.
2. George Culmer received an annual performance bonus of £489,720 in respect of performance year 2008. His allowances include 15% of base salary as a retirement allowance, paid monthly. During 2008 the amount paid was £78,000. He also received car benefits worth £26,000 and medical benefits worth £1,000.
3. Andy Haste received an annual performance bonus of £840,840 in respect of performance year 2008. His allowances include an age related percentage of base salary as a retirement allowance, paid monthly. During 2008 the allowance was 28% and the amount paid was £251,000. He also received car benefits and additional taxable travel benefits worth £40,000 and medical and life assurance benefits worth £9,000.
4. Simon Lee received an annual performance bonus of £367,200 in respect of performance year 2008. His allowances also included 17.5% of base salary as a retirement allowance, paid monthly. During 2008 the amount paid was £70,000. He also received car benefits and additional taxable travel benefits worth £16,000 and medical benefits worth £1,000.
5. Bridget McIntyre resigned as director on 31 December 2008. Her allowances included 15% of basic salary as a retirement allowance, paid monthly from 1 January to 31 August. From 1 September she elected not to receive further employer contributions to the Stakeholder Pension Plan. Her retirement allowance was increased to 30% of basic salary from 1 September 2008 to 31 December 2008 to take account of this. During 2008 the amount paid was £82,000. She also received car benefits and additional taxable travel benefits worth £19,000 and medical benefits worth £1,000.

   Bridget McIntyre's contract of employment was terminated by mutual consent, effective from 31 December 2008, when she stood down from the Board. The Committee approved termination payments that comprised an amount payable in lieu of notice, in line with the contractual entitlement, equivalent to one year's base salary and a bonus for 2008.

   No amount is payable in respect of a bonus for 2009. An amount equivalent to 30% of base salary is payable in respect of retirement allowance for the notice period. The balance comprises other contractual benefits.

   The sums payable in respect of base salary, pension and benefits which amount to £555,202 in aggregate are subject to mitigation. They will be paid in 12 monthly instalments during 2009 and are subject to reduction, in whole or in part, by any amount received as remuneration or fees from employment, consultancy or any other arrangement until the final payment is made. The sum payable of £326,325 in respect of bonus for 2008 will be paid in March 2009.

Pension benefits (audited part)

Non-executive directors are not entitled to any pension benefits. The pension benefits earned by the executive directors, as members of Group defined benefit schemes, were as follows:

	Change in accrued pension in year £	Total accrued pension at 31 December 2008 £	Transfer value of total accrued pension at 31 December 2008 £	Transfer value of total accrued pension at 31 December 2007 £	Difference in transfer values less member contribution (note 1) £
Andy Haste	2,268	11,079	194,984	94,190	94,974

Notes:

1. The difference in transfer values reflects the difference between the two transfer values calculated using relevant information on the respective dates and is not necessarily the actuarial increase of the underlying pension.
2. The figures set out in the table above provide information as required by the Directors' Remuneration Report Regulations 2002. The Listing Rules require the change in accrued pension to be shown excluding the effects of inflation and the transfer value of this increase. These figures are shown in the notes below.
3. The accrued pension figures shown are the annual amounts of member's pension payable from normal retirement age. Increases to pensions when in payment are applied in accordance with the relevant scheme rules. On the death of the member leaving a surviving spouse and/or children, spouse's and/or children's pensions are payable in accordance with scheme rules.
4. The benefits shown above in respect of Andy Haste relate to his membership of a defined benefit pension scheme up to the earnings cap.
5. For Andy Haste the increase in his accrued pension during the year, excluding the effects of inflation, was £1,941 p.a. and the transfer value in respect of this less his contributions was £28,340 at 31 December 2008.
6. Andy Haste is required to contribute to the scheme and also has the option of paying Additional Voluntary Contributions (AVCs). Neither voluntary contributions nor the resulting benefits are included in the table.
7. The transfer value of the accrued benefits represents the value of assets that the pension scheme would need to transfer to another pension provider on transferring the scheme's liability in respect of Andy Haste's pension benefits. The transfer values do not represent sums payable or due to Andy Haste.

Directors' emoluments and interests continued

The Company contributions paid in respect of executive directors who are members of Group defined contribution schemes, were as follows:

	Company contributions paid in 2008 £	Company contributions paid in 2007 £
George Culmer	**77,625**	70,575
Bridget McIntyre	**40,462**	57,656

Simon Lee elected not to join a Group pension plan on appointment, and receives a taxable cash allowance of 17.5% of base salary instead.

Shareholdings (non audited part)

The interests of directors in ordinary shares of 27.5p each of the Company, as declared and recorded in accordance with the FSA Listing Rules, are as follows:

	Notes	Shares held at 31 December 2008	Shares held at 1 January 2008
Executive directors			
George Culmer	1,2	**159,296**	144,344
Andy Haste	1,2	**1,158,231**	866,634
Simon Lee	1,2	**348,123**	100,528
Bridget McIntyre	1,2	**70,781**	63,126
Non-executive directors			
Noel Harwerth		**10,000**	10,000
Edward Lea		**439,801**	416,467
Malcolm Le May		**16,515**	15,360
John Maxwell		**315,057**	304,251
John Napier		**560,671**	314,265
Johanna Waterous		**–**	–

Notes:

1. In addition to the interests shown above, the directors indicated, in common with the employees, had a beneficial interest as at 31 December 2008 in 3,919,975 (2007: 4,938,894) ordinary shares of 27.5p each held in the Royal & SunAlliance ESOP Trust No 2.
2. The directors had a beneficial interest as at 31 December 2008 in the voluntary Deferred Shares of 27.5p each held under the Long Term Incentive Plan which are not included in the above table.
3. On 25 February 2009 the directors' interests remained unchanged.

Options (audited part)

Movements in option holdings during 2008 were as follows:

		Options held at 1 January 2008	Options granted during the year	Options exercised during the year	Options lapsed during the year	Options held at 31 December 2008
George Culmer	ESOS	1,994,318	–	–	–	**1,994,318**
	SAYE	12,466	–	–	–	**12,466**
Andy Haste	ESOS	7,573,433	–	–	–	**7,573,433**
	SAYE	23,858	**4,008**	**5,917**	–	**21,949**
Simon Lee	ESOS	1,355,496	–	–	–	**1,355,496**
	SAYE	23,858	**2,297**	**5,917**	–	**20,238**
Bridget McIntyre	ESOS	301,724	–	–	–	**301,724**
	SAYE	15,448	–	–	–	**15,448**

Options granted following the AGM in May 2003 are exercisable as, at the end of the period of three business years starting with the business year in which the options were granted, the Group achieved a return on capital (ROC) of at least 6% per annum (after inflation and excluding items of an exceptional nature which in the view of the Committee do not reflect the underlying performance of the business) when averaged over the period. Options granted between September 1998 and May 2003 were also subject to a performance condition that the Group must achieve a ROC of at least 6% when averaged over a consecutive three year period. This performance condition was achieved in respect of all options granted between those dates. Options granted between April 1997 and September 1998 were subject to a different performance condition linked to TSR. For options to be eligible for exercise, the Group's TSR has to be at or above the median of companies in the FTSE 100 Index over a consecutive period of three years, between the year of grant and the completion of the 10 year life of the option. The test is conducted twice per year, at the end of March and September, by independent external specialists. None of the terms or conditions of any of the existing options over shares of the Group were varied during the year. Full details of all directors' shareholdings and options to subscribe for shares are recorded in the Group's Register of Directors' Interests which is open to inspection in accordance with the provisions of the FSA Listing Rules.

The official closing middle market price at its highest during the year was 165.8p per share and at its lowest was 116.3p per share; on the last dealing day of the year it was 138.1p per share.

Options held during 2008 in respect of the ordinary shares of the Company as a result of executive and SAYE share option schemes are as follows:

	Number of options at 1 January 2008	**Number of options at 31 December 2008**	Exercise price (pence)	Dates exercisable from	Dates exercisable to
George Culmer	481,012	**481,012**	79.0	14.06.07	13.06.14
	500,000	**500,000**	76.0	18.11.07	17.11.14
	787,500	**787,500**	80.0	08.04.08	07.04.15
	225,806	**225,806**	93.0	18.08.08	17.08.15
	12,466	**12,466**	75.0	01.12.08	31.05.09
Andy Haste	3,052,915	**3,052,915**	59.0	02.04.06	01.04.13
	1,298,701	**1,298,701**	92.4	16.10.06	15.10.13
	5,917	**–**	75.0	01.12.08	31.05.09
	443,037	**443,037**	79.0	14.06.07	13.06.14
	10,643	**10,643**	59.0	01.12.09	31.05.10
	921,052	**921,052**	76.0	18.11.07	17.11.14
	1,443,750	**1,443,750**	80.0	08.04.08	07.04.15
	413,978	**413,978**	93.0	18.08.08	17.08.15
	7,298	**7,298**	75.0	01.12.10	31.05.11
	–	**4,008**	117.0	01.12.13	31.05.14
Simon Lee	206,049	**206,049**	114.05	04.06.06	03.06.13
	125,000	**125,000**	92.4	16.10.06	15.10.13
	161,392	**161,392**	79.0	14.06.07	13.06.14
	167,763	**167,763**	76.0	18.11.07	17.11.14
	525,937	**525,937**	80.0	08.04.08	07.04.15
	169,355	**169,355**	93.0	18.08.08	17.08.15
	5,917	**–**	75.0	01.12.08	31.05.09
	10,643	**10,643**	59.0	01.12.09	31.05.10
	7,298	**7,298**	75.0	01.12.10	31.05.11
	–	**2,297**	117.0	01.12.11	31.05.12
Bridget McIntyre	301,724	**301,724**	116.0	13.12.08	31.12.09
	15,448	**15,448**	106.0	31.12.08	30.06.09

Notes:
All of the above options were granted for nil consideration.

Directors' emoluments and interests continued

Long term incentive schemes (audited part)

Long term incentive scheme interests held during 2008 in respect of the ordinary shares of the Company are as follows:

Share Matching Plan

	Notes		Share awards held at 1 January 2008	Share awards granted during the year	Share awards vested during the year	Share awards exercised during the year	Share awards lapsed during the year	Share awards held at 31 December 2008	Dates by which qualifying conditions must be fulfilled
George Culmer	1,3	Deferred Share awards	128,938	–	**128,938**	–	–	**128,938**	08.04.08
		Matching Share awards	386,814	–	**386,814**	–	–	**386,814**	08.04.08
Andy Haste	1,3	Deferred Share awards	462,182	–	**265,136**	**197,046**	–	**265,136**	08.04.08
		Matching Share awards	1,017,281	–	**795,408**	**221,873**	–	**795,408**	08.04.08
Simon Lee	1,3	Deferred Share awards	96,082	–	**96,082**	**96,082**	–	–	–
		Matching Share awards	288,246	–	**288,246**	**288,246**	–	–	–
Bridget McIntyre	1,2	Deferred Share awards	150,000	–	**150,000**	**150,000**	–	–	–
		Matching Share awards	450,000	–	**450,000**	**450,000**	–	–	–

Notes:

1. The market price of ordinary shares on 14 June 2004, 8 April 2005 and 1 November 2005, the dates on which the above long term incentive scheme interests were granted, was 79.25p, 81.25p and 100p respectively.
2. Bridget McIntyre's award of Deferred and Matching Shares was approved prior to her appointment on 1 November 2005. Due to dealing restrictions in accordance with the Model Code, these awards could not be granted until 12 June 2006. The number of shares was calculated with reference to the share price on 1 November 2005. These awards vested on the third anniversary of her appointment. In all other respects these awards are subject to the same rules as other awards granted in 2005.
3. Matching Share awards are capable of vesting in respect of a maximum of three times the number of Deferred Shares awarded, subject to the achievement of TSR targets over a single two year period. TSR performance is measured relative to other companies specified by the Remuneration Committee. For awards granted in 2004 and 2005, TSR was measured partly relative to FTSE 100 companies and partly relative to the following financial services comparator group companies: Aegon, Legal & General Group, Allianz Group, Old Mutual, AXA, Prudential, AVIVA, RAS, Generali and Zurich Financial Services Group. For 50% of the Matching Share awards, where TSR is measured against the FTSE 100, full vesting will only occur at upper decile performance, vesting will occur in the ratio of shares under Matching Share awards to shares under Deferred Share awards of 2:1 at upper quartile performance and vesting in the ratio 1:1 will occur at median performance. For the other 50% of the Matching Share awards, where TSR is measured against the financial services comparator group, full vesting will occur if TSR is highest in the comparator group, vesting in the ratio 2:1 will occur at upper quartile performance and vesting in the ratio 1:1 will occur at median performance. Matching Share awards will not vest at below median performance. For awards granted in 2004, the targets were measured over the period from 1 April 2004 to 31 March 2006. For awards granted in 2005, the targets were measured over the period from 1 April 2005 to 31 March 2007. The relevant TSR figures were averaged over the three months before the beginning and end of this performance period. Additionally, no Matching Shares vest unless the Committee is satisfied that there has been a sustained improvement in the underlying performance of the Company over the performance period.

Long Term Incentive Plan

	Notes		Share awards held at 1 January 2008	**Share awards granted during the year**	**Share awards held at 31 December 2008**	Date by which qualifying conditions must be fulfilled
George Culmer	1,2,5	Deferred Shares	270,003	**172,481**	**442,484**	09.04.11
	3,5	Matching Shares	848,843	**545,974**	**1,394,817**	09.04.11
	4,5	Performance Shares	588,935	**350,518**	**939,453**	09.04.11
Andy Haste	1,2,5	Deferred Shares	550,981	**307,233**	**858,214**	09.04.11
	3,5	Matching Shares	1,732,197	**972,521**	**2,704,718**	09.04.11
	4,5	Performance Shares	1,121,498	**624,361**	**1,745,859**	09.04.11
Simon Lee	1,2,5	Deferred Shares	206,713	**137,660**	**344,373**	09.04.11
	3,5	Matching Shares	649,871	**435,751**	**1,085,622**	09.04.11
	4,5	Performance Shares	399,774	**270,921**	**670,695**	09.04.11
Bridget McIntyre	1,2,5	Deferred Shares	158,535	**114,245**	**272,780**	09.04.11
	3,5	Matching Shares	498,213	**361,632**	**859,845**	09.04.11
	4,5	Performance Shares	511,988	**256,316**	**768,304**	09.04.11

Notes:

1. The market price of ordinary shares on 9 April 2008, the date on which long term incentive scheme interests were granted during the year, was 135.7p.
2. Deferred Shares are inclusive of voluntary Deferred Shares and compulsory Deferred Shares. Voluntary Deferred Shares are purchased by Lloyds TSB Offshore Trust Company Limited on behalf of each participant using part of the net annual bonus paid to them and are held in trust for three years. These Deferred Shares are not at risk of forfeiture and may be withdrawn from the trust at any time, but the related Matching Share awards would lapse if the voluntary Deferred Shares are withdrawn within three years of acquisition. Compulsory Deferred Shares are awarded as part of the annual bonus. These Deferred Shares will normally vest in three years from the date of grant subject to continuous employment with the Group.
3. Matching Shares are capable of vesting in respect of a maximum of 2.5 times the number of Deferred Shares awarded, subject to the achievement of performance conditions over a three year period. One half of the Matching Shares relating to compulsory Deferred Shares are subject to TSR performance relative to other companies specified by the Remuneration Committee. For awards granted in 2006, 2007 and 2008 TSR will be measured relative to the following comparator group companies: Aegon, Alleanza, Allianz Group, AVIVA, AXA, Baloise, Generali, Legal & General Group, Munich Re, QBE, Swiss Re and Zurich Financial Services. Full vesting will only occur at upper quintile performance; at median performance 25% of the Matching Shares will vest. Vesting will be on a straight line basis in between. The remaining half of the Matching Shares relating to compulsory Deferred Shares (and all of the Matching Shares relating to voluntary Deferred Shares) are subject to a ROE performance condition. If underlying ROE over three years commencing on the year of grant is below 10% (12% for awards granted in 2008), no part of the award subject to ROE performance will vest. If underlying ROE over three years is 10% (12% for awards granted in 2008), 25% of the award will vest. If underlying average annual ROE over three years is 16% or higher (18% for awards granted in 2008), 100% of the awards will vest. Vesting will be on a straight line basis in between. For the purpose of establishing the number of Matching Shares relating to voluntary Deferred Shares that may be awarded, the gross value of that part of the annual bonus payment that a participant elects to voluntarily defer is used.
4. Performance conditions relating to awards of Performance Shares are the same as those relating to compulsory Deferred Shares as described above. One half of an award of Performance Shares may vest subject to the TSR performance condition and one half may vest subject to the ROE performance condition.
5. The above table shows the date by which qualifying conditions for awards made on 9 April 2008 must be fulfilled. For awards made on 12 June 2006, the date by which qualifying conditions must be fulfilled is 12 June 2009. For awards made on 16 April 2007, the date by which qualifying conditions must be fulfilled is 16 April 2010.
6. No other directors of the Company held long term incentive scheme interests during 2008.

John Maxwell

Chairman of the Remuneration Committee, on behalf of the Board

25 February 2009

Responsibility statement

We confirm to the best of our knowledge:

- The financial statements on pages 64 to 123, prepared in accordance with International Financial Reporting Standards as adopted by the EU, give a fair view of the assets, liabilities, financial position and profit of the Group
- The business review on pages 6 to 29, which is incorporated into the directors' report, includes a fair review of the development and performance of the business and the position of the Group and
- The risk framework section on pages 30 to 32, which is incorporated into the directors' report, includes a description of the principal risks and uncertainties faced by the Group.

Signed on behalf of the Board

Andy Haste
Chief Executive Officer
25 February 2009

George Culmer
Chief Financial Officer
25 February 2009

Independent auditors' report to the members of RSA Insurance Group plc

We have audited the consolidated financial statements of RSA Insurance Group plc for the year ended 31 December 2008 which comprise the consolidated income statement, the consolidated statement of recognised income and expense, the consolidated balance sheet, the consolidated cashflow statement, significant accounting policies, estimation techniques, risks, uncertainties and contingencies, risk management and related notes 1 to 34. These consolidated financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the remuneration report that is described as having been audited.

We have reported separately on the Parent Company financial statements of RSA Insurance Group plc for the year ended 31 December 2008.

This report is made solely to the Company's members, as a body, 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 members 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 members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the remuneration report and the consolidated financial statements in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union are set out in the directors' report.

Our responsibility is to audit the consolidated financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the consolidated financial statements give a true and fair view, whether the consolidated financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation and whether the part of the remuneration report described as having been audited has been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the directors' report is consistent with the consolidated financial statements. The information given in the directors' report includes that specific information presented in the Group CEO's business review, the regional business reviews and the estimation techniques, risks, uncertainties and contingencies that are cross referred from the business review section of the directors' report.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the corporate governance statement reflects the Company's compliance with the nine provisions of the 2006 Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report as described in the contents section and consider whether it is consistent with the audited consolidated financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the consolidated financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the consolidated financial statements and the part of the remuneration report to be audited. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the consolidated financial statements, and of whether the accounting policies are appropriate to the Group'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 consolidated financial statements and the part of the remuneration report to be audited 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 consolidated financial statements and the part of the remuneration report to be audited.

Opinion

In our opinion:

- The consolidated financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the Group's affairs as at 31 December 2008 and of its profit for the year then ended
- The consolidated financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation
- The part of the remuneration report described as having been audited has been properly prepared in accordance with the Companies Act 1985 and
- The information given in the directors' report is consistent with the consolidated financial statements.

Deloitte LLP
Chartered Accountants and Registered Auditors
London, UK
25 February 2009

Consolidated income statement

for the year ended 31 December 2008

	Notes	2008 £m	2007 £m
Continuing operations			
Income			
Gross written premiums		**7,273**	6,596
Less: reinsurance premiums		**(811)**	(759)
Net written premiums		**6,462**	5,837
Change in the gross provision for unearned premiums		**(112)**	(235)
Less: change in provision for unearned premiums, reinsurers' share		**8**	5
Change in provision for unearned premiums		**(104)**	(230)
Net earned premiums		**6,358**	5,607
Net investment return	2	**681**	709
Other operating income	4	**104**	113
Total income		**7,143**	6,429
Expenses			
Gross claims incurred		**(4,205)**	(4,044)
Less: claims recoveries from reinsurers		**63**	387
Net claims and benefits	3	**(4,142)**	(3,657)
Underwriting and policy acquisition costs		**(1,925)**	(1,776)
Unwind of discount		**(92)**	(81)
Other operating expenses	4	**(117)**	(119)
Total expenses		**(6,276)**	(5,633)
Results of operating activities		**867**	796
Finance costs	4	**(108)**	(104)
Profit/(loss) on disposal of subsidiaries		**18**	(22)
Net share of loss after tax of associates	11	**(18)**	–
Profit before tax on continuing operations		**759**	670
Income tax expense	5	**(173)**	(29)
Profit for the year from continuing operations		**586**	641
Discontinued operations			
Loss for the year from discontinued operations	34	**–**	(13)
Profit for the year		**586**	628
Attributable to:			
Equity holders of the Parent Company		**574**	596
Minority interests		**12**	32
		586	628
Earnings per share on profit from continuing operations attributable to the ordinary shareholders of the Parent Company			
Basic	6	**17.3p**	19.3p
Diluted	6	**17.0p**	19.0p
Earnings per share on profit attributable to the ordinary shareholders of the Parent Company			
Basic	6	**17.3p**	18.9p
Diluted	6	**17.0p**	18.6p
Ordinary dividends paid and proposed for the year			
Interim dividend paid (per share)	7	**2.73p**	2.48p
Final dividend proposed (per share)	7	**4.98p**	4.53p

The attached notes form an integral part of these consolidated financial statements.

Consolidated statement of recognised income and expense

for the year ended 31 December 2008

	2008 £m	2007 £m
Exchange gains net of tax	**326**	140
Fair value losses net of tax	**(193)**	(67)
Pension fund actuarial gains/(losses) net of tax	**204**	(16)
Net gains recognised in equity	**337**	57
Profit for the year	**586**	628
Total recognised income for the year	**923**	685
Attributable to:		
Equity holders of the Parent Company	**901**	670
Minority interests	**22**	15
	923	685

The attached notes form an integral part of these consolidated financial statements.

Consolidated balance sheet

as at 31 December 2008

	Notes	2008 £m	2007 £m
Assets			
Goodwill and other intangible assets	8	**744**	663
Property and equipment	9	**309**	377
Investment property	10	**365**	429
Investments in associates	11	**123**	105
Financial assets	12	**12,748**	11,340
Total investments		**13,236**	11,874
Reinsurers' share of insurance contract liabilities	13	**1,759**	1,872
Insurance and reinsurance debtors	14	**2,890**	2,579
Deferred acquisition costs	15	**653**	542
Current tax assets	23	**40**	19
Deferred tax assets	23	**142**	87
Other debtors and other assets	16	**1,477**	963
		1,659	1,069
Cash and cash equivalents	17	**1,614**	1,509
		22,864	20,485
Non current and disposal group assets held for sale	34	**3**	108
Total assets		**22,867**	20,593
Equity, reserves and liabilities			
Equity and reserves			
Shareholders' equity		**3,839**	3,077
Minority interests		**81**	67
Total equity and reserves	18	**3,920**	3,144
Liabilities			
Loan capital	19	**1,311**	1,194
Insurance contract liabilities	20	**15,055**	13,727
Insurance and reinsurance liabilities	21	**545**	426
Borrowings	22	**300**	303
Current tax liabilities	23	**215**	92
Deferred tax liabilities	23	**238**	224
Provisions	24	**240**	331
Other liabilities	25	**1,043**	1,087
Provisions and other liabilities		**1,736**	1,734
		18,947	17,384
Non current and disposal group liabilities held for sale	34	**–**	65
Total liabilities		**18,947**	17,449
Total equity, reserves and liabilities		**22,867**	20,593

The attached notes form an integral part of these consolidated financial statements.

The financial statements were approved on 25 February 2009 by the Board of Directors and are signed on its behalf by:

George Culmer
Chief Financial Officer

Consolidated cashflow statement

for the year ended 31 December 2008

	Notes	2008 £m	2007 £m
Cash generated from continuing operations	31	**137**	66
Tax paid		**(101)**	(127)
Interest received		**632**	587
Interest paid		**(107)**	(101)
Dividends received		**3**	1
Pension asset reallocation funding		**(37)**	(86)
Cashflows from discontinued operations		**–**	(37)
Net cashflows from operating activities		**527**	303
Proceeds from sales or maturities of:			
Investment contracts		**5,184**	8,672
Investment property		**3**	18
Property and equipment		**20**	26
Intangible assets		**–**	1
Investments in subsidiaries (net of cash disposed of)	30	**78**	(407)
Investments in associates		**–**	22
Purchase or settlement of:			
Investment contracts		**(5,528)**	(8,878)
Investment property		**(10)**	(8)
Property and equipment		**(64)**	(28)
Intangible assets		**(72)**	(66)
Investments in subsidiaries (net of cash acquired)	30	**(25)**	(52)
Investments in associates		**(32)**	(64)
Cashflows from discontinued operations		**–**	83
Net cashflows from investing activities		**(446)**	(681)
Proceeds from issue of share capital		**19**	304
Purchase of shares from minorities		**–**	(616)
Dividends paid to ordinary shareholders		**(172)**	(102)
Dividends paid to preference shareholders		**(9)**	(9)
Dividends paid to minority interests		**(8)**	(31)
Net movement in long term borrowings		**–**	(25)
Net movement in other borrowings		**(2)**	293
Net cashflows from financing activities		**(172)**	(186)
Net decrease in cash and cash equivalents and bank overdrafts		**(91)**	(564)
Cash and cash equivalents and bank overdrafts at beginning of the year		**1,538**	2,040
Effect of exchange rate changes on cash and cash equivalents		**167**	62
Cash and cash equivalents and bank overdrafts at end of the year	17	**1,614**	1,538

The attached notes form an integral part of these consolidated financial statements.

Significant accounting policies

The principal accounting policies applied in the preparation of the consolidated financial statements are set out below.

Consolidated financial statements

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). The consolidated financial statements are prepared under the historical cost convention as modified by the revaluation of available for sale financial assets, investment property, Group occupied property and financial assets and financial liabilities held for trading (which include all derivative contracts).

Except where otherwise stated, all figures included in the consolidated financial statements are presented in millions of British Pounds Sterling ('Sterling'), shown as '£m', rounded to the nearest million.

Selection of accounting policies

The Group exercises judgement in selecting each Group accounting policy. The accounting policies of the Group are selected by the directors to present financial statements that they consider provide the most relevant information. For certain accounting policies there are different accounting treatments that could be adopted, each of which would be in compliance with IFRS and would have a significant influence upon the basis on which the financial statements are presented. The bases of selection of the accounting policies for the accounting for financial assets and for the recognition of actuarial gains and losses related to pension obligations are set out below:

- The Group designates financial assets that are held as investments on the basis on which the investment return is managed and the performance is evaluated internally. Where the investment return is managed on the basis of the periodic cashflows arising from the investment, a financial asset is designated as an available for sale financial asset with unrealised gains recognised in the statement of recognised income and expense. Where the investment return is managed on the basis of the total return on the investment (including unrealised investment gains), the financial asset is designated as at fair value through the income statement
- The Group accounting policy is to recognise actuarial gains and losses arising from the recognition and funding of the Group's pension obligations in the statement of recognised income and expense during the period in which they arise. This policy has been adopted as it provides the most relevant basis of recognition of such gains and losses.

Consolidation

Subsidiaries

Subsidiaries are entities over which the Group has the power to govern the financial and operating policies so as to obtain benefits from their activities, generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group.

The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, including costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Changes in the ownership interests of a subsidiary between shareholders of the Group and minority shareholders are accounted for as transactions between equity holders of the Group. Any difference between the fair value of the consideration given by the transferee and the carrying value of the ownership interest transferred is recognised directly in equity.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries are changed where necessary to ensure consistency with the policies adopted by the Group.

Associates

Associates are entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost.

The Group's shares of its associates' post acquisition profits or losses are recognised in the income statement, and its share of post acquisition movements in reserves is recognised in reserves. The cumulative post acquisition movements are adjusted in the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Adjustments are made, where necessary, to conform the accounting policies of associates to ensure consistency with the policies adopted by the Group.

Translation of foreign currencies

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency).

The results and financial position of those Group entities whose functional currency is not Sterling are translated into Sterling as follows:

- Assets and liabilities for each balance sheet presented are translated at the closing exchange rate at the date of that balance sheet
- Income and expenses for each income statement are translated at average exchange rates during each period
- All resulting exchange differences are recognised as a component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to equity. When a foreign entity is sold, the cumulative exchange differences relating to that foreign entity are recognised in the income statement as part of the gain or loss on sale.

Goodwill arising on the acquisition of a foreign entity is treated as an asset of the foreign entity and the carrying value is translated at the closing exchange rate.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Translation differences on non monetary items, such as equities classified as available for sale financial assets, are included in the fair value reserve in equity.

Goodwill and other intangible assets

Goodwill, being the difference between the cost of a business acquisition and the Group's interest in the net fair value of the identifiable assets and liabilities acquired, is initially capitalised in the balance sheet at cost and is subsequently recognised at cost less accumulated impairment losses. The cost of the acquisition is the amount of cash paid and the fair value of other purchase consideration given together with associated expenses. Goodwill is allocated to cash generating units for the purpose of impairment testing. Each of those cash generating units represents the Group's investment within each operation. Goodwill is subject to an impairment review at least annually. An impairment review is also carried out whenever there is an indication that goodwill or other intangible assets are impaired. Where the carrying amount is more than the recoverable amount, an impairment is recognised in the income statement.

When calculating the goodwill arising on an acquisition, claims provisions are discounted to present value. Immediately following the acquisition, the claims provisions are valued at full nominal value. This increase in liabilities is matched by the recognition of an intangible asset arising from acquired claims provisions, representing the present value of future investment income implicit in the claims discount. The intangible asset is amortised over the expected run off period and is tested in the context of the liability adequacy test of insurance liabilities where the balances of intangible assets associated with insurance contracts is deducted from the carrying amount of the insurance liabilities. The run off period is normally between five and 11 years.

Expenditure that increases the future economic benefits arising from computer software in excess of its standard of performance assessed immediately before the expenditure was made is recognised as an intangible asset.

Other intangible assets comprise renewal rights, customer lists, brands and other acquired identifiable non monetary assets without physical form.

Computer software and other intangible assets are carried at cost less accumulated amortisation. Amortisation on computer software and other intangible assets is calculated using the straight line method to allocate the cost over their estimated useful lives, which is normally estimated to be between three and 12 years.

Property and equipment

Property and equipment comprise Group occupied land and buildings, fixtures, fittings and equipment (including computer hardware and motor vehicles). These assets are depreciated over their estimated useful life after taking into account residual values.

Group occupied property is stated at fair value, less subsequent depreciation for buildings. All other assets are stated at depreciated cost. Fair value movements are recorded in equity.

Fair value is based on current prices in an active market for similar property in the same location and condition and subject to similar contractual terms of ownership. Valuations are performed by external professionally qualified valuation surveyors on at least an annual basis, with reference to current market conditions.

All other classes are stated at cost less accumulated depreciation. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset only when it is probable that future economic benefits associated to the item will flow to the Group and the cost can be measured reliably.

Significant accounting policies continued

Land is not depreciated. Depreciation on all other items is calculated on the straight line method to write down the cost of such assets to their residual value over their estimated useful lives as follows:

Group occupied buildings	normally 30 years
Fixtures and fittings	10 years
Motor vehicles	4 years
Equipment	3-5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the balance sheet date.

An impairment review is carried out whenever there is an indication that the assets are impaired. An asset's carrying amount is written down to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Increases in the carrying amount arising on the revaluation of Group occupied property are credited to revaluation reserves in equity. Decreases that offset the previous increases of the same asset are charged against revaluation surplus directly in equity; other decreases are charged to the income statement. Each year the difference between depreciation based on the fair value of the asset charged to the income statement and depreciation based on the assets original cost is transferred from revaluation surplus to retained earnings.

Investment property

Investment property, comprising freehold and leasehold land and buildings, is held for long term rental yields and is not occupied by the Group.

Investment property is recorded at fair value, measured by independent professionally qualified valuers, who hold a recognised and relevant professional qualification and have recent experience in the location and category of the investment property being valued. Valuations are carried out on an annual basis or more frequently and by internal valuers for interim periods, with reference to current market conditions. Related unrealised gains and unrealised losses or changes thereof are recognised in net investment return.

Financial assets

A financial asset is initially recognised, on the date the Group commits to purchase the asset, at fair value plus, in the case of all financial assets not classified as at fair value through the income statement, transaction costs that are directly attributable to its acquisition. A financial asset is derecognised when the rights to receive cashflows from the investment have expired or have been transferred and when the Group has transferred substantially the risks and rewards of ownership of the asset.

On initial recognition, the financial assets may be categorised into the following categories: financial assets at fair value through the income statement, loans and receivables, held to maturity financial assets and available for sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition.

The Group designates investments in accordance with its investment strategy on the basis on which the investment return is managed and the performance is evaluated internally. Where the investment return is managed on the basis of the periodic cashflows arising from the investment, a financial asset is designated as an available for sale financial asset. Where the investment return is managed on the basis of the total return on the investment (including unrealised investment gains), the financial asset is designated as at fair value through the income statement.

Financial assets arising from non investment activities are not classified on initial recognition as available for sale assets and are therefore categorised as loans and receivables.

Where the cumulative changes recognised in equity represent an unrealised loss the individual asset or group of assets is reviewed to test whether an indication of impairment exists.

For securities whose fair values are readily determined and where there is objective evidence that such an asset is impaired, including a significant or prolonged decline in the fair value below cost, the unrealised loss charged to equity is reclassified to the income statement.

If the fair value of a previously impaired debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed and the reversal recognised in the income statement. Impairment losses on equity investments are not reversed.

For other loans and receivables, where there is evidence that the contracted cashflows will not be received in full, an impairment charge is recognised in the income statement to reduce the carrying value of the financial asset to its recoverable amount.

Investment income is recognised in the income statement. Dividends on equity investments are recognised on the date at which the investment is priced 'ex dividend'. Interest income is recognised using the effective interest method. Unrealised gains and losses on available for sale investments are recognised directly in equity, except for impairment losses and foreign exchange gains and losses on monetary items (which are recognised in the income statement). On derecognition of an investment classified as available for sale, the cumulative gain or loss previously recognised in equity is recognised in the income statement.

Derivative financial instruments

Derivatives are recognised in the balance sheet on a trade date basis and are carried at fair value. Derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and the nature of the item being

hedged. Where a derivative is not designated as a hedging instrument, changes in its fair value are recognised in the income statement.

Hedging

Transactions are classified as hedging transactions when the following conditions for hedge accounting are met:

- There is a formal designation and documentation of the hedging relationship and the Group's risk management objective and strategy for undertaking the hedge
- The hedge is expected to be highly effective in achieving offsetting changes in fair value or cashflows attributable to the hedged risk, consistent with the originally documented risk management strategy for that particular hedging relationship
- The effectiveness of the hedge can be reliably measured
- For cashflow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cashflows that could ultimately affect profit or loss
- The hedge is assessed on an ongoing basis and determined to have been highly effective.

Where loan capital or a forward foreign exchange contract is designated as a hedging instrument against the net investment in foreign entities, the effective portion of the hedge is recognised in equity; the gain or loss relating to the ineffective portion is recognised immediately in the income statement. Gains and losses accumulated in equity are included in the income statement when the underlying hedged item is derecognised.

Estimation of the fair value of financial assets and liabilities

The methods and assumptions used by the Group in estimating the fair value of financial assets and liabilities are:

- For fixed maturity securities, fair values are generally based upon quoted market prices. Where market prices are not readily available, fair values are estimated using either values obtained from quoted market prices of comparable securities or estimated by discounting expected future cashflows using a current market rate applicable to the yield, credit quality and maturity of the investment
- For equity securities fair values are based upon quoted market prices
- If the market for a financial asset is not active, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cashflow analysis and option pricing models
- For mortgage loans on real estate and collateral loans, fair values are estimated using discounted cashflow calculations based upon prevailing market rates
- For cash, short term investments, commercial paper, other assets, liabilities and accruals, carrying amounts approximate to fair values
- For notes, bonds, loans payable and loan capital, fair values are determined by reference to quoted market prices or estimated using discounted cashflow calculations based upon prevailing market rates. Loan capital is carried at amortised cost and, when different, fair value is shown in the relevant note. For borrowings that carry a variable rate of interest (other than loan capital), carrying values approximate to fair values
- For derivatives, fair values are generally based upon quoted market prices.

Insurance contracts

Product classification

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk is transferred when the Group agrees to compensate a policyholder if a specified uncertain future event (other than a change in a financial variable) adversely affects the policyholder. Any contracts not meeting the definition of an insurance contract under IFRS are classified as investment contracts or derivative contracts, as appropriate.

Recognition of income

Premiums written are accounted for in the period in which the contract is entered into and include estimates where the amounts are not determined at the balance sheet date. Premiums written exclude taxes and duties levied on premiums and directly related expenses, e.g. commissions. Premiums are earned as revenue over the period of the contract and are calculated principally on a daily pro rata basis.

Acquisition costs

Acquisition costs comprise the direct and indirect costs of obtaining and processing new insurance business. These costs are recognised as a deferred acquisition cost asset and amortised on the same basis as the related premiums are earned.

Insurance liabilities

The provision for unearned premium represents the portion of the premiums written relating to periods of insurance coverage subsequent to the balance sheet date.

The provisions for claims outstanding, whether reported or not, comprise the estimated cost of claims incurred but not settled at the balance sheet date. It includes related expenses and a deduction for the expected value of salvage and other recoveries. The provision is determined using the best information available of claims settlement patterns, forecast inflation and settlement of claims. The provisions for claims outstanding relating to long term permanent disability claims in Canada and Scandinavia are also determined using recognised actuarial methods.

The provisions for claims outstanding, and related reinsurance recoveries, are discounted where there is a particularly long period from incident to claims settlement and where there exists a suitable claims payment pattern from which to calculate the discount. In defining those claims with a long period from incident to claims settlement, those categories of claims where the average period of settlement is six years

Significant accounting policies continued

or more from the balance sheet date has been used as a guide. The discount rate used is based upon an investment return expected to be earned by assets, which are appropriate in magnitude and nature to cover the provisions for claims outstanding being discounted, during the period necessary for the payment of such claims.

Differences between the estimated cost and subsequent settlement of claims are recognised in the income statement in the year in which they are settled or in which the provisions for claims outstanding are re-estimated.

At each balance sheet date an assessment is made of whether the provisions for unearned premiums are adequate. A separate provision is made, based on information available at the balance sheet date, for any estimated future underwriting losses relating to unexpired risks. The provision is calculated after taking into account future investment income that is expected to be earned from the assets backing the provisions for unearned premiums (net of deferred acquisition costs). The unexpired risk provision is assessed in aggregate for business classes which, in the opinion of the directors, are managed together.

Reinsurance ceded

Premiums payable in respect of reinsurance ceded are recognised in the period in which the reinsurance contract is entered into and include estimates where the amounts are not determined at the balance sheet date. Premiums are expensed over the period of the reinsurance contract, calculated principally on a daily pro rata basis.

A reinsurance asset (reinsurers' share of insurance liabilities) is recognised to reflect the amount estimated to be recoverable under the reinsurance contracts in respect of the outstanding claims reported under insurance liabilities. The amount recoverable from reinsurers is initially valued on the same basis as the underlying claims provision. The amount recoverable is reduced when there is an event arising after the initial recognition that provides objective evidence that the Group may not receive all amounts due under the contract and the event has a reliably measurable impact on the expected amount that will be recovered from the reinsurer.

The reinsurers' share of each unexpired risk provision is recognised on the same basis.

Annuities purchased by the Group to make payments under structured settlement arrangements are accounted for as reinsurance ceded if the Group remains liable for the settlement in the event of default by the annuity provider. Any gain or loss arising on the purchase of an annuity is recognised in the income statement at the date of purchase.

Cash and cash equivalents

Cash and cash equivalents are short term, highly liquid investments that are subject to insignificant changes in value and are readily convertible into known amounts of cash. Cash equivalents comprise financial assets with less than three months maturity from the date of acquisition.

Treasury shares

Treasury shares are deducted from equity. No gain or loss is recognised on the purchase, sale, issue or cancellation of the treasury shares. Any consideration paid or received is recognised directly in equity.

Loan capital

Loan capital comprises subordinated bonds which are initially measured at the consideration received less transaction costs. Subsequently, loan capital is measured at amortised cost using the effective interest rate method.

An exchange with an existing lender of loan capital with substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cashflows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cashflows of the original financial liability. An exchange where the terms are not substantially different is accounted for as an exchange.

If an exchange of loan capital or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If it is accounted for as an exchange, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability and no adjustment is made to the carrying value of the liability to reflect its fair value at the date of exchange.

Taxation

Taxation in the income statement is based on profits and income for the year as determined in accordance with the relevant tax legislation, together with adjustments to provisions for prior years. UK tax in respect of overseas subsidiaries and principal associated undertakings is recognised as an expense in the year in which the profits arise, except where the remittance of earnings can be controlled and it is probable that remittance will not take place in the foreseeable future, in which case UK tax is based on dividends received.

Deferred tax is provided in full using the liability method on temporary differences arising between the tax bases of assets and liabilities and the carrying amounts in the financial statements. However, if the deferred tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting, nor taxable profit or loss, it is not accounted for. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the related deferred tax liability is settled.

Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which these temporary differences can be utilised.

Employee benefits

Pension obligations

Group companies operate various pension schemes. The schemes are generally funded through payments to trustee administered funds, determined by periodic actuarial calculations. The Group has both defined contribution and defined benefit schemes. A defined contribution scheme is a pension scheme under which the Group pays fixed contributions into a separate entity. A defined benefit scheme is a pension scheme that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary.

Post retirement benefits (including pension schemes and post retirement health schemes)

Contributions to defined contribution pension schemes are charged in the period in which the employment services qualifying for the benefit are provided. The Group has no further payment obligations once the contributions have been paid.

The amounts charged (or credited where relevant) in the income statement relating to post retirement benefits in respect of defined benefit schemes are as follows:

- The current service cost
- The past service costs for additional benefits granted in the current or earlier periods
- The interest cost for the period
- The impact of any curtailments or settlements during the period
- The expected return on scheme assets (where relevant).

The current service cost in respect of defined benefit schemes comprises the present value of the additional benefits attributable to employees' services provided during the period.

The present value of defined benefit obligations and the present values of additional benefits accruing during the period are calculated using the Projected Unit Credit Method.

Past service costs arise where additional benefits are granted. The cost of providing additional benefits is recognised on a straight line basis over the remaining period of service until such benefits vest. The cost of providing additional benefits that vest on their introduction are recognised immediately.

The calculation of the present value of accrued benefits includes an actuarial assumption of future interest rates, which is used to discount the expected ultimate cost of providing the benefits. The discount rate is determined at each balance sheet date by reference to current market yields on high quality corporate bonds identified to match the currency and estimated term of the obligations. The interest cost for the period is calculated by multiplying the discount rate determined at the start of the period by the defined benefit obligations during the period.

The change in the present value of the defined benefit obligation and the changes in the fair value of scheme assets resulting from any curtailments and settlements of scheme liabilities during the period are recognised in the income statement. Additionally, any previously unrecognised past service costs related to these liabilities are recognised in the gains or losses on settlement and curtailment.

The expected returns on scheme assets are determined for each asset class, at the beginning of the period, as the expected investment returns on scheme assets over the entire life of the related obligations. All returns are net of investment expenses.

Actuarial gains and losses arise from changes to actuarial assumptions when revaluing future benefits and from actual experience in respect of scheme liabilities and investment performance of scheme assets being different from previous assumptions. Actuarial gains and losses are recognised in the statement of recognised income and expense.

The value recognised in the balance sheet for each individual post retirement scheme is calculated as follows:

- The present value of defined benefit obligation of the scheme at the balance sheet date
- Minus any past service cost not yet recognised
- Minus the fair value at the balance sheet date of the scheme assets out of which the obligations are to be settled directly.

For those individual schemes in deficit, the resulting net liabilities are recognised on the consolidated balance sheet in provisions. For those individual schemes in surplus, an asset is recognised on the balance sheet in other debtors and other assets to the extent that the Group can realise an economic benefit, in the form of a refund or a reduction in future contributions, at some point during the life of the scheme or when the scheme liabilities are settled.

Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after the balance sheet date are discounted to present value.

Share based payment

The value of the employee share options and other equity settled share based payments is calculated at fair value at the grant date using appropriate and recognised option pricing models. The value of liabilities in respect of cash settled share based payment transactions is based upon the fair value of the awards at the balance sheet date.

Significant accounting policies continued

Vesting conditions, which comprise service conditions and performance conditions, other than those based upon market conditions, are not taken into account when estimating the fair value of such awards but are taken into account by adjusting the number of equity instruments included in the ultimate measurement of the transaction amount. The value of the awards is recognised as an expense on a systematic basis over the period during which the employment services are provided. Where an award of options is cancelled by an employee, the full value of the award (less any value previously recognised) is recognised at the cancellation date.

The proceeds received net of any transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Dividends to equity holders

The final dividend is recognised as a liability when approved at the Annual General Meeting. The interim dividend is recognised as a liability when paid.

Leases

Rental income from operating leases is recognised on a straight line basis over the term of the lease. Payments made under operating leases are charged on a straight line basis over the term of the lease.

Operating segments

Operating segments are identified on the basis of the regional structure of the Group. Internal reports about these segments are regularly reviewed by the Group Chief Executive Officer and by the Board of Directors to assess their performance and to allocate capital and resources.

Non current and disposal group assets and liabilities held for sale and discontinued operations

Non current and disposal group assets are classified as held for sale if their carrying amount is to be recovered principally through a sale transaction, that is highly probable to complete within one year from the date of classification, rather than through continuing use. Such assets are measured at the lower of carrying amount and fair value less costs to sell and are classified separately from other assets in the balance sheet. Assets and liabilities of a disposal group are not netted. In the period where a non current asset or disposal group is recognised for the first time the balance sheet for the comparative prior period presented is not restated.

Discontinued operations are presented on the face of the income statement as a single amount comprising the total of the net profit or loss of discontinued operations and the after tax gain or loss recognised on the sale or the measurement to fair value less costs to sell of the net assets constituting the discontinued operations. In the period where an operation is presented for the first time as discontinued, the income statement for the comparative prior period presented is restated to present that operation as discontinued.

Unless otherwise stated, in the period where an operation is presented as discontinued, the notes to the financial statements contain amounts attributable to continuing operations only. The comparatives for the notes to the income statement are restated.

Current and non current distinction

Assets are classified as current when expected to be realised within the Group's normal operating cycle of one year. Liabilities are classified as current when expected to be settled within the Group's normal operating cycle of one year. All other assets and liabilities are classified as non current.

The Group's consolidated balance sheet is not presented using current and non current classifications. However, the following balances are generally classified as current: cash and cash equivalents; deferred acquisition costs; and insurance and reinsurance debtors.

The following balances are generally classified as non current: goodwill and other intangible assets; property and equipment; investment property; investment in associates; financial assets; deferred tax assets; loan capital; and deferred tax liabilities.

The remaining balances are of a mixed nature. The current and non current portions of such balances are set out in the respective notes or in the risk management section.

Recently issued accounting pronouncements

Pronouncements issued by the International Accounting Standards Board (IASB) but which are not yet mandatory for adoption in the Group financial statements are listed below:

a) Published standards and amendments to published standards that are not yet effective but which have been early adopted by the Group

- The Group first adopted IFRS 8 'Operating segments' in its financial statements in 2007. IFRS 8 is mandatory for accounting periods beginning on or after 1 January 2009.

b) Published standards and amendments to published standards that are not yet effective and have not been early adopted by the Group

- On 6 September 2007 the IASB issued a revised version of IAS 1 'Presentation of Financial Statements'.

  The revised standard changes certain aspects of the presentation of financial statements including the mandatory introduction of a statement of comprehensive income. The revised standard gives preparers of financial statements the option of presenting items of income and expense and components of other comprehensive income either in a single statement of comprehensive income with subtotals, or in two separate statements (a separate income statement followed by a statement of comprehensive income). In addition, the revisions include changes in the titles of some of the financial statements to standardise accounting terminology (for example, the balance sheet is renamed a statement of financial position). The new titles will be used in accounting standards, but are not mandatory for use in financial statements.

  The revised standard will come into effect for the annual periods beginning on or after 1 January 2009, but early adoption is permitted. The revisions will result in changes to the presentation of the financial statements but are not expected to change the results or the earnings per share of the current period, the comparative period or earlier periods, and the Group's financial position at the end of each such period.

- On 10 January 2008 the IASB issued a revised version of IFRS 3 'Business Combinations' and an amended version of IAS 27 'Consolidated and Separate Financial Statements'. The revisions include the following changes to existing accounting practice:

  - An equity interest in a subsidiary entity that is not held by the reporting and controlling entity is now described as a non controlling interest (currently described as a minority interest)
  - Total comprehensive income is attributed to a non controlling interest even if this results in the non controlling interest having a deficit balance
  - A change in a controlling interest arising from a transaction between a controlling interest and a non controlling interest that does not result in a loss of control, is accounted for as an equity transaction
  - In a business combination, the acquiring company must measure the non controlling interest at either fair value or as the non controlling interest's proportionate share of the identifiable net assets. Currently only the second basis is permitted
  - Costs incurred by the acquirer in connection with a business combination must be accounted for separately from the business combination. This will result in such costs being expensed and not being included in goodwill
  - All consideration (including contingent consideration) transferred in a business combination is measured at fair value at the acquisition date. Changes in the value of contingent consideration are measured in accordance with the relevant accounting treatment under IFRS
  - Pre-existing equity interests in an acquiree are remeasured to fair value at the date of, and immediately before, the business combination and any resulting gain or loss is recognised in the income statement.

The revised standards will come into effect for the annual periods beginning on or after 1 July 2009, but early adoption is permitted. The revised standards have not yet been adopted by the EU. The new standards will be applied prospectively and so will have no impact on the results and the earnings per share of the current period, the comparative period or earlier periods, and on the Group's financial position at the end of each such period. It is not possible to assess the impact the changes will have on future periods.

c) Other standards and interpretations to published standards issued that are not relevant for the Group's operations or not expected to change accounting policies

- Amendment to IAS 23 'Borrowing Costs' (issued 29 March 2007)
- Interpretation IFRIC 13 'Customer Loyalty Programmes' (issued 28 June 2007)
- Amendment to IFRS 2 'Share Based Payment' (issued 17 January 2008)
- Amendments to IAS 32 'Financial Instruments: Presentation' and IAS 1 'Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation' (issued 14 February 2008)
- Improvements to IFRSs (issued 22 May 2008)
- Amendments to IFRS 1 and IAS 27 'Cost of an investment in a subsidiary, jointly controlled entity or associate' (issued 22 May 2008)
- Interpretation IFRIC 15 'Agreements for the Construction of Real Estate' (issued 3 July 2008)
- Interpretation IFRIC 16 'Hedges of a Net Investment in a Foreign Operation' (issued 3 July 2008)
- Amendment to IAS 39 'Financial Instruments: Recognition and Measurement: Eligible Hedged Items' (issued 31 July 2008)
- Interpretation IFRIC 17 'Distributions of Non cash Assets to Owners' (issued 27 November 2008)
- Revised IFRS 1 'First Time Adoption of IFRS' (issued 27 November 2008).

None of the above are anticipated to have a material impact on the Group financial statements.

Estimation techniques, risks, uncertainties and contingencies

Introduction

One of the purposes of insurance is to enable policyholders to protect themselves against uncertain future events. Insurance companies accept the transfer of uncertainty from policyholders and seek to add value through the aggregation and management of these risks.

The uncertainty inherent in insurance is inevitably reflected in the financial statements of insurance companies. The uncertainty in the financial statements principally arises in respect of the insurance liabilities of the company.

The insurance liabilities of an insurance company include the provision for unearned premiums and unexpired risks and the provision for outstanding claims. Unearned premiums and unexpired risks represent the amount of income set aside by the company to cover the cost of claims that may arise during the unexpired period of risk of insurance policies in force at the balance sheet date. Outstanding claims represent the company's estimate of the cost of settlement of claims that have occurred by the balance sheet date but have not yet been finally settled.

In addition to the inherent uncertainty of having to make provision for future events, there is also considerable uncertainty as regards the eventual outcome of the claims that have occurred by the balance sheet date but remain unsettled. This includes claims that may have occurred but have not yet been notified to the company and those that are not yet apparent to the insured.

As a consequence of this uncertainty, the insurance company needs to apply sophisticated estimation techniques to determine the appropriate provisions.

Estimation techniques

Claims and unexpired risks provisions are determined based upon previous claims experience, knowledge of events and the terms and conditions of the relevant policies and on interpretation of circumstances. Particularly relevant is experience with similar cases and historical claims payment trends. The approach also includes the consideration of the development of loss payment trends, the potential longer term significance of large events, the levels of unpaid claims, legislative changes, judicial decisions and economic and political conditions.

Where possible, the Group adopts multiple techniques to estimate the required level of provisions. This assists in giving greater understanding of the trends inherent in the data being projected. The Group's estimates of losses and loss expenses are reached after a review of several commonly accepted actuarial projection methodologies and a number of different bases to determine these provisions. These include methods based upon the following:

- The development of previously settled claims, where payments to date are extrapolated for each prior year
- Estimates based upon a projection of claims numbers and average cost
- Notified claims development, where notified claims to date for each year are extrapolated based upon observed development of earlier years and
- Expected loss ratios.

In addition, the Group uses other methods such as the Bornhuetter-Ferguson method, which combines features of the above methods. The Group also uses bespoke methods for specialist classes of business. In selecting its best estimate, the Group considers the appropriateness of the methods and bases to the individual circumstances of the provision class and underwriting year. The process is designed to select the most appropriate best estimate.

Large claims impacting each relevant business class are generally assessed separately, being measured either at the face value of the loss adjusters' estimates or projected separately in order to allow for the future development of large claims.

Provisions are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable from reinsurers based upon the gross provisions and having due regard to collectability.

The claims provisions are subject to close scrutiny both within the Group's business units and at Group Corporate Centre. In addition, for major classes where the risks and uncertainties inherent in the provisions are greatest, regular and ad hoc detailed reviews are undertaken by advisers who are able to draw upon their specialist expertise and a broader knowledge of current industry trends in claims development. As an example, the Group's exposure to asbestos and environmental pollution is examined on this basis. The results of these reviews are considered when establishing the appropriate levels of provisions for outstanding claims and unexpired periods of risk.

It should be emphasised that the estimation techniques for the determination of insurance liabilities involve obtaining corroborative evidence from as wide a range of sources as possible and combining these to form the overall estimate. This technique means that the estimate is inevitably deterministic rather than stochastic. A stochastic valuation approach, whereby a range of possible outcomes is estimated and probabilities assigned thereto, is only possible in a limited number of situations.

The pension assets and pension and post retirement liabilities are calculated in accordance with International Accounting Standard 19 (IAS 19). The assets, liabilities and income statement charge, calculated in accordance with IAS 19, are sensitive to the assumptions made from time to time, including inflation, interest rate, investment return and mortality. IAS 19 compares, at a given date, the current market value of a pension fund's assets with its long term liabilities, which are calculated using a discount rate in line with yields on 'AA' rated bonds of suitable duration and currency. As such, the financial position of a pension fund on this basis is highly sensitive to changes in bond rates and will also be impacted by changes in equity markets.

Uncertainties and contingencies

The uncertainty arising under insurance contracts may be characterised under a number of specific headings, such as:

- Uncertainty as to whether an event has occurred which would give rise to a policyholder suffering an insured loss
- Uncertainty as to the extent of policy coverage and limits applicable
- Uncertainty as to the amount of insured loss suffered by a policyholder as a result of the event occurring and
- Uncertainty over the timing of a settlement to a policyholder for a loss suffered.

The degree of uncertainty will vary by policy class according to the characteristics of the insured risks and the cost of a claim will be determined by the actual loss suffered by the policyholder.

There may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the Group. Following the identification and notification of an insured loss, there may still be uncertainty as to the magnitude and timing of the settlement of the claim. There are many factors that will determine the level of uncertainty such as inflation, inconsistent judicial interpretations and court judgments that broaden policy coverage beyond the intent of the original insurance, legislative changes and claims handling procedures.

The establishment of insurance liabilities is an inherently uncertain process and, as a consequence of this uncertainty, the eventual cost of settlement of outstanding claims and unexpired risks can vary substantially from the initial estimates, particularly for the Group's long tail lines of business. The Group seeks to provide appropriate levels of claims provision and provision for unexpired risks taking the known facts and experience into account.

The Group has exposures to risks in each class of business within each operating segment that may develop and that could have a material impact upon the Group's financial position. The geographic and insurance risk diversity within the Group's portfolio of issued insurance policies make it not possible to predict whether material development will occur and, if it does occur, the location and the timing of such an occurrence. The estimation of insurance liabilities involves the use of judgments and assumptions that are specific to the insurance risks within each territory and the particular type of insurance risk covered. The diversity of the insurance risks results in it not being possible to identify individual judgments and assumptions that are more likely than others to have a material impact on the future development of the insurance liabilities.

The sections below identify a number of specific risks relating to asbestos and environmental claims. There may be other classes of risk which could develop in the future and that could have a material impact on the Group's financial position.

The Group evaluates the concentration of exposures to individual and cumulative insurance risk and establishes its reinsurance policy to reduce such exposure to levels acceptable to the Group.

Asbestos and environmental claims

The estimation of the provisions for the ultimate cost of claims for asbestos and environmental pollution is subject to a range of uncertainties that is generally greater than those encountered for other classes of insurance business. As a result it is not possible to determine the future development of asbestos and environmental claims with the same degree of reliability as with other types of claims, particularly in periods when theories of law are in flux. Consequently, traditional techniques for estimating claims provisions cannot wholly be relied upon and the Group employs specialised techniques to determine provisions using the extensive knowledge of both internal asbestos and environmental pollution experts and external legal and professional advisors.

Factors contributing to this higher degree of uncertainty include:

- The long delay in reporting claims from the date of exposure (for example, cases of mesothelioma can have a latent period of up to 40 years). This makes estimating the ultimate number of claims we will receive particularly difficult
- Issues of allocation of responsibility among potentially responsible parties and insurers
- Emerging court decisions and the possibility of retrospective legislative changes increasing or decreasing insurer liability
- The tendency for social trends and factors to influence court awards
- Developments pertaining to the Group's ability to recover reinsurance for claims of this nature and
- For US liabilities from our London market business, developments in the tactics of US plaintiff lawyers and court decisions and awards.

Acquisitions and disposals

The Group makes acquisitions and disposals of businesses as part of its normal operations. All acquisitions are made after due diligence, which will include, amongst other matters, assessment of the adequacy of claims reserves, assessment of the recoverability of reinsurance balances, inquiries with regard to outstanding litigation and inquiries of local regulators and taxation authorities. Consideration is also given to potential costs, risks and issues in relation to the integration of any proposed acquisitions with existing RSA operations. The Group will seek to receive the benefit of appropriate contractual representations and warranties in connection with any acquisition and, where necessary, additional indemnifications in relation to specific risks although there can be no guarantee that such protection will be adequate in all circumstances. The Group may also provide relevant representations, warranties and indemnities to counterparties on any disposal. While such representations, warranties and indemnities are essential components of many contractual relationships, they do not represent the underlying purpose for the transaction.

These clauses are customary in such contracts and may from time to time lead to us receiving claims from counterparties.

Estimation techniques, risks, uncertainties and contingencies continued

Contracts with third parties

The Group enters into joint ventures, outsourcing contracts and distribution arrangements with third parties in the normal course of its business and is reliant upon those third parties being willing and able to perform their obligations in accordance with the terms and conditions of the contracts.

Litigation, disputes and investigations

The Group, in common with the insurance industry in general, is subject to litigation, mediation and arbitration, and regulatory, governmental and other sectoral inquiries and investigations in the normal course of its business. In addition the Group is exposed to the risk of litigation in connection with its former ownership of the US operation. The directors do not believe that any current mediation, arbitration, regulatory, governmental or sectoral inquiries and investigations and pending or threatened litigation or dispute will have a material adverse effect on the Group's financial position, although there can be no assurance that losses or financial penalties resulting from any current mediation, arbitration, regulatory, governmental or sectoral inquiries and investigations and pending or threatened litigation or dispute will not materially affect the Group's financial position or cashflows for any period.

Reinsurance

The Group is exposed to disputes on, and defects in, contracts with its reinsurers and the possibility of default by its reinsurers. The Group is also exposed to the credit risk assumed in fronting arrangements and to potential reinsurance capacity constraints. In selecting the reinsurers with whom we do business our strategy is to seek reinsurers with the best combination of financial strength, price and capacity. We publish internally a list of authorised reinsurers who pass our selection process and which our operations may use for new transactions.

The Group monitors the financial strength of its reinsurers, including those to whom risks are no longer ceded. Allowance is made in the financial position for non recoverability due to reinsurer default by requiring operations to provide, in line with Group standards, having regard to companies on the Group's 'Watch List'. The 'Watch List' is the list of companies whom the directors believe will not be able to pay amounts due to the Group in full.

Investment risk

The Group is exposed to market risk and credit risk on its invested assets. Market risk includes the risk of potential losses from adverse movements in market rates and prices including interest rates, equity prices, property prices and foreign currency exchange rates. The Group's exposure to market risks is controlled by the setting of investment limits in line with the Group's risk appetite. From time to time the Group also makes use of derivative financial instruments to reduce exposure to adverse fluctuations in interest rates, foreign exchange rates and equity markets. The Group has strict controls over the use of derivative instruments.

Credit risk includes the non performance of contractual payment obligations on invested assets and adverse changes in the credit worthiness of invested assets including exposures to issuers or counterparties for bonds, equities, deposits and derivatives. Limits are set at both a portfolio and counterparty level based on likelihood of default to manage the Group's overall credit profile and specific concentrations within risk appetite.

Our insurance investment portfolios are concentrated in listed securities with very low levels of exposure to assets without quoted market prices. We use model based analysis to verify asset values when market values are not readily available.

Rating environment

The ability of the Group to write certain types of insurance business is dependent on the maintenance of the appropriate credit ratings from the rating agencies. The Group has the objective of maintaining single 'A' ratings. At the present time the ratings are 'A' (stable) from S&P upgraded from 'A-' in December 2007, 'A-' (positive outlook) from AM Best and 'A2' (stable) from Moody's upgraded from 'A3' in December 2008. Any worsening in the ratings could have an adverse impact on the ability of the Group to write certain types of general insurance business.

In assessing credit risk in relation to reinsurance and investments, the Group takes into account a variety of factors, including credit rating. If any such rating changes, or is otherwise reassessed, this has potential implications for the related exposures.

Changes in foreign exchange rates may impact our results

We publish our consolidated financial statements in Pounds Sterling. Therefore, fluctuations in exchange rates used to translate other currencies, particularly other European currencies and the US Dollar, into Pounds Sterling will impact our reported consolidated financial condition, results of operations and cashflows from period to period. These fluctuations in exchange rates will also impact the Pound Sterling value of our investments and the return on our investments.

Income and expenses for each income statement item are translated at average exchange rates. Balance sheet assets and liabilities are translated at the closing exchange rates at the balance sheet date.

Regulatory environment

The legal, regulatory and accounting environment is subject to significant change in many of the jurisdictions in which we operate, including developments in response to changes in the economic and political environment. We continue to monitor the developments and react accordingly.

In particular the Group is continuing to monitor and respond to developments relating to the Solvency II Framework Directive, which is intended, in the medium term, to achieve greater harmonisation of approach across European member states to assessing capital resources and requirements. The directors are confident that the Group will continue to meet all future regulatory capital requirements.

Risk management

As an insurance company, the Group is fundamentally concerned with the management of risks. This note summarises the key risks to the Group and the steps taken to manage them.

As set out in the corporate governance report, the Group's Board of Directors (the 'Board') defines the risk appetite of the organisation.

The Group employs a comprehensive risk management framework to identify, assess, manage and monitor the risks arising as a result of operating the business. The framework includes a comprehensive suite of risk policies, procedures, measurement, reporting and monitoring techniques and a series of stress tests and scenario analyses to ensure that the Group's risk exposures are managed appropriately.

The Group is exposed to financial risk through its financial assets, financial liabilities (investment contracts and borrowings), reinsurance assets and insurance liabilities. In particular the key financial risk is that the proceeds from the realisation of its financial assets are not sufficient to fund the obligations arising from its insurance and investment contracts.

The Group manages its financial assets within a framework that has been developed to seek to ensure the ability to meet its obligations under insurance and investment contracts. A key principle behind this process is to hold assets of sufficient credit quality and currency that provide a broad match against the liabilities arising from insurance and investment contracts.

The components of insurance, reinsurance, credit, market and liquidity risk management are addressed below:

Insurance risk

The Group's insurance activities are primarily concerned with the pricing, acceptance and management of risks from its customers. In accepting risk the Group is committing to the payment of claims and therefore these risks must be understood and controlled. Disciplined underwriting, encompassing risk assessment, risk management, pricing and exposure control is critical to the Group's success.

Property and casualty insurance risks

The Group manages these risks through its underwriting strategy, adequate reinsurance arrangements and proactive claims handling. The underwriting strategy aims to ensure that the underwritten risks are well diversified in terms of type and amount of risk, industry and geography.

Pricing for property and casualty products is generally based upon historical claims frequencies and claims severity averages, adjusted for inflation and trended forward to recognise anticipated changes in claims patterns. While claims remain the Group's principal cost, the Group also makes allowance in the pricing procedures for acquisition expenses, administration expenses, investment income, the cost of reinsurance and for a profit loading that adequately covers the cost of the capital the Group exposes to risk.

Underwriting limits are in place to enforce appropriate risk selection criteria. For example, the Group has the right not to renew individual policies, it can impose deductibles and it has the right to reject the payment of a fraudulent claim. In certain territories, legislation imposes a minimum amount for which employers can be liable for claims for compensation from employees injured at work. These liabilities are usually insured under an employers' liability (or similar) insurance policy; all policies issued by the Group comply with minimum statutory requirements.

All of the Group's underwriters have specific licences that set clear parameters for the business they can underwrite, based on the experience of the individual underwriter. Additionally the Group has a centrally managed forum looking at Group underwriting issues, reviewing and agreeing underwriting direction and setting policy and directives where appropriate. The Group has a quarterly portfolio management process across all its business units, which provides a consistent assessment of each portfolio performance against a set of key performance indicators. Under the portfolio management system, key risk indicators are tracked to monitor emerging trends, opportunities and risks and, on an annual basis, a review forum of business and underwriting leaders undertakes a detailed review of each portfolio utilising data from the quarterly reviews.

Reinsurance arrangements in place include excess, stop loss and catastrophe coverage. The effect of such reinsurance arrangements is that the Group should not suffer total net insurance losses beyond the Group's risk appetite in any one year.

Reserves – an overview

The Group establishes property and casualty loss reserves to account for the anticipated ultimate costs of all losses and related loss adjustment expenses (LAE) on losses that have already occurred. The Group establishes reserves for reported losses and LAE, as well as for incurred but not yet reported (IBNR) losses and unallocated loss adjustment expenses (ULAE). Loss reserve estimates are based on known facts and on interpretation of circumstances including the Group's experience with similar cases and historical claims payment trends. The Group also considers the development of loss payment trends, levels of unpaid claims, judicial decisions and economic conditions.

Risk management continued

The Group uses a variety of statistical techniques and a number of different bases to set reserves, depending on the business unit and line of business in question. The Group's reserving managers consider claims developments separately for each line of business and subdivide certain lines of business by major claim types or sub classifications of business. Large claims impacting each relevant account are also generally assessed separately, either being reserved at the face value of the loss adjusters' estimates or projected separately in order to allow for the future development of large claims.

The Group has a Group Reserving Committee consisting of the Group Chief Executive Officer, Chief Financial Officer, Group Underwriting and Claims Director and Group Chief Actuary. A similar committee has been established in each of the Group's major operating segments. The Group Reserving Committee monitors the decisions and judgments made by the business units as to the level of reserves recommended and makes the final decision on the reserves to be included within the consolidated financial statements ('Management Best Estimate'). In making its judgment, the Group Reserving Committee's aim is that, over the longer term, reserves should be more likely to run off favourably than adversely. However, there can be no assurance that reserves will not develop adversely and exceed the Management Best Estimate. In making its judgment of the Management Best Estimate of reserves to include in the consolidated financial statements, the Group Reserving Committee adopts the following approach:

- The Group's actuaries provide an indication of ultimate losses together with an assessment of risks and possible favourable or adverse developments that may not have been fully considered in calculating these indications. At the end of 2008 these risks and developments include: the possibility of future legislative change having retrospective effect on open claims; changes in claims settlement procedures potentially leading to future claims payment patterns differing from historical experience; the possibility of new types of claim, such as disease claims, emerging from business written several years ago; general uncertainty in the claims environment; the emergence of latent exposures such as asbestos; the outcome of litigation on claims received; failure to recover reinsurance and unanticipated changes in claims inflation
- Consideration is also made of the views of internal peer reviewers of the reserves and of third parties including actuaries, legal counsel, risk directors, underwriters and claims managers
- Consideration is made of how previous actuarial indications have developed.

In forming its collective judgment, the Committee considers this information as a whole.

Emerging and legal risks

These are risks that have been identified as potentially affecting the Group but for which the extent of risk has not yet been identified. Existing or potential future risk exposures are investigated in a structured way, using internal and external resources, and actions to mitigate, contain or remove these risks are taken.

In addition, to the extent that legal decisions in any of the jurisdictions in which the Group operates worldwide may increase court awards, and that the impact may be applied prospectively or retrospectively, claims reserves may prove insufficient to cover actual losses, LAE or future policy benefits. In such an event, or where it has been previously estimated that no liability would apply, the Group would add to its reserves and incur a charge to earnings. Such insufficiencies could have a material adverse effect on the Group's future consolidated financial condition, financial results and cashflows.

In the ordinary course of its insurance activities, the Group is routinely involved in legal or arbitration proceedings with respect to liabilities, which are the subject of policy claims.

As insurance industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues can have a negative effect on the Group's financial results by either extending coverage beyond its underwriting intent or by increasing the number and size of claims.

Reinsurance risk

The Group is exposed to multiple insured losses arising out of a single occurrence, whether a natural peril event such as a hurricane, flood or an earthquake, or man made catastrophes such as an explosion or fire at a major industrial facility. Any such catastrophic event could generate insured losses under one or more of its policies.

The ability of the business units in each territory to assess the aggregation risk of a single event impacting on thousands of policyholders is vital. The Group employs proprietary exposure measurement systems to assess these risks. In some markets, particularly in the UK, the Group has in addition developed its own expertise in catastrophe modelling that is used in conjunction with outside consultants. The accurate estimation of the potential expected maximum loss for a catastrophe is critical and is the primary factor considered in designing the Group's catastrophe reinsurance programme.

The expertise within the Group on catastrophe modelling is shared through the Worldwide Reinsurance Practice Group, which also provides an overview of the Groupwide catastrophe exposures and reinsurance adequacy. A reinsurance programme is considered to be 'adequate' only if it covers at least 199 out of 200 possible events by loss size. This is referred to as the '1 in 200 year expected maximum loss'. Since 1999, the Group has set its total retention for a single catastrophic event based on geographic location.

All of the Group's operations are required to purchase reinsurance within agreed local reinsurance appetite parameters. The Group Corporate Centre reviews the operations' proposed catastrophe purchases to check that they at least meet the Group's '1 in 200 year' standard. Group Corporate Centre also checks to see that total Group exposures are within the limits set out above and also are consistent with the required risk based capital. As a result the Group may decide to purchase further catastrophe coverage at the Group level.

In addition to local reinsurance arrangements, the Group reinsures a portion of the risks underwritten to control exposure to losses, to reduce volatility and protect capital. The Group's reinsurance strategy is to purchase reinsurance in the most effective manner from reinsurers who meet its security standards.

The Group uses financial analysis models to assess the risk and reward effects of different reinsurance structures and prices.

The Group remains primarily liable as the direct insurer on all risks reinsured, although the reinsurer is liable to the Group to the extent of the insurance risk ceded.

Credit risk

Credit risk is the risk of loss of value of the financial assets due to counterparties failing to meet all or part of their obligations. The Board Risk Committee (BRC) is responsible for ensuring that the Board approved Group credit risk appetite is not exceeded, through the setting and imposition of Group policies, procedures and limits. In defining its risk appetite for credit risk the Group looks at exposures at both an aggregate and business unit level distinguishing between credit risks incurred as a result of offsetting insurance risks or operating in the insurance market (e.g. reinsurance credit risks and insurance operations credit risks) and credit risks incurred for the purposes of generating a return (e.g. invested assets credit risk).

Limits are set at both a portfolio and counterparty level based on likelihood of default, derived from the rating of the counterparty, to ensure that the Group's overall credit profile and specific concentrations are managed and controlled within risk appetite. Financial assets are graded according to current credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. For invested assets, restrictions are placed on each of the Group's investment managers as to the level of exposure to not rated securities.

The following table provides information regarding the aggregated credit risk exposure for financial assets of the Group as at 31 December 2008.

	Credit rating relating to financial assets that are neither past due nor impaired						Total of financial assets that are neither past due nor impaired
	AAA £m	AA £m	A £m	BBB £m	<BBB £m	Not rated £m	£m
Debt securities	8,253	1,495	1,461	303	79	50	11,641
Other financial assets	59	7	2	1	3	88	160
Short term investments	1	–	5	–	–	–	6
Reinsurers' share of insurance contract liabilities	71	495	762	175	50	184	1,737
Insurance and reinsurance debtors[1]	26	45	74	31	6	2,414	2,596
Derivative assets	–	–	118	–	–	–	118
Other debtors	–	–	–	–	–	357	357
Cash and cash equivalents	282	781	313	29	1	208	1,614

Notes:

1. The insurance and reinsurance debtors classified as not rated comprise personal policyholders and small corporate customers that do not have individual credit ratings. The overall credit risk to the Group is deemed to be low as the cover could be cancelled if payment were not received on a timely basis.

Risk management continued

As at 31 December 2007

	Credit rating relating to financial assets that are neither past due nor impaired						Total of financial assets that are neither past due nor impaired
	AAA £m	AA £m	A £m	BBB £m	<BBB £m	Not rated £m	£m
Debt securities	6,635	1,528	1,010	201	70	134	9,578
Other financial assets	55	3	8	2	1	82	151
Short term investments	7	26	53	2	1	32	121
Reinsurers' share of insurance contract liabilities	63	702	714	191	115	74	1,859
Insurance and reinsurance debtors[1]	2	75	71	43	8	2,200	2,399
Derivative assets	–	–	33	–	–	–	33
Other debtors	–	–	–	–	1	288	289
Cash and cash equivalents	334	822	191	–	3	159	1,509

Notes:
1. The insurance and reinsurance debtors classified as not rated comprise personal policyholders and small corporate customers that do not have individual credit ratings. The overall credit risk to the Group is deemed to be low as the cover could be cancelled if payment were not received on a timely basis.

With the exception of AAA rated government debt securities, the largest aggregate credit exposure does not exceed **3%** of the Group's total financial assets.

The Group is exposed to concentrations of risk with individual reinsurers, due to the nature of the reinsurance market and the restricted range of reinsurers that have acceptable credit ratings. Reinsurance counterparties are subject to a rigorous internal assessment process on an ongoing basis to ensure that their creditworthiness continues to be satisfactory and the potential impact from reinsurer default is measured regularly and managed accordingly. The Group Reinsurance Credit Committee oversees the management of these risks. Group standards are set such that reinsurers that have a financial strength rating of less than 'A–' with Standard & Poor's, or a comparable rating with AM Best, are removed from the Group's authorised list unless the Group's internal review discovers exceptional circumstances in favour of the reinsurer. Collateral is taken to mitigate exposures, where appropriate, to acceptable levels or the size or credit quality of the exposure. At 31 December 2008 the Group held collateral against **£64m** (2007: £65m) of reinsurers' share of insurance contract liabilities.

The Group's largest reinsurance exposures to active reinsurance groups are Munich Re, SEB Group and Swiss Re. At 31 December 2008 the reinsurance asset recoverable from these groups does not exceed **3%** of the Group's total financial assets. Stress tests are regularly performed on the Group's reinsurance assets and the limits are set such that in a catastrophic event, the exposure to a single reinsurer is estimated not to exceed **1%** of the Group's total financial assets. Certain of the Group's subsidiaries are members of government mandated pools in various parts of the world. As of 31 December 2008 the largest pool (by premium volume) was Pool Re operated by the UK Government to provide terrorism cover.

There were no material financial assets that would have been past due or impaired had the terms not been renegotiated.

The following table provides information regarding the carrying value of financial assets that have been impaired and the ageing of financial assets that are past due but not impaired as at 31 December 2008.

		Financial assets that are past due but not impaired						
	Neither past due nor impaired £m	Up to three months £m	Three to six months £m	Six months to one year £m	Greater than one year £m	Financial assets that have been impaired £m	Carrying value in the balance sheet £m	Impairment losses charged to the income statement £m
Debt securities	**11,641**	–	–	–	–	**1**	**11,642**	**18**
Other financial assets	**160**	–	–	–	–	–	**160**	–
Short term investments	**6**	–	–	–	–	–	**6**	–
Reinsurers' share of insurance contract liabilities	**1,737**	–	–	–	–	**22**	**1,759**	**(3)**
Insurance and reinsurance debtors	**2,596**	**186**	**33**	**22**	**31**	**22**	**2,890**	**(8)**
Derivative assets	**118**	–	–	–	–	–	**118**	–
Other debtors	**357**	**10**	**5**	**1**	**14**	–	**387**	–
Cash and cash equivalents	**1,614**	–	–	–	–	–	**1,614**	–

As at 31 December 2007

	Neither past due nor impaired £m	Financial assets that are past due but not impaired				Financial assets that have been impaired £m	Carrying value in the balance sheet £m	Impairment losses charged to the income statement £m
		Up to three months £m	Three to six months £m	Six months to one year £m	Greater than one year £m			
Debt securities	9,578	–	–	–	–	3	9,581	2
Other financial assets	151	–	–	–	–	–	151	–
Short term investments	121	–	–	–	–	–	121	–
Reinsurers' share of insurance contract liabilities	1,859	–	–	–	–	13	1,872	(3)
Insurance and reinsurance debtors	2,399	90	33	11	26	20	2,579	3
Derivative assets	33	–	–	–	–	–	33	–
Other debtors	289	27	32	5	2	–	355	–
Cash and cash equivalents	1,509	–	–	–	–	–	1,509	–

Regional operations are responsible for assessing and monitoring the creditworthiness of their counterparties (e.g. brokers and policyholders). Local credit committees are responsible for ensuring these exposures are within the risk appetite of the local operations within the overall financial control framework. Exposure monitoring and reporting is embedded throughout the organisation with aggregate credit positions reported and monitored at Group level.

The Group's investments comprise a broad range of financial investments issued principally in the UK, Canada and Scandinavia.

At 31 December 2008, the Group had pledged **£1,049m** (2007: £954m) of financial assets as collateral for liabilities or contingent liabilities and had accepted **£1,329m** (2007: £1,536m) collateral that could be sold or pledged. The nature of the assets pledged as collateral comprises government securities of **£893m** (2007: £933m), cash and cash equivalents of **£93m** (2007: £21m) and debt securities of **£63m** (2007: £nil). The terms and conditions of the collateral pledged are market standard in relation to letter of credit facilities.

The Group is permitted to sell or repledge collateral held in the event of default by the owner, the fair value of which has been noted above at **£1,329m**. The terms and conditions of the collateral held are market standard. The assets held as collateral are readily convertible into cash.

At 31 December 2008, the Group had entered into short term sale and repurchase agreements for UK government securities (repos). The Group continues to recognise the debt securities on the balance sheet as the Group remains exposed to the risks and rewards of ownership. The carrying value of these debt securities recognised on the balance sheet is **£297m** (2007: £295m) and the carrying value of the associated liabilities is **£297m** (2007: £295m).

Certain of the Group's equities and debt securities that are held at fair value are unlisted (2008: **£656m**; 2007: £577m). These primarily comprise cash instruments which are highly liquid and redeemable at short notice at carrying value. The amount also includes a number of other unlisted investments which are valued either by reference to industry pricing sources or model based calculations.

Market risk

The Group is exposed to the risk of potential losses from adverse movements in market rates and prices as follows:

- Interest rate risk
- Equity price risk
- Property price risk
- Foreign currency exchange risk
- Derivatives.

The investment risk policy governs the Group's exposure to market risks. Exposures are controlled by the setting of investment limits in line with the Group's risk appetite.

Risk management continued

The Group Investment Committee (GIC), on behalf of the Group Board, is responsible for reviewing and approving the investment strategy for the Group's investment portfolios. It provides approval for all major changes of the Group's investment strategy and, in particular, approves any substantive changes to the balance of the Group's funds between the major asset classes. Importantly the GIC also approves the terms of reference of the Group's main operational investment committee, the Group Asset Management Committee (GAMC). The BRC issues GAMC with investment risk limits.

Interest rate risk

The fair value of the Group's portfolio of fixed income securities is inversely correlated to changes in the market interest rates. Thus if interest rates fall, the fair value of the portfolio would tend to rise and vice versa as set out in the sensitivity analysis on page 86.

Equity price risk

The Group's portfolio of equity securities is subject to equity risk arising from changes in market price. Thus if the value of equities rise so will the fair value of its portfolio and vice versa as set out in the sensitivity analysis on page 86.

The Group sets appropriate risk limits to ensure that no significant concentrations to individual companies or sectors arise. The Group takes a long term view in selecting shares and looks to build value over a sustained period of time rather than churning the portfolio looking for short term gains from its equity holdings.

The Group makes use of derivative products as appropriate to protect the portfolio from losses outside of its risk appetite.

The Group does not have material holdings of unquoted equities.

Property price risk

The Group's portfolio of properties is subject to property price risk arising from changes in the market value of properties. Thus if the value of property falls so will the fair value of the portfolio as set out in the sensitivity analysis on page 86.

A number of the Group's property holdings are Group occupied and therefore are reported within property and equipment. The Group's investment in investment property is recorded as such and these investments are held as part of an efficient portfolio management strategy.

Foreign currency exchange risk

The Group operates in 33 countries. Accordingly, its net assets are subject to foreign currency exchange rate movements. The Group's primary foreign currency exposures are to the Danish Kroner, Canadian Dollar, Swedish Krona and the Euro. If the value of Sterling strengthens then the value of non Sterling net assets will decline when translated into Sterling and consolidated.

The Group incurs exposure to foreign currency exchange risk in two ways:

- Operational foreign currency exchange risk – by underwriting liabilities in currencies other than the currency of the primary environment in which the business units operate (non functional currencies)
- Structural foreign currency exchange risk – by investing in overseas subsidiaries and operating an international insurance group.

Operational foreign currency exchange risk is managed within the Group's individual operations by broadly matching assets and liabilities by currency.

Structural foreign currency exchange risk is managed at a Group level through forward foreign exchange contracts. Derivatives are used to manage exposures within the limits that have been set. In managing structural foreign currency exchange risk, net assets maintained by the Group's subsidiaries in local currencies are taken into account to satisfy local regulatory solvency and internal risk based capital requirements. These assets should prove adequate to support local insurance activities irrespective of foreign currency exchange rate movements. Consequently, this may affect the value of the consolidated shareholders' equity expressed in Sterling.

At 31 December 2008, the Group's total shareholders' equity, analysed by currency is:

	Sterling £m	Danish Kroner £m	Canadian $ £m	Swedish Krona £m	Euro £m	Other £m	Total £m
Shareholders' equity at 31 December 2008	**669**	**688**	**911**	**806**	**202**	**563**	**3,839**
Shareholders' equity at 31 December 2007	482	690	798	441	349	317	3,077

Shareholders' equity is stated before taking account of the effect of forward foreign exchange contracts. After taking account of the effect of forward foreign exchange contracts, a 10% change in Sterling against Danish Kroner, Canadian Dollar or Swedish Krona would have the following impact on shareholders' equity:

	10% strengthening in Sterling against Danish Kroner £m	10% weakening in Sterling against Danish Kroner £m	10% strengthening in Sterling against Canadian $ £m	10% weakening in Sterling against Canadian $ £m	10% strengthening in Sterling against Swedish Krona £m	10% weakening in Sterling against Swedish Krona £m
Movement in shareholders' equity at 31 December 2008	**(2)**	**3**	**(26)**	**32**	**(39)**	**48**
Movement in shareholders' equity at 31 December 2007	(15)	19	(38)	47	(15)	18

Apart from the impact on derivative financial instruments covered below, the changes arise from retranslation of foreign subsidiaries' balance sheets from their functional currencies into Sterling, with movements being taken through the currency translation reserve. These movements in exchange rates therefore have no impact on profit.

Derivatives

The Group may use derivative financial instruments for the purpose of reducing its exposure to adverse fluctuations in interest rates, foreign exchange rates and equity price risk. The Group does not use derivatives to leverage its exposure to markets and does not hold or issue derivative financial instruments for speculative purposes. Forward contracts are used to reduce the risk of adverse currency movements on certain forecast future cash transactions and for structural hedging. The policy on use of derivatives is approved by the BRC.

	Remaining life			Fair value		Notional principal amounts	
	Less than one year £m	**One to five years £m**	**More than five years £m**	**2008 £m**	2007 £m	**2008 £m**	2007 £m
Cross currency							
Asset	–	–	–	–	1	–	4
Liability	**83**	–	**2**	**85**	31	**1,286**	1,247
Equity/index							
Asset	**118**	–	–	**118**	32	**see below**	see below
Liability	**61**	–	–	**61**	31	**see below**	see below

At 31 December 2008 there were derivative contracts in place to protect the value of the UK and European equity portfolios of the Group. These provided limited protection against declines in market levels whilst also capping participation in any appreciation of the market. In total, this strategy covered an underlying equity value up to approximately **£572m**. If UK and European equity markets decreased by 15%, the impact of these derivatives as of 31 December 2008, would be to decrease the impact of the decline by **£32m** (2007: £47m).

At 31 December 2008 the Group held forward foreign exchange contracts that are designated as hedging instruments to reduce structural foreign exchange risk. The derivatives are included in the table above. Further information on designated hedges can be found in note 28.

Risk management continued

Sensitivity analysis

The Group uses a number of sensitivity or stress test based risk management tools to understand the impact on earnings and capital in both normal and stressed conditions. These stress tests combine deterministic shocks, analysis of historical scenarios and stochastic modelling using the Individual Capital Assessment (ICA) models to inform the Group's decision making and planning process and also for identification and management of risks within the business units.

The following table provides an indication of some of the single factor changes adopted within the Group.

Changes in the income statement and equity:

	Increase/(decrease) in income statement		Decrease in equity	
	2008 £m	2007 £m	**2008 £m**	2007 £m
Interest rate markets:[2]				
Impact on fixed interest securities of increase in interest rates of 100bps	**–**	–	**(290)**	(264)
Impact on loan capital of increase in interest rates of 100bps[3]	**(3)**	–	**–**	–
Decrease of equity markets:[4]				
Direct impact on equities of a 15% fall in equity markets	**(50)**	–	**(91)**	(223)
Mitigating impact arising from derivatives held	**32**	47	**–**	–
Property markets:[4]				
Decrease of property markets of 15%	**(55)**	(64)	**(28)**	(44)

Notes:

1. This analysis assumes that there is no correlation between equity price, interest rate and property market rate risks. It also assumes that all other assets and liabilities remain unchanged and that no management action is taken. This analysis does not represent management's view of future market change, but reflects management's view of key sensitivities.
2. The sensitivity of the fixed interest securities of the Group has been modelled by reference to a reasonable approximation of the average interest rate sensitivity of the investments held within each of the portfolios.
3. The impact on the fair value of the loan capital is a decrease of **£32m** (2007: £124m).
4. The effect of movements in equity and property markets is reflected as a one time decrease of worldwide equity and property markets on 1 January 2009 and 1 January 2008 which results in a 15% decline in the value of the Group's assets in these investment categories.
5. This analysis has not considered the impact of the above market changes on the valuation of the Group's insurance liabilities.

With reference to sensitivity analysis within insurance risk, the Group has exposures to risks in each class of business within each operating segment that may develop and that could have a material impact upon the Group's financial position. The geographical and insurance risk diversity within the Group's portfolio of issued insurance policies makes it not possible to predict whether material development will occur and, if it does occur, the location and timing of such an occurrence.

The Group evaluates the concentration of exposures to individual and cumulative insurance risk and establishes its reinsurance policy to reduce such exposures to levels acceptable to the Group.

Liquidity risk

Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The Group has no tolerance for liquidity risk and is committed to meeting all liabilities as they fall due. The investment risk limits set by the BRC ensure that the Group's portfolio is kept in highly liquid marketable securities sufficient to meet its liabilities as they come due based on actuarial assessment. The limits are monitored at a Group level as part of the Group Risk exposure monitoring and BRC reporting process.

In addition the Group has committed credit facilities available as set out in note 22.

Maturity periods or contractual repricing

The following table summarises the contractual repricing or maturity dates (whichever is earlier) for financial liabilities that are subject to fixed and variable interest rates. Insurance liabilities are also presented and are analysed by remaining duration.

As at 31 December 2008

	Less than one year £m	One to two years £m	Two to three years £m	Three to four years £m	Four to five years £m	Five to ten years £m	Greater than ten years £m	Total £m	Balance sheet carrying value* £m
Subordinated guaranteed US$ bonds	–	–	–	–	–	–	16	16	15
Subordinated guaranteed Euro bonds	484	–	–	–	–	–	–	484	481
Subordinated Sterling perpetual guaranteed bonds	–	–	–	–	–	375	–	375	310
Subordinated guaranteed perpetual notes	–	–	–	–	–	450	–	450	505
Provision for unearned premiums	3,361	382	67	7	7	7	4	3,835	3,835
Provision for losses and loss adjustment expenses	4,033	1,933	1,380	962	679	1,615	1,565	12,167	11,220
Direct insurance creditors	222	1	–	–	–	1	–	224	224
Reinsurance creditors	320	1	–	–	–	–	–	321	321
Borrowings	298	1	1	–	–	–	–	300	300
Deposits received from reinsurers	73	3	–	–	–	–	–	76	76
Derivative trading liabilities	144	–	–	–	–	2	–	146	146
Total	8,935	2,321	1,448	969	686	2,450	1,585	18,394	17,433
Interest on perpetual bonds and notes	97	65	65	65	65	146	16	519	

* Balance sheet carrying value differs to the totals in the above tables as the balance sheet totals are on a discounted basis.

As at 31 December 2007

	Less than one year £m	One to two years £m	Two to three years £m	Three to four years £m	Four to five years £m	Five to ten years £m	Greater than ten years £m	Total £m	Balance sheet carrying value* £m
Subordinated guaranteed US$ bonds	–	–	–	–	–	–	12	12	11
Subordinated guaranteed Euro bonds	–	367	–	–	–	–	–	367	365
Subordinated Sterling perpetual guaranteed bonds	–	–	–	–	–	375	–	375	305
Subordinated guaranteed perpetual notes	–	–	–	–	–	450	–	450	513
Provision for unearned premiums	3,134	152	59	8	5	9	16	3,383	3,383
Provision for losses and loss adjustment expenses	3,418	1,880	1,357	957	678	1,541	1,337	11,168	10,344
Direct insurance creditors	165	1	–	–	–	–	–	166	166
Reinsurance creditors	250	10	–	–	–	–	–	260	260
Borrowings	302	1	–	–	–	–	–	303	303
Deposits received from reinsurers	47	16	1	–	–	–	–	64	64
Derivative trading liabilities	60	–	–	–	–	–	2	62	62
Total	7,376	2,427	1,417	965	683	2,375	1,367	16,610	15,776
Interest on perpetual bonds and notes	88	88	64	64	64	208	13	589	

The figures above are presented on an undiscounted basis.

Risk management continued

The capital and interest payable on the bonds and notes has been included until the dates on which the Group has the option to call the instruments and the interest rates are reset. For further information on the terms of the bonds and notes see note 19 to the financial statements.

Undiscounted interest payments are calculated based on underlying fixed interest rates or prevailing market floating rates as applicable (as detailed in note 19). Year end exchange rates have been used for interest projections on loans in foreign currencies.

Capital management

The maintenance of a strong capital position of the Group is critical to its ability to conduct business.

The Group maintains sufficient capital, which comprises shareholders' equity and subordinated loan capital, to meet its plan and objectives. This represents sufficient surpluses for both regulatory and economic capital, as well as sufficient capital to support the Group's aim of maintaining single 'A' ratings.

To provide protection against material events or shocks, the Group would normally expect to hold sufficient capital to maintain significant economic and regulatory surpluses.

The maintenance of a capital position in excess of regulatory requirements is an absolute requirement for all of the Group's regulated entities. There is no tolerance for breaching capital requirements for any regulated entity.

Economic capital

Economic capital is the Group's preferred measure of capital sufficiency. It is the Group's own assessment of the amount of capital it needs to hold to meet its obligations given the Group's risk appetite. Assets and liabilities are valued on an economic basis providing the most realistic representation of the Group's financial condition.

The economic capital analysis compares the economic value of the Group's assets with the total resources required in a range of adverse scenarios, calibrated to a defined risk tolerance consistent with the Group's 'A' rating which is in line with target. The economic capital surplus is the amount by which the economic assets exceed the total resources required. The total resources required is the amount of assets the Group needs today to meet its liabilities under the defined risk tolerance. The Group defines the economic capital required as the difference between the total resource requirement and the accounting value of liabilities. At 31 December 2008, the Group's surplus economic capital was approximately **£1.8bn** (2007: £2.2bn).

The economic capital model is used to support, inform and improve the Group's decision making across the Group. It is used to determine the Group's optimum capital structure, its investment strategy, its reinsurance programme and to determine the pricing and target returns for each portfolio. The economic capital model is also used for the Group's ICA. The only adjustment made is to use the FSA's required calibration.

Regulatory solvency position

The Group remains fully compliant with both the FSA's risk based ICA methodology and Solvency I, which is used to calculate the Insurance Groups Directive (IGD) requirement.

For the Group's senior regulated insurance company, Royal & Sun Alliance Insurance plc, the capital position continues to be reported under Solvency I.

As at 31 December 2008 the Group had an IGD surplus of approximately **£1.7bn** (2007: £1.5bn). The improvement in IGD surplus is mainly attributable to the profits for the year and positive foreign exchange movements, offset by the dividend paid, unrealised investment losses and an increase in the capital requirement in line with business growth. The coverage ratio stood at **2.5** times at 31 December 2008 (2007: 2.5 times).

The Group received its Individual Capital Guidance (based on its ICA submission) from the FSA in late 2007, which was not changed in 2008 and at the request of the FSA remains confidential. The ICA is a forward looking, economic assessment of the capital requirements of the Group based on its assessment of the risks to which it is exposed. The models used to determine the ICA have been integrated into the Group's business processes and are used to enhance the management of the Group.

The Group is also continuing to implement a number of capital management initiatives, including optimising its regulatory structure and improving the capital efficiency of its discontinued lines of business.

Notes to the financial statements

1. Operating segments

The Group is organised into three operating segments – International, Emerging Markets and the UK. The UK is the Group's country of domicile and principal market (based on value of premium written in a single country). International comprises operations in Scandinavia, Canada, Ireland and Italy and Emerging Markets comprises the Group's operations in Latin America, Asia and the Middle East, the Baltics and the Group's joint ventures in Central and Eastern Europe, which are accounted for as associates. All operations are engaged in providing personal and commercial general insurance services. Central functions include the Group's internal reinsurance function and Group Corporate Centre.

This structure brings together operations with similar challenges and opportunities in order to give due focus to achieving the Group's objective of profitable growth across the business. Each operating segment is managed by a Chief Executive Officer (CEO) who is directly accountable to the Group CEO and the Board of Directors.

The Group uses the following key measures to assess the performance of its operating segments:

- Net written premiums
- Underwriting result
- Combined operating ratio (COR).

Net written premiums is the key measure of revenue used in internal reporting. Underwriting result and COR are the key internal measures of profitability of the operating segments. The COR reflects the ratio of claims costs and expenses (including commission) to premiums, expressed as a percentage.

All of these items are measured in accordance with the Group's accounting policies. Certain items included within the Group's investment result are allocated to the operating segments based on economic capital requirements.

Transfers or transactions between segments are entered into under normal commercial terms and conditions that would also be available to unrelated third parties.

Management basis

The management basis reflects the way management monitor the business. Operating result on a management basis comprises the underwriting result, the investment result and other activities.

Major components of underwriting result are net earned premiums, other operating income, net claims and benefits and underwriting and policy acquisition costs.

The investment result, excluding unwind of discount and foreign exchange, is disclosed as net investment return on the statutory basis. Investment income on the statutory basis includes an adjustment for depreciation on Group occupied properties.

Other activities primarily comprise administration and other expenses of **£67m** (2007: £72m), the Group share in the loss after tax of its associates of **£18m** (2007: £nil) and investment expenses and charges of **£26m** (2007: £21m).

Notes to the financial statements continued

1. Operating segments continued

Segment revenue and results

Year ended 31 December 2008

	UK £m	International £m	Emerging Markets £m	Central functions £m	Total Group £m
Net written premiums	2,711	2,998	738	15	6,462
Underwriting result	99	262	23	–	384
Investment result	317	237	40	–	594
Insurance result	416	499	63	–	978
Other activities	1	(6)	(29)	(77)	(111)
Operating result (management basis)	417	493	34	(77)	867
Amortisation					(18)
Add: net share of losses after tax of associates					18
Results of operating activities (per income statement)					867
Combined operating ratio (%)	97.6	91.2	96.4	–	94.5
Other segment items included in the income statement:					
Investment income	325	259	38	32	654
Interest expense	–	(8)	(8)	(10)	(26)
Depreciation and amortisation	(55)	(50)	(3)	(1)	(109)

Year ended 31 December 2007

	UK £m	International £m	Emerging Markets £m	Central functions £m	Total Group £m
Net written premiums	2,688	2,513	615	21	5,837
Underwriting result	65	206	18	(11)	278
Investment result	372	212	42	3	629
Insurance result	437	418	60	(8)	907
Other activities	(1)	(8)	(6)	(78)	(93)
Operating result (management basis)	436	410	54	(86)	814
Amortisation					(18)
Results of operating activities (per income statement)					796
Combined operating ratio (%)	97.6	91.3	95.3	–	94.9
Other segment items included in the income statement:					
Investment income	328	198	35	30	591
Interest expense	–	(6)	(6)	(9)	(21)
Depreciation and amortisation	(38)	(39)	(6)	(5)	(88)

No other material non cash expenses are reported internally by segment.

Segment assets and capital expenditure

Year ended 31 December 2008

	UK £m	International £m	Emerging Markets £m	Central functions £m	Total Group £m
Segment assets	**8,903**	**11,003**	**1,938**	**897**	**22,741**
Investment in associates	**8**	**4**	**111**	**–**	**123**
Total assets of continuing operations	**8,911**	**11,007**	**2,049**	**897**	**22,864**
Non current and disposal group assets held for sale					**3**
Total assets					**22,867**
Capital expenditure:					
Property and equipment	**36**	**31**	**5**	**2**	**74**
Goodwill	**12**	**13**	**–**	**–**	**25**
Intangible assets	**50**	**22**	**–**	**–**	**72**

Year ended 31 December 2007

	UK £m	International £m	Emerging Markets £m	Central functions £m	Total Group £m
Segment assets	8,716	8,977	1,474	1,213	20,380
Investment in associates	–	4	101	–	105
Total assets of continuing operations	8,716	8,981	1,575	1,213	20,485
Non current and disposal group assets held for sale					108
Total assets					20,593
Capital expenditure:					
Property and equipment	3	18	7	–	28
Goodwill	–	35	–	–	35
Intangible assets	42	60	2	–	104

Net written premiums and non current assets from major geographical regions

	Net written premiums		Non current assets	
	2008 £m	2007 £m	**2008 £m**	2007 £m
UK	**2,711**	2,688	**385**	306
Scandinavia	**1,602**	1,379	**435**	463
Canada	**884**	703	**164**	157
Other Europe	**512**	431	**59**	31
Other	**753**	636	**498**	617
	6,462	5,837	**1,541**	1,574

Net written premiums are allocated to the countries in which the business is underwritten or managed.

Non current assets comprise goodwill and intangible assets, property and equipment, investment property and investments in associates.

Other Europe comprises the Group's businesses in Ireland and Italy.

Notes to the financial statements continued

2. Net investment return

A summary of the gross investment income, net realised and net unrealised gains/(losses) included in the income statement is given below.

	Investment income		Net realised gains/(losses)		Net unrealised gains/(losses)		Impairments		Total investment return	
	2008 £m	2007 £m	**2008 £m**	2007 £m	**2008 £m**	2007 £m	**2008 £m**	2007 £m	**2008 £m**	2007 £m
Investment property	**14**	19	**–**	12	**(98)**	(42)	**–**	–	**(84)**	(11)
Equity securities	**50**	48	**65**	185	**(12)**	(2)	**(43)**	(1)	**60**	230
Debt securities	**478**	391	**3**	(29)	**(10)**	–	**(18)**	(2)	**453**	360
Other investments:										
Loans secured by mortgages	**1**	1	**(1)**	1	**–**	–	**–**	–	**–**	2
Other loans	**4**	5	**–**	–	**–**	–	**–**	–	**4**	5
Other	**36**	31	**(2)**	(4)	**–**	(8)	**–**	–	**34**	19
Deposits, cash and cash equivalents	**57**	83	**3**	1	**1**	–	**–**	–	**61**	84
Derivatives	**12**	15	**82**	8	**59**	(3)	**–**	–	**153**	20
Net investment return	**652**	593	**150**	174	**(60)**	(55)	**(61)**	(3)	**681**	709

The net investment return arising on assets categorised as at fair value through the income statement includes the net return arising on derivatives and assets designated as fair value through the income statement.

During 2008 the accrued interest income on impaired financial assets was **£nil** (2007: £nil).

Direct operating expenses (including repairs and maintenance) arising from investment properties were not material in 2008 and 2007.

Unrealised capital gains and losses recognised directly in equity for available for sale assets are as follows:

	Net unrealised gains/(losses)		Net realised (gains)/ losses transferred to income statement		Impairments transferred to income statement		Net movement recognised in equity	
	2008 £m	2007 £m	**2008 £m**	2007 £m	**2008 £m**	2007 £m	**2008 £m**	2007 £m
Equity securities	**(429)**	49	**(65)**	(194)	**43**	1	**(451)**	(144)
Debt securities	**242**	1	**(3)**	27	**18**	2	**257**	30
Other	**1**	1	**1**	(1)	**–**	–	**2**	–
Total	**(186)**	51	**(67)**	(168)	**61**	3	**(192)**	(114)

3. Net claims and benefits

	2008 £m	2007 £m
Gross claims paid	**4,747**	4,145
Gross changes in insurance contract liabilities for claims	**(542)**	(101)
Reinsurance recoveries on losses and loss expenses paid	**(484)**	(519)
Reinsurers' share of change in insurance contract liabilities for claims	**421**	132
Net claims and benefits	**4,142**	3,657

4. Profit before tax

The following items have been included in arriving at the profit before tax on continuing operations:

Other operating income

	2008 £m	2007 £m
Engineering inspection fees	**54**	41
Other income	**50**	73
Net losses on derivatives	**–**	(1)
Other operating income	**104**	113

Engineering inspection fees are ancillary to the provision of engineering insurance cover.

Other operating expenses

	2008 £m	2007 £m
Administration and other expenses	**76**	83
Investment expenses and charges	**26**	21
Amortisation of intangible assets	**18**	18
Foreign exchange gains	**(3)**	(3)
Other operating expenses	**117**	119

Other lease payments

The operating lease payments recognised as an expense during the year were **£53m** (2007: £48m). The Group has no significant lease agreements that include contingent rents.

Finance costs

	2008 £m	2007 £m
Interest expense on loan capital	**88**	90
Other loan interest	**20**	14
Finance costs	**108**	104

Auditors' remuneration

	Deloitte LLP		PricewaterhouseCoopers LLP		Total	
	2008 £m	2007 £m	2008 £m	2007 £m	2008 £m	2007 £m
Fees payable to the Company's auditors for audit of the Company's annual accounts	**0.9**	0.9	–	–	**0.9**	0.9
Fees payable to the Company's auditors and its associates for other services:						
The audit of the Company's subsidiaries, pursuant to legislation	**3.1**	2.6	–	0.3	**3.1**	2.9
Other services pursuant to legislation	**0.3**	0.1	–	0.1	**0.3**	0.2
Tax services	**0.1**	0.1	–	0.8	**0.1**	0.9
Services relating to corporate finance activities	**0.6**	1.1	–	0.3	**0.6**	1.4
Other	**3.3**	0.4	–	0.2	**3.3**	0.6
Fees in respect to pension scheme:						
Audit	**–**	–	–	0.1	**–**	0.1
	8.3	5.2	–	1.8	**8.3**	7.0

Other includes fees payable to the Company's auditors in respect of consultancy services relating to business transformation processes and regulatory development projects.

Directors' emoluments

The aggregate emoluments of the directors, including amounts received from subsidiaries, were as follows:

	2008 £000	2007 £000
Emoluments of executive directors	**4,838**	4,479
Fees and other payments to non-executive directors	**584**	556
	5,422	5,035

Details of directors' remuneration and pension benefits, including that of the highest paid director (Andy Haste), are included in the directors' emoluments. Details of directors' interests in the Parent Company are shown in the directors' emoluments and interests.

Notes to the financial statements continued

4. Profit before tax continued

Employee information

Staff costs for all employees comprise:

	2008 £m	2007 £m
Wages and salaries	**717**	657
Social security costs	**89**	74
Pension costs	**91**	43
Share based payments to directors and employees	**25**	19
	922	793

The average number of employees of the continuing operations during the year was as follows:

	2008 Number	2007 Number
UK	**9,322**	9,626
International	**7,789**	7,418
Emerging Markets	**5,353**	5,509
	22,464	22,553

Discontinued operations

The loss before tax from discontinued operations includes the following:

	2008 £m	2007 £m
Reorganisation expenses	–	1
Amortisation and impairment of intangible assets	–	1

Staff costs for employees of discontinued operations comprise:

	2008 £m	2007 £m
Wages and salaries	–	5
Social security costs	–	1
Pension costs	–	1
	–	7

Auditors' remuneration of **£nil** (2007: £nil) was paid in 2008 in respect of the audit services for discontinued operations.

5. Income tax expense

The tax amounts charged in the income statement are as follows:

	2008 £m	2007 £m
Current tax	**240**	168
Deferred tax	**(67)**	(139)
Taxation attributable to the Group	**173**	29

UK corporation tax is calculated at **28.5%** (2007: 30%) of the estimated assessable profit for the year. Since the Group operates around the world, it is subject to income taxes in many different jurisdictions. Taxation for jurisdictions other than the UK is calculated at the rates prevailing in those jurisdictions. Of the above taxation attributable to the Group **£38m** (2007: £37m) relates to UK corporation tax and **£135m** (2007: £(8)m) to overseas taxation.

	2008 £m	2007 £m
Profit before tax on continuing operations	**759**	670
Tax at the UK rate of **28.5%** (2007: 30%)	**216**	201
Tax effect of:		
Income/gains not taxable	**(28)**	(26)
Expenses not deductible for tax purposes	**11**	10
Tax losses not recognised	**1**	–
Release of tax held in respect of Security Fund/Safety Reserve	**–**	(103)
Release of tax provided in respect of prior periods	**(14)**	(15)
Different tax rates of subsidiaries operating in other jurisdictions	**(26)**	(32)
Other	**13**	(6)
Income tax expense	**173**	29

6. Earnings per share attributable to the ordinary shareholders of the Parent Company

The earnings per ordinary share is calculated by reference to the profit attributable to the ordinary shareholders and the weighted average of shares in issue during the year.

Basic

Basic earnings per share is calculated by dividing the profit attributable to the ordinary shareholders of the Parent Company by the weighted average number of ordinary shares in issue during the period, excluding ordinary shares purchased by the ESOP Trusts and held as treasury shares.

	Continuing operations		Total Group	
	2008 £m	2007 £m	2008 £m	2007 £m
Profit attributable to the ordinary shareholders of the Parent Company	**574**	609	**574**	596
Less: cumulative preference dividends	**(9)**	(9)	**(9)**	(9)
Profit for the calculation of earnings per share	**565**	600	**565**	587
Weighted average number of ordinary shares in issue (thousands)	**3,273,492**	3,106,017	**3,273,492**	3,106,017
Basic earnings per share (p)	**17.3**	19.3	**17.3**	18.9

Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Parent Company has share options and contingently issuable shares as categories of dilutive potential ordinary shares.

The calculation is performed for the dilutive potential ordinary shares to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Parent Company's shares) based on the monetary value of the subscription rights attached to outstanding dilutive potential ordinary shares. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the dilutive potential ordinary shares.

	Continuing operations		Total Group	
	2008 £m	2007 £m	2008 £m	2007 £m
Profit for the calculation of earnings per share	**565**	600	**565**	587
Weighted average number of ordinary shares in issue (thousands)	**3,273,492**	3,106,017	**3,273,492**	3,106,017
Adjustments for share options (thousands)	**53,034**	43,869	**53,034**	43,869
Weighted average number of ordinary shares for diluted earnings per share (thousands)	**3,326,526**	3,149,886	**3,326,526**	3,149,886
Diluted earnings per share (p)	**17.0**	19.0	**17.0**	18.6

Earnings per share attributable to discontinued operations

The loss for the year from discontinued operations is **£nil** (2007: £13m). The basic earnings per share from discontinued operations is **nil** (2007: (0.4)p) and the diluted earnings per share from discontinued operations is **nil** (2007: (0.4)p).

Notes to the financial statements continued

7. Dividends

	2008 p	2007 p	2008 £m	2007 £m
Ordinary dividend:				
Final paid in respect of prior year	**4.53**	4.12	**147**	123
Interim paid in respect of current year	**2.73**	2.48	**90**	79
			237	202
Preference dividend			**9**	9
			246	211

At the Annual General Meeting (AGM) on 18 May 2009, a dividend in respect of 2008 of **4.98p** per share amounting to a total dividend of **£165m** is to be proposed. The proposed dividend will be paid and accounted for in shareholders' equity as an appropriation of retained earnings in the year ending 31 December 2009.

The Group subsidiaries may be subject to restrictions on the amount of dividends they can pay to shareholders as a result of local regulatory requirements. However, based on the information currently available, the Group does not believe that such restrictions materially impact the ability to meet obligations or pay dividends.

The trustees of the Royal & SunAlliance ESOP Trust and the Royal & SunAlliance ESOP Trust No 2 waived their entitlement to dividends which reduced the total dividend paid by **£1m** (2007: £1m).

8. Goodwill and other intangible assets

	Goodwill £m	Intangible asset arising from acquired claims provisions £m	Software development £m	Other £m	Total £m
Cost					
At 1 January 2008	**263**	**102**	**448**	**150**	**963**
Additions and transfers	**25**	**–**	**70**	**2**	**97**
Disposals and transfers	**–**	**–**	**(4)**	**(2)**	**(6)**
Other	**10**	**–**	**–**	**(14)**	**(4)**
Exchange adjustment	**46**	**32**	**19**	**8**	**105**
At 31 December 2008	**344**	**134**	**533**	**144**	**1,155**
Accumulated amortisation					
At 1 January 2008	**–**	**77**	**179**	**44**	**300**
Amortisation charge	**–**	**8**	**54**	**12**	**74**
Amortisation on disposals	**–**	**–**	**(4)**	**–**	**(4)**
Exchange adjustment	**–**	**27**	**13**	**1**	**41**
At 31 December 2008	**–**	**112**	**242**	**57**	**411**
Net book amount at 31 December 2008	**344**	**22**	**291**	**87**	**744**

No goodwill and other intangible assets as at 31 December 2008 have been impaired.

During the year, the provisional valuation of the 2007 acquisition of Thomson Jemmett Vogelzang in Canada was revised and a balance previously classified as other of £14m was transferred to goodwill, net of deferred tax of £4m. The increase in goodwill is £10m. Comparative information has not been adjusted as the impact is not material.

Other intangible assets include renewal rights and acquired brands.

	Goodwill £m	Intangible asset arising from acquired claims provisions £m	Software development £m	Other £m	Total £m
Cost					
At 1 January 2007	213	89	399	106	807
Additions and transfers	35	6	51	47	139
Disposals and transfers	–	–	(9)	(20)	(29)
Exchange adjustment	15	7	7	17	46
At 31 December 2007	263	102	448	150	963
Accumulated amortisation					
At 1 January 2007	–	65	145	45	255
Amortisation charge	–	6	38	12	56
Amortisation on disposals	–	–	(8)	(20)	(28)
Exchange adjustment	–	6	4	7	17
At 31 December 2007	–	77	179	44	300
Net book amount at 31 December 2007	263	25	269	106	663

Amortisation expense of **£56m** (2007: £38m) has been charged to underwriting and policy acquisition costs.

Additions of software development comprise **£13m** (2007: £17m) of external software and **£57m** (2007: £34m) of internally developed software.

Impairment tests for goodwill

Goodwill is allocated to the Group's cash generating units (CGUs) as follows:

	2008 £m	2007 £m
UK	**55**	43
International	**239**	175
Emerging Markets	**50**	45

When testing for impairment, the recoverable amount of a CGU is determined based on value in use calculations. These calculations use cashflow projections based on financial budgets approved by management covering a five year period. Cashflows beyond the five year period are extrapolated using the estimated growth rates which do not exceed the long term average past growth rate for the insurance business in which the CGU operates.

A number of other assumptions and estimates are involved in the application of a cashflow model to forecast operating cashflows, premium volumes, expenses and working capital requirements. Forecasts of future cashflows are based on the best estimates of future premiums, operating expenses using historical trends, general geographical market conditions, industry trends and forecasts and other available information. These assumptions are subject to review by management and the Group Audit Committee. The cashflow forecasts are adjusted by appropriate discount rates. Discount rates used are within a range of **8%** to **16%** (2007: 10% to 15%), are pre tax and reflect specific risks relating to the relevant segments at the date of evaluation. The weighted average growth rates used in 2008 are within a range of **0.9%** to **3.5%** (2007: 0.9% to 3%).

No impairments have been recognised during the year, or in prior years.

Notes to the financial statements continued

9. Property and equipment

	Group occupied property – land and buildings £m	Other £m	Total £m
Cost/valuation			
At 1 January 2008	**293**	**347**	**640**
Additions	**9**	**65**	**74**
Disposal of subsidiaries	**(92)**	**–**	**(92)**
Disposals	**–**	**(22)**	**(22)**
Revaluation adjustment	**(53)**	**–**	**(53)**
Exchange adjustment	**30**	**37**	**67**
At 31 December 2008	**187**	**427**	**614**
Accumulated depreciation			
At 1 January 2008	**–**	**258**	**258**
Depreciation charge	**3**	**32**	**35**
Depreciation on disposals	**–**	**(11)**	**(11)**
Revaluation adjustment	**(3)**	**–**	**(3)**
Exchange adjustment	**–**	**20**	**20**
At 31 December 2008	**–**	**299**	**299**
Accumulated impairment			
At 1 January 2008	**–**	**5**	**5**
Exchange adjustment	**–**	**1**	**1**
At 31 December 2008	**–**	**6**	**6**
Net book amount at 31 December 2008	**187**	**122**	**309**

	Group occupied property – land and buildings £m	Other £m	Total £m
Cost/valuation			
At 1 January 2007	298	320	618
Additions	7	21	28
Disposal of subsidiaries	(4)	–	(4)
Disposals	(19)	(8)	(27)
Revaluation adjustment	17	–	17
Exchange adjustment	17	14	31
Transfer to investment property	(10)	–	(10)
Transfer to non current and disposal group assets held for sale	(13)	–	(13)
At 31 December 2007	293	347	640
Accumulated depreciation			
At 1 January 2007	–	227	227
Depreciation charge	4	28	32
Depreciation on disposals	–	(5)	(5)
Revaluation adjustment	(4)	–	(4)
Exchange adjustment	–	8	8
At 31 December 2007	–	258	258
Accumulated impairment			
At 1 January 2007	–	6	6
Exchange adjustment	–	(1)	(1)
At 31 December 2007	–	5	5
Net book amount at 31 December 2007	293	84	377

The Group occupied property was revalued on 31 December 2008 by independent valuers.

Depreciation expenses of **£35m** (2007: £32m) have been charged to underwriting and policy acquisition costs.

The carrying amount of Group occupied property that would have been recognised had the assets been carried under the cost model at 31 December 2008 is **£160m** (2007: £189m).

10. Investment property

Investment property consists of the following:

	2008 £m	2007 £m
Land and buildings:		
Freehold and long leasehold	**363**	426
Short leasehold	**2**	3
Total land and buildings	**365**	429

Movement in the carrying value of investment property is detailed below:

	2008 £m	2007 £m
Investment property at 1 January	**429**	454
Additions from subsequent expenditure	**10**	9
Transfer from property and equipment	**–**	10
Sales and purchases	**(3)**	1
Fair value losses	**(98)**	(50)
Exchange adjustment	**27**	5
Investment property at 31 December	**365**	429

Investment properties are included in the Group's investment portfolio to provide investment returns over the longer term in accordance with the Group's investment strategy. Investment properties are managed by external managers.

The lease agreements are normally drawn up in line with local practice and the Group has no significant exposure to leases that include contingent rents.

11. Investments in associates

The Group has the following investments in associates:

	Country	Ordinary shareholding
Intouch Insurance Group BV	Netherlands	50.0%
Caunce O'Hara & Company Limited	United Kingdom	30.0%
Royal Sundaram Alliance Insurance Company Limited	India	26.0%
Huestis Insurance & Associates Limited	Canada	25.0%
H&R Insurance Limited	Canada	25.0%
Syn Mun Kong Public Limited Company	Thailand	20.0%

Syn Mun Kong Public Limited Company is listed on the Stock Exchange of Thailand. The fair value of the Group's holding at 31 December was **£5m**.

On 14 March 2008 Global Direct Insurance Investments BV changed its name to Intouch Insurance Group BV.

On 5 February, the Group announced that it had reached an agreement to acquire the remaining share capital of Intouch Insurance Group BV for a consideration of **€70m**. The transaction requires regulatory approval prior to the Group obtaining control of the business. It is expected this approval will be granted by the third quarter of 2009.

Summarised below are the assets, liabilities, revenue and profit and loss of the companies above. The comparatives below have not been restated for associates acquired during 2008.

	2008 £m	2007 £m
Total assets	**400**	251
Total liabilities	**292**	173
Total revenue	**237**	116
Goodwill on acquisition	**88**	56
(Loss)/profit for the year after tax	**(26)**	2

The Group's share of net assets and profit and loss are accounted for under the equity method.

Some associates that do not materially affect the results or assets of the Group have been omitted from this statement.

Notes to the financial statements continued

12. Financial assets

	2008 £m	2007 £m
Equity securities	**940**	1,487
Debt securities	**11,642**	9,581
Other financial assets	**160**	151
Short term investments	**6**	121
Total financial assets – available for sale	**12,748**	11,340

The Group does not hold significant financial assets classified as fair value through the income statement.

The Group's portfolio of equity securities comprises ordinary shares and unit trusts of **£780m** (2007: £1,132m) and other equity instruments of **£160m** (2007: £355m). Other equity instruments include preference shares of **£97m** (2007: £125m) and collective investment vehicles primarily invested in cash and bond assets of **£63m** (2007: £230m). The performance of these assets is typically not expected to correlate strongly to the performance of ordinary shareholdings.

Over 98% of financial assets are valued using their quoted market prices in active markets. The Group does not hold significant financial assets that are not valued using quoted market prices.

13. Reinsurers' share of insurance contract liabilities

	2008 £m	2007 £m
Reinsurers' share of provision for unearned premiums	**259**	215
Reinsurers' share of provisions for losses and loss adjustment expenses	**1,500**	1,657
Total reinsurers' share of insurance contract liabilities	**1,759**	1,872
To be settled within 12 months	**734**	723
To be settled after 12 months	**1,025**	1,149

The following changes have occurred in the reinsurers' share of the provision for unearned premiums during the year:

	2008 £m	2007 £m
Reinsurers' share of provision for unearned premiums at 1 January	**215**	189
Premiums ceded to reinsurers	**811**	759
Reinsurers' share of premiums earned	**(803)**	(754)
Changes in reinsurance asset	**8**	5
Reinsurers' share of portfolio transfers and (disposals)/acquisitions of subsidiaries	**(1)**	12
Exchange adjustment	**37**	9
Reinsurers' share of provision for unearned premiums at 31 December	**259**	215

The following changes have occurred in the reinsurers' share of the provision for losses and loss adjustment expenses during the year:

	2008 £m	2007 £m
Reinsurers' share of provisions for losses and loss adjustment expenses at 1 January	**1,657**	1,738
Reinsurers' share of total claims incurred	**63**	387
Total reinsurance recoveries received	**(484)**	(519)
Reinsurers' share of portfolio transfers and acquisitions of subsidiaries	**2**	50
Exchange adjustment	**256**	57
Other movements	**6**	2
Transfer to non current and disposal group assets held for sale	**–**	(58)
Reinsurers' share of provisions for losses and loss adjustment expenses at 31 December	**1,500**	1,657

14. Insurance and reinsurance debtors

	2008 £m	2007 £m
Insurance debtors comprise:		
Due from policyholders	**1,218**	1,086
Due from intermediaries	**1,411**	1,254
Total insurance debtors	**2,629**	2,340
Reinsurance debtors	**261**	239
Total insurance and reinsurance debtors	**2,890**	2,579

15. Deferred acquisition costs

	2008 £m	2007 £m
Deferred acquisition costs at 1 January	**542**	453
Exchange adjustment	**53**	20
Acquisition costs deferred during the year	**793**	766
Amortisation charged during the year	**(728)**	(705)
Credit to income statement in the year	**65**	61
Acquisition of subsidiaries	**–**	8
Other	**(7)**	–
Deferred acquisition costs at 31 December	**653**	542

The Group records acquisition costs recovered from reinsurers as a deduction from deferred acquisition costs.

16. Other debtors and other assets

	2008 £m	2007 £m
Derivative assets	**118**	33
Other debtors	**387**	355
Pension scheme surplus	**602**	263
Accrued interest and rent	**193**	150
Prepayments	**177**	162
Total other debtors and other assets	**1,477**	963
To be settled within 12 months	**806**	643
To be settled after 12 months	**671**	320

17. Cash and cash equivalents

	2008 £m	2007 £m
Cash and cash equivalents and bank overdrafts (as reported within the cashflow statement)	**1,614**	1,538
Add: bank overdrafts	**–**	3
Less: transfer to non current and disposal group assets held for sale	**–**	(32)
Total cash and cash equivalents	**1,614**	1,509

The interest bearing financial assets and financial liabilities included in cash and cash equivalents and bank overdrafts had an effective interest rate of **2.64%** (2007: 4.85%) and had an average maturity of **15 days** (2007: 23 days).

Notes to the financial statements continued

18. Equity and reserves

Changes in equity

Changes in equity for the year ended 31 December 2008

	Ordinary share capital £m	Ordinary share premium £m	Treasury shares £m	Preference shares £m	Revaluation reserves £m	Capital redemption reserve £m	Translation reserve £m	Retained earnings £m	Share-holders' funds £m	Minority interests £m	Total equity £m
Balance at 1 January	895	943	(38)	125	422	8	47	675	3,077	67	3,144
Total recognised (expense)/ income for the year	–	–	–	–	(195)	–	317	779	901	22	923
Dividends – paid (note 7)	–	–	–	–	–	–	–	(246)	(246)	(8)	(254)
Issued by scrip	14	51	–	–	–	–	–	–	65	–	65
Issued for cash	6	13	–	–	–	–	–	–	19	–	19
Treasury shares utilised	–	–	28	–	–	–	–	(28)	–	–	–
Changes in shareholders' interests in subsidiaries	–	–	–	–	(2)	–	–	–	(2)	–	(2)
Depreciation transfer	–	–	–	–	(1)	–	–	1	–	–	–
Share options	–	–	–	–	–	–	–	25	25	–	25
Balance at 31 December	**915**	**1,007**	**(10)**	**125**	**224**	**8**	**364**	**1,206**	**3,839**	**81**	**3,920**

The above amounts are presented net of deferred tax. The deferred tax charged or credited directly to equity is set out in note 23.

Changes in equity for the year ended 31 December 2007

	Ordinary share capital £m	Ordinary share premium £m	Treasury shares £m	Preference shares £m	Revaluation reserves £m	Capital redemption reserve £m	Translation reserve £m	Retained earnings £m	Share-holders' funds £m	Minority interests £m	Total equity £m
Balance at 1 January	821	857	(57)	125	456	8	(81)	432	2,561	331	2,892
Total recognised (expense)/ income for the year	–	–	–	–	(43)	–	136	577	670	15	685
Dividends – paid (note 7)	–	–	–	–	–	–	–	(211)	(211)	(31)	(242)
Issued by scrip	19	81	–	–	–	–	–	–	100	–	100
Issued for cash	55	5	–	–	–	–	–	244	304	–	304
Treasury shares utilised	–	–	19	–	–	–	–	(19)	–	–	–
Changes in shareholders' interests in subsidiaries	–	–	–	–	11	–	(8)	(371)	(368)	(248)	(616)
Depreciation transfer	–	–	–	–	(2)	–	–	2	–	–	–
Share options	–	–	–	–	–	–	–	21	21	–	21
Balance at 31 December	895	943	(38)	125	422	8	47	675	3,077	67	3,144

The above amounts are presented net of deferred tax. The deferred tax charged or credited directly to equity is set out in note 23.

During 2007, Codan A/S purchased £24m of its own shares on the market. In addition, the Group launched a voluntary conditional public tender offer for the acquisition of all the outstanding issued shares and voting rights in Codan A/S. As a result the Group acquired sufficient shareholding to effect a compulsory acquisition of the remaining shares and, as the transaction is not reversible, to account for 100% of the subsidiary. The total consideration was £590m. The two transactions reduced minority interests by £246m and shareholders' funds by £368m.

Ordinary and preference shares

During the year **24,707,235** (2007: 12,448,823) ordinary shares were issued on the exercise of employee share options for a cash consideration of **£19m** (2007: £9m). The Parent Company also issued **51,770,891** (2007: 66,632,200) ordinary shares during the year under the scrip scheme as approved by shareholders.

During 2007, to fund the acquisition of Codan A/S the Parent Company issued 186,350,000 ordinary shares in a placing raising gross proceeds of approximately £300m. The placing was made through a company established specifically for the placing. The placing was structured in such a way as to enable the Parent Company to obtain merger relief on the issue of the placing shares in accordance with section 131 of the Companies Act 1985. The effect of this is to relieve the Parent Company of a requirement to credit any amount paid up on the shares in excess of their nominal value to a share premium account. This excess was therefore recognised in retained earnings.

The total nominal value of ordinary shares issued during the year was **£20m** (2007: £74m).

	2008 £m	2007 £m
Authorised		
4,250,000,000 ordinary shares of 27.5p each (2007: 3,923,636,364 ordinary shares of 27.5p each)	**1,169**	1,079
300,000,000 preference shares of £1 each (2007: 300,000,000 preference shares of £1 each)	**300**	300
Issued and fully paid		
3,329,435,791 ordinary shares of 27.5p each (2007: 3,252,957,665 ordinary shares of 27.5p each)	**915**	895
125,000,000 preference shares of £1 each (2007: 125,000,000 preference shares of £1 each)	**125**	125
	1,040	1,020

The Royal & SunAlliance ESOP Trust holds ordinary shares in the Parent Company, which may subsequently be transferred to employees (other than the executive directors). At 31 December 2008 the Trust held **7,976,673** ordinary shares (2007: 15,102,896) in the Parent Company with a nominal value of **£2m** (2007: £4m) and a mid market value, based on the market value of the Parent Company's shares at the close of business on 31 December 2008 as shown in the Official List of the London Stock Exchange, of **£11m** (2007: £22m).

The Royal & SunAlliance ESOP Trust No 2 holds ordinary shares in the Parent Company, which may subsequently be transferred to employees including executive directors. At 31 December 2008 the Trust held **3,919,975** ordinary shares (2007: 4,938,894) in the Parent Company with a nominal value of **£1m** (2007: £1m) and a mid market value, based on the market value of the Parent Company's shares at the close of business on 31 December 2008 as shown in the Official List of the London Stock Exchange, of **£5m** (2007: £7m).

Rights attaching to the shares

The rights attaching to each class of share may be varied with the consent of the holders of 75% of the issued shares of that class.

Preference shareholders shall not have any right to receive notice of, attend, speak or vote at any general meeting of the Parent Company unless:

- The preferential dividend on such shares for the dividend payment period immediately prior to the issue of the notice is in arrears or if any arrears of deficiency of dividend in respect of any preceding period has not been paid in full
- A resolution is proposed varying the rights attached to preference shares, for the winding up of the Parent Company or for a reduction of capital in the Parent Company (in which case preference shareholders may only vote on such resolution)
- In such other circumstances as the directors may determine prior to the allotment of any preference shares.

The Parent Company in general meeting may by ordinary resolution declare dividends, but no dividend shall exceed the amount recommended by the directors or permitted by law. The directors may also pay such interim dividends as they think fit and pay the fixed dividends payable on any shares of the Parent Company half yearly or otherwise on fixed dates. Subject to shareholder approval, the directors may allow shareholders to receive new ordinary shares in lieu of dividends paid in cash.

Provided a resolution of the Board exists, and in priority to any payment of dividend to other shareholders (other than any dividend not exceeding 0.1p per share), holders of preference shares are entitled to a cumulative preferential dividend of 7.375% per annum, payable out of the profits available for distribution, to be distributed in half yearly instalments and the shares are not redeemable. Preference shareholders have no further right to participate in the profits of the Parent Company. In addition, preference shares do not confer:

- Any right to participate in any offer by way of rights or otherwise to subscribe for additional shares in the Parent Company (except where required by law)
- Any rights of conversion
- Any right to participate in any issue of bonus shares.

Notes to the financial statements continued

18. Equity and reserves continued

The directors may deduct from any dividend or other monies payable to any shareholder all sums of money presently payable by him to the Parent Company on account of calls or otherwise in relation to his shares in the Parent Company.

If the Parent Company is wound up, the liquidator may, with the sanction of an extraordinary resolution of the Parent Company divide among the shareholders the whole or any part of the assets of the Parent Company and may, for such purpose, set such value as he deems fair upon any property to be divided. The liquidator may also, with like sanction, vest the whole of any part of the Parent Company's assets in trustees upon such trusts for the benefit of the contributories as the liquidator shall think fit. No shareholder shall be compelled to accept any shares or other securities or other assets that are subject to any liability.

On a return of capital on a winding up (liquidation), preference shareholders are entitled, in priority to holders of ordinary shares of the Parent Company, to receive out of the surplus assets of the Parent Company any arrears and accruals of the dividend together with the greater of the price at which the gross yield on each preference share is equal to the mean gross yield on 3.5% War Loan or such Government Stock as may be agreed (but not exceeding twice the nominal amount of the preference share) and the nominal amount of the share together with any premium paid on issue.

The directors may make calls on shareholders in respect of monies unpaid on their shares. If any call is not complied with the directors may serve a notice on such shareholder requiring him to pay the call together with any interest and expenses incurred by the Parent Company. Failure to comply with a notice may result in forfeiture of any share which is the subject of the notice (including any dividends declared and other monies payable in respect of the shares so forfeited).

The Parent Company has a first and paramount lien on every share that is not fully paid for all monies called or payable in respect of such share. The Parent Company may sell any share on which the Parent Company has a lien passed following service of a notice on the shareholder demanding payment of the sum and giving notice of the Parent Company's intention to sell in default of such payment.

The Parent Company shall be entitled to sell any share of a shareholder if no cheque, warrant or order sent by the Parent Company in respect of the share in question has been cashed and no communication has been received by the Parent Company from the shareholder for a period of 12 years.

No shareholder is, unless the directors otherwise determine, entitled to attend or vote either personally or by proxy at any general meeting if:

- Any call or any sum presently payable by him to the Parent Company in respect of such share remains unpaid or
- The shareholder has failed to comply with a notice under section 793 of the Companies Act 2006 and is in default for a period of 14 days from the date of service of such notice.

Further, if a shareholder who holds 0.25% or more (in nominal value) of the issued shares is in default of a section 793 notice then the directors may also withhold the payment of any dividend and restrict the transfer of shares held by such shareholder.

Save with the consent of preference shareholders, the directors shall not increase the amount of any shares of any class (or any securities convertible into any shares of any class), ranking as regards participation in the profits or assets of the Parent Company (otherwise than on a redemption or purchase by the Parent Company of any such share) in priority to the preference shares.

The directors may refuse to register any transfer of any share which is not a fully paid up share provided that such refusal does not prevent dealing in the shares from taking place on an open and proper basis. The directors may likewise refuse to register any transfer in favour of more than four persons jointly.

The directors may also refuse to register any transfer of any certificated share unless:

- A duly stamped instrument of transfer is delivered to the Parent Company's registered office together with the certificates of the shares to which it relates and any other evidence that the directors may reasonably require to show the right of the transferor to make the transfer and
- The instrument of transfer is in respect of only one class of share.

The directors can require a shareholder to provide evidence that shares held by such shareholder are not held by or on behalf of a US Holder (as defined in the Articles of Association). The directors may require a US Holder to sell its shares to a non US resident, failing which the Parent Company may effect a sale of such shares. The directors may refuse to register a transfer by a US Holder where it is made to a US resident.

19. Loan capital

	2008 £m	2007 £m
Subordinated guaranteed US$ bonds	**15**	11
Subordinated guaranteed Euro bonds	**481**	365
Total dated loan capital	**496**	376
Subordinated Sterling perpetual guaranteed bonds	**310**	305
Subordinated guaranteed perpetual notes	**505**	513
Total loan capital	**1,311**	1,194

The subordinated guaranteed US Dollar bonds ('Yankee Bonds') have a nominal value of $23,679,000 and a redemption date of 15 October 2029. The rate of interest payable on the Yankee Bonds is 8.95%.

The subordinated guaranteed Euro bonds (€500m) have a redemption date of 15 October 2019. €200m of the Euro bonds bear interest at a fixed rate of 6.875% until 15 October 2009 and a floating rate thereafter. €300m of the Euro bonds bear interest at a floating rate from the date of issue of EURIBOR plus 1.25%. The Parent Company has the option to repay the Euro bonds on specific dates from 15 October 2009. If the bonds are not repaid on that date, the rate of interest payable would be EURIBOR plus 2.25%.

The subordinated Sterling perpetual guaranteed bonds have a nominal value of £375m and the rate of interest payable is 6.701% of the nominal value. The Group has the option to repay the bonds on specific dates starting 12 July 2017. If the bonds are not repaid, from that date, the interest rate payable would be LIBOR plus 2.51%.

The subordinated guaranteed perpetual notes have a nominal value of £450m and pay an annual coupon of 8.50% with an option to call the notes, or if not called for the coupon rate to be reset, on 8 December 2014 and every five years thereafter.

The bonds and the notes are contractually subordinated to all other creditors of the Parent Company such that in the event of a winding up or of bankruptcy, they are to be repaid only after the claims of all other creditors have been met.

The aggregate fair value of the dated loan capital, subordinated Sterling perpetual guaranteed bonds, and subordinated guaranteed perpetual notes at 31 December 2008 is **£1,079m** (2007: £1,234m).

20. Insurance contract liabilities

	2008 £m	2007 £m
Provision for unearned premiums	**3,835**	3,383
Provision for losses and loss adjustment expenses	**11,220**	10,344
Total insurance contract liabilities	**15,055**	13,727

Provision for unearned premiums

The following changes have occurred in the provision for unearned premiums during the year:

	2008 £m	2007 £m
Provision for unearned premiums at 1 January	**3,383**	2,969
Premiums written	**7,273**	6,596
Less: premiums earned	**(7,161)**	(6,361)
Changes in provision for unearned premiums	**112**	235
Gross portfolio transfers, acquisitions and disposals	**(3)**	37
Exchange adjustment	**343**	142
Provision for unearned premiums at 31 December	**3,835**	3,383

Notes to the financial statements continued

20. Insurance contract liabilities continued

Provision for losses and loss adjustment expenses

The following changes have occurred in the provision for losses and loss adjustment expenses during the year:

	2008 £m	2007 £m
Provision for losses and loss adjustment expenses at 1 January	**10,344**	9,821
Claims losses and expenses incurred	**4,205**	4,044
Total claims payments made in the year, net of recoveries	**(4,747)**	(4,145)
Gross portfolio transfers, acquisitions and disposals	**(12)**	204
Exchange adjustment	**1,362**	421
Other movements	**68**	57
Transfer to non current and disposal group assets held for sale	**–**	(58)
Provision for losses and loss adjustment expenses at 31 December	**11,220**	10,344

Assumptions

The total value of outstanding claims provisions less related reinsurance recoveries before discounting amounted to **£10,391m** (2007: £9,288m).

Claims on certain classes of business have been discounted as follows:

		Discount rate		Average number of years to settlement	
	Category	2008 %	2007 %	2008 Years	2007 Years
UK	Asbestos and environmental	**5.00**	5.00	**15**	15
Scandinavia	Disability	**3.66**	3.66	**11**	12
Canada	Asbestos and environmental	**5.00**	5.00	**6**	6

In determining the average number of years to ultimate claims settlement, estimates have been made based on the underlying claims settlement patterns.

Claims development tables

The tables below present changes in the historical provision for losses and loss adjustment expenses that were established in 2001 and the provision for losses and loss adjustment expenses arising in each subsequent accident year. The tables are presented at current year cumulative average exchange rates and have been adjusted for operations that have been disposed of.

The top triangle of the tables presents the estimated provision for ultimate incurred losses and loss adjustment expenses at the end of each accident year as at each balance sheet date.

The lower (paid) triangle of the tables presents the amounts paid against those provisions in each subsequent accounting period.

The estimated provision for ultimate incurred losses changes as more information becomes known about the actual losses for which the initial provisions were set up and as the rate of exchange changes. The 2008 redundancy/(deficiency) represents the claims development of earlier accident years in the current accounting period.

Consolidated claims development table gross of reinsurance

	2001 and prior £m	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	**2008 £m**	Total £m
Estimate of cumulative claims									
At end of accident year	9,457	3,229	3,168	2,639	2,790	2,464	2,802	**2,557**	
One year later	10,029	2,993	3,001	2,427	2,710	2,488	2,819		
Two years later	10,230	3,077	2,889	2,253	2,613	2,406			
Three years later	10,553	3,047	2,778	2,179	2,498				
Four years later	10,882	2,976	2,702	2,107					
Five years later	11,349	2,944	2,650						
Six years later	11,213	2,912							
Seven years later	11,005								
Claims paid									
One year later	3,084	1,290	1,175	900	1,197	1,014	1,311		
Two years later	1,554	460	351	299	349	376			
Three years later	1,268	310	240	207	199				
Four years later	789	205	174	158					
Five years later	522	111	116						
Six years later	407	88							
Seven years later	359								
Cumulative claims paid	7,983	2,464	2,056	1,564	1,745	1,390	1,311		
2008 redundancy/(deficiency)	208	32	52	72	115	82	(17)		544
Reconciliation to the balance sheet									
Current year provision before discounting	3,022	448	594	543	753	1,016	1,508	**2,557**	10,441
Exchange adjustment to closing rates									999
Discounting									(717)
Annuities									497
Present value recognised in the balance sheet									**11,220**

Notes to the financial statements continued

20. Insurance contract liabilities continued

Consolidated claims development table net of reinsurance

	2001 and prior £m	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	**2008 £m**	Total £m
Estimate of cumulative claims									
At end of accident year	7,380	2,534	2,314	2,139	2,321	2,332	2,399	**2,343**	
One year later	7,660	2,479	2,317	2,014	2,178	2,300	2,394		
Two years later	7,788	2,481	2,235	1,836	2,098	2,221			
Three years later	8,181	2,462	2,129	1,768	2,030				
Four years later	8,229	2,382	2,072	1,712					
Five years later	8,699	2,353	2,027						
Six years later	8,637	2,322							
Seven years later	8,552								
Claims paid									
One year later	2,372	1,036	835	675	887	929	1,068		
Two years later	1,213	347	286	247	280	332			
Three years later	1,063	254	200	178	161				
Four years later	557	166	104	134					
Five years later	395	90	88						
Six years later	259	72							
Seven years later	254								
Cumulative claims paid	6,113	1,965	1,513	1,234	1,328	1,261	1,068		
2008 redundancy	85	31	45	56	68	79	5		369
Reconciliation to the balance sheet									
Current year provision before discounting	2,439	357	514	478	702	960	1,326	**2,343**	9,119
Exchange adjustment to closing rates									835
Discounting									(671)
Annuities									437
Present value recognised in the balance sheet									**9,720**

The loss development tables above are presented on an undiscounted basis. Prior year development in 2008 showed favourable experience across all accident years and regions and totalled £369m, net of reinsurance. The total discounting at the end of 2008 was £671m representing an increase of £70m in the year, due to the impact of foreign exchange. In Scandinavia certain long tail liabilities are settled by an annuity and the discounted value of these annuities is shown separately. At the year end the annuity reserves were £437m (2007: £327m) with the increase in the year driven primarily by foreign exchange and growth in the business.

21. Insurance and reinsurance liabilities

	2008 £m	2007 £m
Direct insurance creditors	**224**	166
Reinsurance creditors	**321**	260
Total insurance and reinsurance liabilities	**545**	426

22. Borrowings

The Group's borrowings of **£300m** (2007: £303m) primarily relate to loans from credit institutions under a repurchase agreement. Further information is contained in the risk management section.

At 31 December 2008 total unsecured loans from credit institutions under committed credit facilities of **£455m** (2007: £500m) were available to the Group. There were no amounts outstanding at 31 December 2008 (2007: £nil). The facility expires in 2013.

At 31 December 2008 and 2007 the Group had in place a one billion US Dollar Euro commercial paper program. There were no amounts outstanding at 31 December 2008 (2007: £nil).

The Articles of Association of the Group defines a cap on borrowing limits. This cap is not being amended at the 2009 AGM. At 31 December 2008 the cap on borrowing limits was **£5,243m** (2007: £4,221m) of which **£1,625m** (2007: £1,507m) had been utilised.

23. Current and deferred tax

Current tax

	Asset		Liability	
	2008 £m	2007 £m	**2008 £m**	2007 £m
To be settled within 12 months	**27**	13	**124**	15
To be settled after 12 months	**13**	6	**91**	77
	40	19	**215**	92

Deferred tax

	2008 £m	2007 £m
Deferred tax assets	**142**	87
Deferred tax liabilities	**(238)**	(224)
Net deferred tax position at 31 December	**(96)**	(137)

The following are the major deferred tax liabilities and assets recognised by the Group and their movements during the year:

	Reclassification of debt £m	Retirement benefit obligations £m	Net insurance contract liabilities £m	Revaluation of investments £m	Security Fund/ Safety Reserve £m	Other temporary differences £m	Total £m
Deferred tax at 1 January 2007	22	(8)	35	(109)	(101)	(129)	(290)
(Charge)/credit to the income statement for the year	–	(48)	31	3	103	49	138
(Charge)/credit to equity for the year	(2)	9	-	24	–	(7)	24
Net liability on acquisition/disposal of subsidiaries	–	–	1	1	–	(15)	(13)
Exchange adjustment	–	1	4	(2)	(2)	(6)	(5)
Effect of change in tax rates							
- income statement	–	–	(3)	(1)	–	5	1
- equity	(2)	4	–	6	–	–	8
Deferred tax at 31 December 2007	18	(42)	68	(78)	–	(103)	(137)
(Charge)/credit to the income statement for the year	**–**	**(19)**	**(48)**	**14**	**–**	**120**	**67**
(Charge)/credit to equity for the year	**(2)**	**(83)**	**–**	**37**	**–**	**11**	**(37)**
Net liability on acquisition/disposal of subsidiaries	**–**	**–**	**–**	**–**	**–**	**8**	**8**
Exchange adjustment	**–**	**1**	**4**	**(2)**	**–**	**–**	**3**
Deferred tax at 31 December 2008	**16**	**(143)**	**24**	**(29)**	**–**	**36**	**(96)**

International Financial Reporting Standards require the Danish Security Fund and Swedish Safety Reserve in Codan A/S to be recognised within shareholders' equity rather than as liabilities. During 2007, the Group acquired the minority interest in its Scandinavian subsidiaries and as a result of the change in circumstances concluded that no tax base and associated temporary tax difference existed in respect of these reserves and the associated deferred tax liability was released.

Notes to the financial statements continued

23. Current and deferred tax continued

The deferred income tax credited/(charged) to equity is as follows:

	2008 £m	2007 £m
Fair value reserves in shareholders' equity		
Available for sale financial assets	**37**	30
Group occupied property	**10**	(4)
Retirement benefit obligations	**(83)**	13
Share options	**1**	(3)
Reclassification of debt	**(2)**	(4)
Total (charged)/credited to equity for the year	**(37)**	32

The aggregate current tax relating to items that were credited to equity is **£57m** (2007: £3m).

At the balance sheet date, the Group had unused tax losses of **£1,582m** (2007: £1,244m) and unused tax credits of **£14m** (2007: £33m) available for offset against future profits. A deferred tax asset of **£16m** (2007: £2m) has been recognised in respect of losses included within other temporary differences at 31 December 2008. No deferred tax asset has been recognised in respect of **£1,523m** (2007: £1,237m) tax losses and unused tax credits of **£14m** (2007: £33m) due to the unpredictability of future profit streams. Included in unrecognised tax losses are losses of **£68m** (2007: £51m) which will expire between 2009 and 2028. Other tax losses and unused credits may be carried forward indefinitely.

The Group does not recognise deferred tax on the unremitted earnings of overseas subsidiaries, as the Group is able to control the remittance of earnings to the UK and there is no intention to remit any such earnings to the UK in the foreseeable future if the remittance would trigger a material incremental UK tax liability. The temporary differences in respect of the retained earnings of overseas subsidiaries is **£1,410m** (2007: £959m).

24. Provisions

Carrying amount

	2008 £m	2007 £m
Pensions and post retirement obligations	**96**	105
Reorganisation provisions	**14**	37
Other provisions	**130**	189
Total provisions at 31 December	**240**	331

Of the above, **£155m** is due to be settled outside of 12 months (2007: £139m).

Reorganisation provisions comprise costs relating to reorganisations mainly within the UK business. These provisions primarily comprise severance and property costs and are part of an ongoing programme to achieve business improvement and expense savings.

Other provisions includes **£60m** (2007: £65m) held relating to vacant property leases, dilapidations and refurbishments, the costs relating to which will be borne across the period over which the leases expire, which is up to 20 years. Other provisions also includes various litigation provisions of **£nil** (2007: £10m), the payment of which is dependent upon legal processes and Motor Insurance Bureau provision of **£23m** (2007: £33m).

See note 26 for further information regarding the pensions and post retirement benefit obligations.

Movements during the year on reorganisation and other provisions

	Reorganisation provisions £m	Other provisions £m
Provisions at 1 January 2008	**37**	**189**
Exchange adjustment	**–**	**3**
Credited	**7**	**29**
Utilised	**(27)**	**(89)**
Released	**(3)**	**(3)**
Acquisition of subsidiary	**–**	**1**
Provisions at 31 December 2008	**14**	**130**

25. Other liabilities

	2008 £m	2007 £m
Deposits received from reinsurers	**76**	64
Derivative trading liabilities	**146**	62
Other creditors	**480**	614
Accruals and deferred income	**341**	347
Total other liabilities	**1,043**	1,087
To be settled within 12 months	**866**	1,016
To be settled after 12 months	**177**	71

In 2003 a subsidiary of the Group wrote an Adverse Development Cover (ADC) contract with its former US subsidiary. The liabilities arising under the ADC contract comprise an insurance component and a deposit component. The liability arising under the insurance component of £0.1bn represents the timing risk on the settlement of those liabilities. The financial liability arising under the deposit component is offset by the value of funds held in a trust fund whose trust deed only permits the trust fund assets to be used to settle amounts due under the ADC. The value of the funds held in trust at 31 December 2008 is £0.6bn and the value of the liability of the deposit component is £0.6bn.

The insurance component is accounted for within insurance liabilities and the deposit component, offset by the value of the funds held in the trust account, is recognised under other liabilities.

26. Retirement benefit obligations

The Group operates defined contribution pension schemes, funded and unfunded defined benefit pension schemes, and has other post retirement obligations.

Defined contribution pension schemes

Costs of **£39m** (2007: £34m) were recognised in respect of defined contribution schemes by the Group. The Group's Swedish subsidiaries are part of a multi employer defined benefit scheme along with other financial institutions in Sweden. As it is not possible to determine the assets and liabilities in respect of any one employer under this scheme, it is included in these accounts as a defined contribution scheme. Contributions of **£9m** (2007: £23m) were paid to this scheme during 2008 and are included in the costs shown above. The latest information regarding the funding of this scheme is taken from the interim report for the first half of 2008, when the scheme funding rate was **119%** (2007: 132%). The Group's Swedish subsidiaries' share of the total multi employer scheme was less than **15%** (2007: less than 15%).

Defined benefit pension schemes and other post retirement benefits

The major defined benefit pension schemes are located in the UK. The assets of these schemes are held mainly in separate trustee administered funds.

In April 2002, the primary UK defined benefit schemes were effectively closed to new entrants and in 2005, following discussions with the Trustees and consultation with the members, the UK defined benefit schemes were altered from providing benefits on a final salary basis to benefits on a revalued average salary basis with effect from 1 January 2006. Under the new benefit formula, the accrued benefits of current active members are based on salaries at the date of change and will increase in line with inflation each year (limited to 5% in any year) up to their retirement date. Benefits earned in each year from 1 January 2006 are based on salaries in that year and are revalued up to retirement.

In addition to these changes, the 2002 Scheme (which was the scheme to which new UK employees had been admitted following the closure of the defined benefit schemes to new members) has been closed to further accrual from 1 January 2006. It has been replaced by a stakeholder arrangement and members of the 2002 Scheme and future new employees in the UK accrue future benefits on a defined contribution basis under the stakeholder scheme.

For the two main UK defined benefit schemes, the level of contributions in 2008 were **23%** and **22%** of pensionable salaries (2007: 23% and 22%). Additional contributions totalling **£38m** (2007: £86m) were made to the schemes, in accordance with the plan to reduce their funding deficits. Expected contributions to pension and post retirement benefit schemes for the year ending 31 December 2009 are approximately **£71m**, including a further **£33m** of additional contributions.

The major defined benefit schemes are subject to regular valuation using the projected unit method which is the basis used to determine the pension cost in the consolidated income statement. Independent, qualified actuaries carry out valuations of the major defined benefit schemes for the purposes of assessing pension costs.

Notes to the financial statements continued

26. Retirement benefit obligations continued

The Group also provides post retirement healthcare benefits to certain current and retired Canadian employees. The benefits are not prefunded. Life insurance benefits, which provide varying levels of coverage, are provided at no cost to retirees. Healthcare benefits, which also provide varying levels of coverage, require retiree contributions in certain instances. Benefits are generally payable for life. The estimated discounted present values of the unfunded accumulated obligations are calculated in accordance with the advice of independent, qualified actuaries.

Movement in surplus during the year:

	2008 £m	2007 £m
Surplus at 1 January	158	32
Total pension expense	(52)	(9)
Employer contribution	123	168
Actuarial gains/(losses)	287	(28)
Acquisition of subsidiary	–	1
Exchange adjustment	(10)	(6)
Pension and post retirement surplus	**506**	158
Deferred tax in respect of net pension and post retirement asset	(143)	(42)
Net pension and post retirement surplus at 31 December	**363**	116

The amounts recognised in the income statement are as follows:

	2008			2007
	UK £m	Other £m	Total £m	Total £m
Current service cost	37	11	48	52
Interest cost	262	18	280	243
Expected return on scheme assets	(281)	(18)	(299)	(294)
Past service cost	22	1	23	12
Gains on curtailment	–	–	–	(4)
Total (included in staff costs)	**40**	**12**	**52**	9

The actuarial gains/(losses) recognised in equity are as follows:

	2008			2007
	UK £m	Other £m	Total £m	Total £m
Actual return on scheme assets	(63)	(51)	(114)	383
Less: expected return on scheme assets	(281)	(18)	(299)	(294)
Actual return on assets (below)/in excess of expectations	(344)	(69)	(413)	89
Experience losses on liabilities	(97)	(4)	(101)	(78)
Change in actuarial assumptions	734	67	801	(39)
Actuarial gains/(losses)	**293**	**(6)**	**287**	(28)

The accumulated actuarial gains since 1 January 2004 are **£349m** (2007: £62m).

	2008 UK £m	2008 Other £m	2008 Total £m	2007 Total £m
Present value of funded obligations	4,229	232	4,461	5,012
Present value of unfunded obligations	4	71	75	74
Present value of obligations	4,233	303	4,536	5,086
Equities	1,063	110	1,173	1,314
Bonds	3,332	121	3,453	3,527
Cash	67	4	71	177
Property and other	343	2	345	226
Total assets in the schemes	4,805	237	5,042	5,244
Surplus/(deficit) on continuing operations	572	(66)	506	158
Continuing operations analysed:				
Defined benefit pension schemes	572	(42)	530	184
Other post retirement benefits	–	(24)	(24)	(26)
Schemes in surplus (note 16)	576	26	602	263
Schemes in deficit (note 24)	(4)	(92)	(96)	(105)

The following is a reconciliation of the Group's retirement benefit obligations:

	2008 £m	2007 £m
Retirement benefit obligations at 1 January	5,086	4,838
Current service costs	48	52
Past service costs	23	12
Interest costs	280	243
Contributions by scheme participants	2	2
Actuarial (gain)/loss on obligations	(700)	117
Gain on curtailments	–	(4)
Benefits paid	(242)	(226)
Acquisition of subsidiary	2	13
Exchange adjustment	37	39
Retirement benefit obligations at 31 December	4,536	5,086

The following is a reconciliation of the Group's pension schemes' assets:

	2008 £m	2007 £m
Pension schemes' assets at 1 January	5,244	4,870
Return on schemes' assets	(114)	383
Contributions by the employer	123	168
Contributions by schemes' participants	2	2
Benefits paid	(242)	(226)
Acquisition of subsidiary	2	14
Exchange adjustment	27	33
Pension schemes' assets at 31 December	5,042	5,244

Notes to the financial statements continued

26. Retirement benefit obligations continued

Additional information for the current annual period and previous four annual periods:

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
At 31 December					
Present value of defined benefit obligation	**4,536**	5,086	4,838	5,439	4,939
Fair value of plan assets	**5,042**	5,244	4,870	4,967	4,226
Surplus/(deficit)	**506**	158	32	(472)	(713)
Experience adjustments on schemes liabilities	**(101)**	(78)	42	(50)	87
Experience adjustments on schemes assets	**(413)**	89	(14)	434	145

Assumptions

The principal actuarial assumptions used were as follows:

	UK		Other	
	2008 %	2007 %	**2008 %**	2007 %
Assumptions used in calculation of retirement benefit obligation:				
Discount rate	**6.2**	5.6	**6.5**	5.4
Annual rate of general inflation	**2.8**	3.2	**2.0**	2.5
Annual rate of increase in salaries	**4.3**	4.7	**3.9**	4.4
Annual rate of increase in pensions	**2.8**	3.2	**2.0**	2.5
Assumptions used in calculation of income statement credit/charge in year:				
Discount rate	**5.6**	5.1	**5.4**	4.9
Expected return on:				
Equities	**7.5**	7.5	**8.3**	8.3
Bonds	**5.0**	4.4	**5.3**	5.3
Other	**6.5**	6.1	**3.5**	3.5

Expected return on schemes' assets

The weighted average expected return on schemes' assets across the Group for 2008 was **6%** (2007: 6%). The expected return on schemes' assets are determined for each asset class by considering both market conditions at the opening balance sheet date and any expectations for longer term changes in current returns. All returns are net of investment expenses.

Mortality rate

The mortality assumptions are set following investigations of the main schemes' recent experience by the schemes' actuaries for the funding valuations. The mortality assumptions adopted for the main UK schemes used the PMA92 and PFA92 mortality tables for males and females respectively, with age ratings to reflect the schemes' recent experience compared with that expected under these tables.

Reductions in future mortality rates are allowed for using the 'medium cohort' projection and using the projected mortality rates applicable to calendar year 2014 for current pensioners and 2032 for future pensioners. The weighted average assumptions imply that a current pensioner aged 60 has an expected future lifetime of **25.8** years (males) and **27.0** years (females) and a future pensioner aged 60 has a future lifetime of **27.2** years (males) and **28.2** years (females).

Commutation

Each of the UK defined benefit pension schemes has changed its rules to allow for increased commutation following 'A day' in April 2006. The commutation factors are broadly cost neutral (i.e. when valued on the IAS 19 basis, the amount of cash taken is approximately equal to the value of the pension being given up). For this reason there is no change made to previous practice whereby the accounting valuation makes no allowance for commutations.

Post retirement medical benefits

The valuation of liabilities for post retirement liabilities in Canada assumes **7%** decreasing to **5%** in 2017 (2007: 7% decreasing to 5% in 2017).

Sensitivity analysis

The discount rate, the assumed inflation rate and the mortality assumptions all have a significant effect on the IAS 19 accounting valuation. A 0.1% increase in the discount rate would reduce the defined benefit obligations in the UK by **£68m**. A 0.1% increase in the inflation rate assumption would increase the defined benefit obligations in the UK by **£59m**. An increase of one year in life expectancy would increase the defined benefit obligations by approximately **£124m**.

The effect of an increase of one percentage point and the effect of a decrease of one percentage point in the assumed medical cost trend rates in Canada on the following is set out below:

	1% increase		1% decrease	
	2008 £m	2007 £m	**2008 £m**	2007 £m
Aggregate of the current service cost and interest components of net periodic post employment medical costs	**0.5**	0.4	**0.4**	0.3
Accumulated post employment benefit obligation for medical costs	**3.5**	3.9	**2.8**	3.1

27. Share based compensation

The Group has four types of share based payment plans which are settled in the form of ordinary shares: the Executive Share Option Scheme; the Sharesave Plan; the Share Matching Plan; and the Long Term Incentive Plan. Dilution levels for all schemes are held strictly within Association of British Insurers limits.

The total employment cost recorded in the income statement for all plans was **£25m** in 2008 (2007: £19m). These costs include the costs associated with plans which are settled in the form of ordinary shares for awards that have been granted after 7 November 2002. The value of equity settled awards granted prior to this date has been excluded in accordance with the transitional provisions contained in IFRS 2 'Share Based Payment'.

Executive Share Option Scheme

The Group operates an Executive Share Option Scheme, which provides options to purchase ordinary shares to officers and other key employees at prices not less than the fair value of the ordinary shares at the date of grant.

The performance conditions in respect of awards under the Executive Share Option Scheme are described on page 59. The exercise price of all options is the fair value of the ordinary shares on the date of grant. All options expire 10 years after the date of the grant.

Additional information with respect to the Executive Share Option Scheme at 31 December is as follows:

	2008		2007	
	Number of shares	**Weighted average exercise price***	Number of shares	Weighted average exercise price*
Options outstanding at 1 January	**53,633,132**	**139.01**	73,839,962	142.71
Exercised	**(13,230,719)**	**83.46**	(3,865,688)	86.09
Forfeited	**(1,111,080)**	**197.77**	(1,890,835)	139.84
Expired	**(2,176,911)**	**364.25**	(1,890,782)	287.22
Cancelled	**–**	**–**	(12,559,525)	154.63
Options outstanding at 31 December	**37,114,422**	**143.84**	53,633,132	139.01

*Sterling (pence)

The following share options under the Executive Share Option Scheme are outstanding or exercisable at 31 December:

Options outstanding

	2008			2007		
Range of exercise prices	**Number of shares**	**Weighted average remaining contractual life (years)**	**Weighted average exercise price***	Number of shares	Weighted average remaining contractual life (years)	Weighted average exercise price*
50.1 – 100.0	**26,492,486**	**5.79**	**80.38**	39,860,028	6.89	81.04
100.1 – 150.0	**1,625,681**	**4.89**	**114.41**	2,235,290	5.76	114.31
200.1 – 250.0	**2,386,015**	**3.19**	**234.23**	2,705,104	4.19	234.23
250.1 – 300.0	**1,473,816**	**1.23**	**278.65**	1,648,006	2.23	278.65
300.1 – 350.0	**61,819**	**2.88**	**312.58**	61,819	3.88	312.58
350.1 – 400.0	**2,359,726**	**2.18**	**380.16**	2,666,029	3.18	380.15
400.1 – 450.0	**2,714,879**	**1.14**	**418.94**	4,456,856	1.69	413.81
	37,114,422	**4.83**	**143.84**	53,633,132	5.95	139.01

*Sterling (pence)

Notes to the financial statements continued

27. Share based compensation continued

Options exercisable

	2008		2007	
	Number of shares	Weighted average exercise price*	Number of shares	Weighted average exercise price*
50.1 – 100.0	**26,492,486**	**80.38**	17,549,796	77.06
100.1 – 150.0	**1,625,681**	**114.41**	1,933,566	114.05
200.1 – 250.0	**2,386,015**	**234.23**	2,705,104	234.23
250.1 – 300.0	**1,473,816**	**278.65**	1,648,006	278.65
300.1 – 350.0	**61,819**	**312.58**	61,819	312.58
350.1 – 400.0	**2,359,726**	**380.16**	2,666,029	380.15
400.1 – 450.0	**2,714,879**	**418.94**	4,456,856	413.81
	37,114,422	**143.84**	31,021,176	178.68

*Sterling (pence)

Under the scheme, there were no awards during 2007 or 2008. The value of the awards is charged in the income statement over the vesting period. The weighted average share price on the dates the options were exercised in 2008 was **147.57p** (2007: 152.06p).

Sharesave Plan

Under the Group's Sharesave Plan (savings related) eligible employees can receive options to purchase ordinary shares at a price equal to 80% of the fair value of the ordinary shares on the date of grant. All options vest either three or five years from the grant date and expire six months after vesting. The number of shares available for purchase from the plan by each participant is limited to the whole number of shares purchasable from the aggregate value of the individual's savings contract upon maturity. An individual's maximum monthly contribution to all current savings contracts is £250.

Additional information with respect to the Sharesave Plan at 31 December is as follows:

	2008		2007	
	Number of shares	Weighted average exercise price*	Number of shares	Weighted average exercise price*
Options outstanding at 1 January	**62,307,155**	**84.59**	59,964,593	77.16
Granted	**13,932,736**	**117.00**	17,174,075	105.00
Exercised	**(13,497,523)**	**71.76**	(9,889,250)	64.72
Forfeited	**(2,333,568)**	**85.21**	(3,614,970)	79.70
Expired	**(915,562)**	**81.35**	(1,327,293)	173.94
Cancelled	**(2,077,872)**	**86.84**	–	–
Options outstanding at 31 December	**57,415,366**	**95.42**	62,307,155	84.59

*Sterling (pence)

The following share options under the Sharesave Plan are outstanding or exercisable as of 31 December:

Options outstanding

	2008			2007		
Range of exercise prices	Number of shares	Weighted average remaining contractual life (years)	Weighted average exercise price*	Number of shares	Weighted average remaining contractual life (years)	Weighted average exercise price*
50.1 – 100.0	**20,541,037**	**0.99**	**68.73**	36,716,673	1.29	69.54
100.1 – 150.0	**36,874,329**	**2.77**	**110.29**	25,590,482	3.25	106.20
	57,415,366	**2.13**	**95.42**	62,307,155	2.09	84.59

*Sterling (pence)

Options exercisable

	2008		2007	
	Number of shares	Weighted average exercise price*	Number of shares	Weighted average exercise price*
50.1 – 100.0	**2,145,334**	**75.00**	8,649,491	71.63

*Sterling (pence)

Under the Sharesave Plan, the weighted average estimated fair value per option granted by the Parent Company during 2008 was **42.31p** (2007: 45.84p). The fair value of share options granted under the Sharesave Plan during 2008 was **£6m** (2007: £8m). The value of the awards is charged in the income statement over the vesting period. The weighted average share price on the dates the options were exercised in 2008 was **147.21p** (2007: 150.57p).

Fair values for the options granted under the Sharesave Plan were estimated as of the date of grant using the Black Scholes pricing model with the following weighted average assumptions: dividend yields of **5.7%** (2007: 4.0%); expected volatilities of **30%** (2007: 30%); ordinary share price of **158.10p** (2007: 142.90p) risk free interest rates of **4.3%** (2007: 5.0%); and expected terms equal to the vesting terms of **3.2** or **5.2** years. An estimate based on past experience is made of the number of forfeitures during the vesting period due to employees leaving the Group. The actual share price at 31 December 2008 was **138.10p** (2007: 148.20p). The expected volatility is determined by reference to the actual volatility of the share price over the appropriate term ending on the grant date.

Share Matching Plan

The Group's Share Matching Plan for executive directors and other selected executives was adopted following approval obtained at the 2004 AGM. Awards were made during 2004 and 2005.

The performance conditions in respect of awards under the Share Matching Plan are described in the footnote to the long term incentive schemes table (audited part) on page 60. Under the plan, Deferred Share awards granted are held in trust for three years and are normally forfeited upon an employee leaving the Group. No further performance conditions apply.

Participants may also receive Matching Share awards up to a maximum of three times the number of Deferred Shares awarded. Matching Share awards are subject to the achievement of total shareholder return targets over a single two year period, with performance measured by comparison against other UK listed companies. Matching Share awards vest with the Deferred Share awards on the third anniversary of the date of grant to the extent that the performance conditions have been met.

Further information on the Share Matching Plan may be found in the footnote to the long term incentive scheme table (audited part) on page 60.

Additional information with respect to Deferred and Matching Share awards at 31 December is as follows:

	2008 Number of shares	2007 Number of shares
Outstanding Deferred Share awards at 1 January	**2,992,113**	3,433,720
Exercised	**(1,753,046)**	(327,775)
Forfeited	**(312,636)**	(113,832)
Outstanding Deferred Share awards at 31 December	**926,431**	2,992,113
Potential Matching Share awards	**2,412,825**	7,326,649
Total potential share awards outstanding at 31 December	**3,339,256**	10,318,762

Under the Share Matching Plan there were no awards granted in 2007 or 2008.

Long Term Incentive Plan

The Long Term Incentive Plan for executive directors and other selected executives was adopted following approval obtained at the 2006 AGM. Awards have been made each year since 2006 following shareholder approval.

The structure of the plan allows for a number of different types of awards to be made. Voluntary Deferred Shares are purchased by participants from net bonus payable (limited to a maximum value of 33% of net bonus); in addition, for senior executives, the Remuneration Committee may defer a portion of an individual's bonus (limited to 33% of that bonus) into an award over shares referred to for the purpose of the plan as Compulsory Deferred Shares. Voluntary Deferred Shares are held in trust for three years. Compulsory Deferred Shares are normally forfeited on an employee leaving the Group. No further performance conditions apply. The Remuneration Committee may make a conditional award of shares on a 'matched' basis to Voluntary and Compulsory Deferred Shares ('Matching Shares') up to a maximum of 2.5:1 and these are normally forfeited on an employee leaving the Group.

Additionally, the Remuneration Committee may make conditional awards of Performance Shares to senior executives and conditional awards of Restricted Shares to other executives and senior managers.

Awards of Performance Shares and Matching Shares related to Compulsory Deferred Shares are subject to a performance condition consisting of a combination of a return on equity target and a total shareholder return target (with performance measured by comparison against other European insurance companies) over a single three year performance period. Matching Shares related to Voluntary Deferred Shares are subject only to the return on equity performance condition. Restricted Shares are not subject to performance conditions. All awards vest on the third anniversary of the date of grant to the extent that the performance conditions have been met. Performance Shares and Restricted Shares are normally forfeited on an employee leaving the Group.

Further information on the Long Term Incentive Plan may be found outside these financial statements in the remuneration report.

Notes to the financial statements continued

27. Share based compensation continued

	2008				
	Restricted Shares	Voluntary Deferred Shares	Compulsory Deferred Shares	Performance Shares	Total
Share awards outstanding at 1 January	**8,063,261**	**1,372,433**	**3,102,956**	**9,274,148**	**21,812,798**
Granted	**4,061,147**	**1,027,843**	**2,083,620**	**5,933,652**	**13,106,262**
Exercised	**–**	**(57,236)**	**–**	**–**	**(57,236)**
Forfeited	**(295,675)**	**–**	**(46,479)**	**(70,456)**	**(412,610)**
Share awards outstanding at 31 December	**11,828,733**	**2,343,040**	**5,140,097**	**15,137,344**	**34,449,214**
Potential Matching Shares awards	**–**	**10,148,444**	**12,850,187**	**–**	**22,998,631**
Total potential share awards outstanding at 31 December	**11,828,733**	**12,491,484**	**17,990,284**	**15,137,344**	**57,447,845**

	2007				
	Restricted Shares	Voluntary Deferred Shares	Compulsory Deferred Shares	Performance Shares	Total
Share awards outstanding at 1 January	4,208,357	667,002	1,622,178	4,829,205	11,326,742
Granted	4,007,328	749,048	1,675,482	4,901,428	11,333,286
Exercised	–	(25,906)	–	–	(25,906)
Forfeited	(152,424)	(17,711)	(194,704)	(456,485)	(821,324)
Share awards outstanding 31 December	8,063,261	1,372,433	3,102,956	9,274,148	21,812,798
Potential Matching Shares awards	–	5,932,206	7,757,355	–	13,689,561
Total potential share awards outstanding 31 December	8,063,261	7,304,639	10,860,311	9,274,148	35,502,359

Under the Long Term Incentive Plan, the weighted average estimated fair value of each Restricted Share award granted by the Parent Company in 2008 was **116.68p** (2007: 140.68p). The weighted average estimated fair value of each Voluntary Deferred Share award was **£nil** (2007: £nil) and the weighted average estimated fair value of each potential associated Matching Share was **136.50p** (2007: 164.00p). The weighted average estimated fair value of each Compulsory Deferred Share award was **136.50p** (2007: 164.00p) and the weighted average estimated fair value of each potential associated Matching Share was **91.40p** (2007: 113.50p). The weighted average estimated fair value of each Performance Share award granted was **92.03p** (2007: 112.07p). The total fair value of the awards granted under the plan in 2008 was **£24m** (2007: £24m).

Fair values of the awards granted under the Long Term Incentive Plan scheme during 2008 are taken to be the share price on the day preceding the grant date, except for the Restricted Shares where the share price is reduced by an estimate of the value of dividends that will not be received. A dividend yield of **5.7%** (2007: 4.0%) was assumed. Market related performance criteria were based on an arithmetic mean estimate of performance against a specified group of 13 competitors and it is assumed that all non market related performance criteria would be met such that all awards would be exercisable. An estimate based on past experience is made of the number of forfeitures during the vesting period due to employees leaving the Group.

Other share based payments

Certain employees of the Group's former US operation held entitlements under the Equity Incentive Scheme for US Employees prior to the disposal of the operation. On disposal of the US operation the options under the scheme became cash settled and the majority of the options vested. There are also other plans under which awards have been granted to certain employees in the form of cash settled share based awards. Under these plans, if the vesting conditions are satisfied, cash awards are made based upon the underlying performance of the Parent Company's ordinary shares. Awards were made in 1999 and 2001 under old schemes and during 2004 and 2005 on terms that provide the same potential benefits as the Share Matching Plan. The liability in respect of these plans at 31 December 2008 was **£1m** (2007: £4m). The intrinsic value of awards that had vested at 31 December 2008 was **£1m** (2007: £4m).

28. Hedge accounting

The Group designates the loan capital denominated in Euros as a hedging instrument against the net investment in designated subsidiaries to reduce the foreign currency exchange risk. The book value of the hedging instrument at 31 December 2008 was **£481m** (2007: £365m). The fair value of the hedging instrument at 31 December 2008 was **£459m** (2007: £377m). The hedge ineffectiveness recognised in the income statement during 2008 is **£nil** (2007: £nil).

The Group designates certain forward exchange contracts as hedging instruments against the net investment in designated subsidiaries to reduce further the foreign currency exchange risk exposure. On designation, the interest element is separated from the forward exchange rate and is excluded from the hedge relationship. Effectiveness of the hedge is then measured using the spot rate, which is also the exchange rate used when measuring net investment in the designated subsidiaries. The fair value of the hedging instruments at 31 December 2008 is a liability of **£74m** (2007: £26m). The hedge ineffectiveness recognised in the income statement during 2008 is **£nil** (2007: £nil).

Further information on derivatives, including those designated as hedging instruments, can be found in the risk management section.

29. Subsidiaries

Country of incorporation		Principal activity
United Kingdom	Royal Insurance Holdings plc [1]	Holding company
	Royal & Sun Alliance Insurance plc	General insurance
	British Aviation Insurance Company Limited (57.1%)	General insurance
	The Globe Insurance Company Limited	General insurance
	The Marine Insurance Company Limited	General insurance
	Royal International Insurance Holdings Limited	Holding company
	Royal & Sun Alliance Reinsurance Limited	General insurance
	Sun Alliance and London Insurance plc	General insurance
	Sun Insurance Office Limited	General insurance
Argentina	Royal & Sun Alliance Seguros (Argentina) SA	General insurance
Bahrain	Royal & Sun Alliance Insurance (Middle East) Limited E.C. (50.01%)	General insurance
Brazil	Royal & Sun Alliance Seguros (Brasil) SA	General insurance
Canada	Roins Financial Services Limited	Holding company
	Quebec Assurance Company	General insurance
	The Johnson Corporation	Holding company
	Royal & Sun Alliance Insurance Company of Canada	General insurance
	Western Assurance Company	General insurance
	Canadian Northern Shield Insurance Company	General insurance
Chile	Royal & Sun Alliance Seguros (Chile) SA (99.4%)	General insurance
China	Sun Alliance Insurance (China) Limited	General insurance
Colombia	Royal & Sun Alliance Seguros (Colombia) SA (86.7%)	General insurance
Denmark	Codan A/S	Holding company
	Codan Forsikring A/S	General insurance
Guernsey	Insurance Corporation of the Channel Islands Limited	General insurance
Isle of Man	Tower Insurance Company Limited	General insurance
Mexico	Royal & Sun Alliance Seguros (Mexico) SA de C.V.	General insurance
Netherlands	RSA Overseas (Netherlands) BV	Holding company
	RSA Overseas Holdings BV	Holding company
Netherlands Antilles	Royal & Sun Alliance Insurance (Antilles) NV (51.0%)	General insurance
Norway	Duborgh Skadeforsikring AS	Insurance brokerage
	White Label Holding AS Group	Holding company
Republic of Ireland	RSA Insurance Ireland Limited	General insurance
	EGI Holdings Limited	Holding company
Sweden	Trygg-Hansa Försäkrings AB, Publikt	General insurance
Uruguay	Royal & Sun Alliance Seguros (Uruguay) SA	General insurance

Notes:

1. 100% direct subsidiary of RSA Insurance Group plc.
2. Except where indicated all holdings are of equity shares and represent 100% of the nominal issued capital. In all cases the proportion of voting power held equals the proportion of ownership interest.
3. Some subsidiaries have been omitted from this statement to avoid providing particulars of excessive length but none materially affects the results or assets of the Group.

Notes to the financial statements continued

30. Business combinations

Acquisition of subsidiaries

On 11 February 2008 the Group acquired 100% of the share capital of Fyfe Group Limited. On 31 March 2008 the Group acquired 100% of the share capital of Sertus Underwriting Limited. The total consideration was **£28m** and goodwill of **£25m** arose on acquisitions.

	£m
Intangible assets (excluding goodwill)	3
Other assets	3
Cash and cash equivalents	1
Other liabilities	(4)
Net assets	3
Cash consideration including acquisition costs	26
Deferred consideration	2
Goodwill on acquisitions	25

If the acquisitions had occurred on 1 January 2008, Group net written premiums for the year would have increased by **£1m** and the Group's profit after tax would have increased by **£nil**. The total profit after tax of the acquired entities since the acquisition dates included in the Group's profit for the period is **£1m**.

Goodwill is individually assessed on each acquisition. The goodwill shown above arose from the premium paid for strengthening the Group's market position in targeted business segments and acquiring the skilled workforce to drive future profitability in those segments. Goodwill also represents the future cost saving from expected synergies and economies of scale.

Disposal of subsidiaries

During the year disposals of subsidiary undertakings and books of business were made for total proceeds of **£125m**, giving rise to a pre tax profit of **£18m**. Group disposals during the year comprise:

- The disposal of Guildhall Insurance Company Limited on 29 February 2008. Following the writedown in 2007 the transaction generated proceeds, net of costs, of **£33m** and generated a pre tax profit of **£1m**. In 2007 the loss recognised as a result of remeasurement to fair value less costs to sell was £6m.
- The disposal of Ejendomsselskabet Gammel Longevej 60 ApS on 1 October 2008. The transaction generated proceeds, net of costs, of **£85m** and generated a pre tax loss of **£1m**.
- The dissolution of Royal & Sun Alliance SA on 18 May 2008. The transaction generated a pre tax profit of **£17m**. This represents foreign exchange, which is recycled from shareholders' funds and does not impact total equity.
- Other disposals in the year generated proceeds, net of costs, of **£7m** and generated a pre tax profit of **£1m**.

The carrying value of assets and liabilities disposed of were as follows:

	£m
Property and equipment	92
Reinsurers' share of insurance contract liabilities	27
Other assets	6
Cash and cash equivalents	57
Insurance contract liabilities	(49)
Other liabilities	(7)
Net assets	126
Cumulative translation differences	(19)
Profit on disposal	18
Proceeds deferred in respect of assets leased back	10
Total cash consideration	135

31. Cash generated from continuing operations

	2008 £m	2007 £m
Net profit for the year before tax on continuing operations	**759**	670
Adjustments for:		
Depreciation	**35**	32
Amortisation	**74**	56
Fair value losses/(gains) (including loss/(gain) on disposal) on property and equipment	**1**	(4)
Fair value gains (including gain on disposal) on investments	**(187)**	(159)
Fair value losses (including loss on disposal) on investment property	**95**	30
Impairment charge on available for sale financial assets	**61**	3
Share of loss from associates	**18**	–
(Profit)/loss on disposal of subsidiaries	**(18)**	22
Foreign exchange gain	**(152)**	(53)
Amortisation of available for sale investments	**(2)**	7
Other non cash movements	**368**	312
Changes in operating assets/liabilities:		
Movement in technical provisions		
Unearned premiums	**104**	230
Losses and loss adjustment expenses	**(47)**	94
Movement in working capital	**(360)**	(624)
Movement in deferred acquisition costs	**(65)**	(61)
Reclassification of interest received	**(547)**	(489)
Cash generated from continuing operations	**137**	66

32. Related party transactions

The ultimate Parent Company of the Group is RSA Insurance Group plc which is incorporated in Great Britain and registered in England and Wales.

The following transactions were carried out with related parties:

Key management compensation

	2008 £m	2007 £m
Salaries and other short term employee benefits	**5**	4
Bonus awards	**4**	3
Pension benefits	**1**	1
Share based awards	**6**	4
Total	**16**	12

A number of the directors, other key managers, their close families and entities under their control have general insurance policies with subsidiary companies of the Group. Such policies are on normal commercial terms except that executive directors and key managers are entitled to special rates which are also available to other members of staff.

As at 31 December 2008, there was an interest free loan of **£5,000** (2007: £nil) outstanding to a member of the key management team under standard terms of the Group's UK Car Ownership Scheme, which is open to all UK managers within a qualifying salary band.

Investments in associates

In 2007 there was an amount owing to Intouch Insurance Group BV of £25m. This was included within liabilities in the balance sheet and was payable as a capital injection. There were no amounts outstanding as at 31 December 2008.

Notes to the financial statements continued

33. Commitments

Capital commitments

The Group's significant capital commitments in respect of property and equipment and intangible assets are detailed in the table below:

	2008 £m	2007 £m
Property and equipment	**5**	27
Intangible assets	**15**	18
Total	**20**	45

Financial instrument commitments

The Group has a number of guarantees and commitments.

Bank loan guarantees

In Canada, the Group guarantees outstanding loan repayments in the event of bank loan default by broker subsidiaries and special relationship brokers. The bank loan guarantees amount in total to **£11m** (2007: £8m) and have a term of up to 10 years. It is not anticipated that any of the brokers will default, and full recourse is available on any default.

Operating lease commitments

The Group leases various outlets and offices under non cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights.

Operating lease commitments where the Group is the lessee

The future aggregate minimum lease payments under non cancellable operating leases are as follows:

	Land and buildings		Other	
	2008 £m	2007 £m	2008 £m	2007 £m
One year or less	**65**	58	**2**	2
Between one and five years	**214**	192	**3**	2
After five years	**111**	134	**–**	–
	390	384	**5**	4
Recoveries under sub tenancies	**(58)**	(67)	**–**	–
Total	**332**	317	**5**	4

Operating lease commitments where the Group is the lessor

The future aggregate minimum lease payments under non cancellable operating leases are as follows:

	Land and buildings	
	2008 £m	2007 £m
One year or less	**27**	25
Between one and five years	**85**	83
After five years	**109**	125
Total	**221**	233

34. Discontinued operations and non current and disposal group assets and liabilities held for sale

Discontinued operations

Losses related to discontinued operations were **£nil** during 2008 (2007: £13m).

In 2006, the Group recognised the losses arising on the writedown of the carrying value of the US operation to fair value. The loss recognised in 2007 includes the cumulative amount of the exchange gains and losses deferred in equity relating to the disposal of the US operation and to the cumulative exchange gains and losses recorded on a US dollar denominated loan made by a UK subsidiary company to the US operation.

An analysis of the result of discontinued operations is as follows:

	2008 £m	2007 £m
Total income	–	26
Total expenses	–	(26)
Loss recognised on completion/writedown	–	(19)
Loss before tax of discontinued operations	–	(19)
Tax on loss on disposal and writedown	–	6
Loss for the year from discontinued operations	–	(13)

Non current and disposal group assets and liabilities held for sale

The Group has classified office property within the UK operating segment as a non current asset held for sale. The Group is actively marketing the property. No gain or loss has been recognised in the income statement since the reclassification.

In 2007, a UK subsidiary was classified as a disposal group and UK office property was classified as a non current asset held for sale. The sale of these assets has been completed during 2008. No impairment losses have been recognised in respect of these assets during 2008.

The analysis of the non current and disposal group assets and liabilities held for sale is as follows:

	2008 £m	2007 £m
Assets		
Property and equipment	**3**	13
Reinsurers' share of insurance contract liabilities	–	58
Insurance and reinsurance debtors	–	5
Cash and cash equivalents	–	32
Total assets	**3**	108
Liabilities		
Insurance contract liabilities	–	58
Insurance and reinsurance liabilities	–	5
Other liabilities	–	2
Total liabilities	–	65

Independent auditors' report to the members of RSA Insurance Group plc

We have audited the Parent Company financial statements of RSA Insurance Group plc for the year ended 31 December 2008 which comprise the Parent Company balance sheet, statement of changes in equity of the Parent Company, Parent Company cashflow statement and the related notes 1 to 10. These Parent Company financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the Group financial statements of RSA Insurance Group plc for the year ended 31 December 2008 and on the information in the remuneration report that is described as having been audited.

This report is made solely to the Parent Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Parent Company's members 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 Parent Company and the Parent 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 auditors

The directors' responsibilities for preparing the Annual Report and the Parent Company financial statements in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union are set out in the directors' report.

Our responsibility is to audit the Parent Company financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the Parent Company financial statements give a true and fair view and whether the Parent Company financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the directors' report is consistent with the Parent Company financial statements. The information given in the directors' report includes that specific information presented in the financial review, the Group CEO's business review, the regional business reviews and in the estimation techniques, risks, uncertainties and contingencies that is cross referred from the business review section of the directors' report.

In addition we report to you if, in our opinion, the Parent 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 other transactions is not disclosed.

We read the other information contained in the Annual Report as described in the contents section and consider whether it is consistent with the audited Parent Company financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Parent Company financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Parent Company financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the Parent Company financial statements, and of whether the accounting policies are appropriate to the Parent 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 Parent Company 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 Parent Company financial statements.

Opinion

In our opinion:

- The Parent Company financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the Parent Company's affairs as at 31 December 2008
- The Parent Company financial statements have been properly prepared in accordance with the Companies Act 1985
- The information given in the directors' report is consistent with the Parent Company financial statements.

Deloitte LLP

Chartered Accountants and Registered Auditors
London, UK
25 February 2009

Parent Company balance sheet

as at 31 December 2008

	Notes	2008 £m	2007 £m
Assets			
Fixtures and fittings		**4**	2
Investments	2	**4,824**	5,587
Amounts owed by subsidiaries	9	**1,961**	1,273
Current tax assets	6	**4**	26
Deferred tax assets	6	**25**	21
Other debtors and other assets	3	**2**	4
		1,992	1,324
Cash and cash equivalents		**4**	1
Total assets		**6,824**	6,914
Equity, reserves and liabilities			
Equity and reserves			
Share capital	4	**1,040**	1,020
Reserves		**3,277**	3,976
Retained earnings		**684**	422
Total equity and reserves		**5,001**	5,418
Liabilities			
Amounts owed to subsidiaries	9	**436**	232
Loan capital	5	**1,311**	1,194
Current tax liabilities		**5**	–
Accruals and other liabilities		**71**	70
Total liabilities		**1,823**	1,496
Total equity, reserves and liabilities		**6,824**	6,914

The attached notes form an integral part of these separate financial statements.

The separate financial statements were approved on 25 February 2009 by the Board of Directors and are signed on its behalf by:

George Culmer
Chief Financial Officer

Statement of changes in equity of the Parent Company

for the year ended 31 December 2008

Changes in equity for the year ended 31 December 2008

	Ordinary share capital £m	Ordinary share premium £m	Preference shares £m	Revaluation reserves £m	Capital redemption reserve £m	Retained earnings £m	Total equity £m
Balance at 1 January	**895**	**943**	**125**	**3,025**	**8**	**422**	**5,418**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**483**	**483**
Dividends – paid (note 7)	**–**	**–**	**–**	**–**	**–**	**(246)**	**(246)**
Issued by scrip	**14**	**51**	**–**	**–**	**–**	**–**	**65**
Issued for cash	**6**	**13**	**–**	**–**	**–**	**–**	**19**
Share options	**–**	**–**	**–**	**–**	**–**	**25**	**25**
Fair value losses net of tax	**–**	**–**	**–**	**(763)**	**–**	**–**	**(763)**
Balance at 31 December	**915**	**1,007**	**125**	**2,262**	**8**	**684**	**5,001**

Changes in equity for the year ended 31 December 2007

	Ordinary share capital £m	Ordinary share premium £m	Preference shares £m	Revaluation reserves £m	Capital redemption reserve £m	Retained earnings £m	Total equity £m
Balance at 1 January	821	857	125	3,225	8	288	5,324
Profit for the year	–	–	–	–	–	82	82
Dividends – paid (note 7)	–	–	–	–	–	(211)	(211)
Issued by scrip	19	81	–	–	–	–	100
Issued for cash	55	5	–	–	–	244	304
Share options	–	–	–	–	–	19	19
Fair value gains net of tax	–	–	–	(200)	–	–	(200)
Balance at 31 December	895	943	125	3,025	8	422	5,418

The attached notes form an integral part of these separate financial statements.

Parent Company cashflow statement

for the year ended 31 December 2008

	Note	2008 £m	2007 £m
Cash generated from operations	8	**(87)**	70
Purchase of fixtures and fittings		**(2)**	–
Net movement in amounts owed to/by subsidiaries		**254**	(239)
Net cashflows from investing activities		**252**	(239)
Proceeds from issue of share capital		**19**	304
Dividends paid		**(181)**	(111)
Repayment of long term borrowings		**–**	(25)
Net cashflows from financing activities		**(162)**	168
Net increase/(decrease) in cash and cash equivalents		**3**	(1)
Cash and cash equivalents at beginning of the year		**1**	2
Cash and cash equivalents at end of the year		**4**	1

The attached notes form an integral part of these separate financial statements.

Notes to the separate financial statements

1. Significant accounting policies

RSA Insurance Group plc, domiciled in the United Kingdom is the ultimate Parent Company ('the Company') of the RSA group of companies. The principal activity of the Company is to hold investments in its subsidiaries and the receipt and payment of dividends.

These separate financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

Except where otherwise stated, all figures included in the separate financial statements are presented in millions of Pounds Sterling ('Sterling'), shown as £m, rounded to the nearest million.

In accordance with section 230 of Companies Act 1985, the Company's income statement and related notes have not been presented in these separate financial statements.

The accounting policies that are used in preparation of these separate financial statements are consistent with the accounting policies used in preparation of the consolidated financial statements of RSA Insurance Group plc as set out in those financial statements.

The additional accounting policies that are specific to the separate financial statements of the Company are set out below.

Investment in subsidiaries

The Company accounts for its investments in directly owned subsidiaries as available for sale financial assets, which are included in the accounts at fair value.

Changes in the fair value of the investments in subsidiaries are recognised directly in equity in the statement of changes in equity. Where there is a decline in the fair value of a directly owned subsidiary below cost, and there is objective evidence that the investment is impaired, the cumulative loss that has been recognised in equity is removed from equity and recognised in the income statement.

Dividend income

Dividend income from investments in subsidiaries is recognised when the right to receive payment is established.

2. Investments

	2008 £m	2007 £m
Investments at 1 January – at valuation	**5,587**	5,811
Disposals during the year	**–**	(24)
Fair value adjustments	**(763)**	(200)
Investments at 31 December – at valuation	**4,824**	5,587

The balance at 31 December comprises:

	2008 £m	2007 £m
Investment in subsidiaries	**4,445**	5,208
Loans to subsidiaries	**379**	379
	4,824	5,587

The investments in subsidiaries are recognised in the balance sheet at fair value measured in accordance with the Company's accounting policies. Fair value of the Company's significant subsidiary is determined by reference to the market value (derived from relevant indices) of the Company's ordinary shares and loan capital instruments at the balance sheet date, being the most transparent independent available indicator. The market value is adjusted for the fair value of the Company's preference shares, assets and liabilities, excluding directly owned subsidiaries. The adjusting items have been fair valued by determining the present value of future cashflow projections, using an appropriate arms length discount rate. The remaining subsidiaries are held at fair value which has been determined to be net asset value.

The directors believe that the methodology used supports the inclusion of the investments in subsidiaries on the balance sheet, at the fair values ascribed to them. The market value of the Company's ordinary shares at 31 December 2008 was **138.10p**. A movement of 1% in the share price would have an impact of **£46m** on the fair value.

Full details of the principal subsidiaries of the Company are set out in note 29 to the consolidated financial statements.

3. Other debtors and other assets – to be settled within 12 months

	2008 £m	2007 £m
Other prepayments and accrued income	1	2
Other debtors	1	2
Total other debtors and other assets	**2**	4

4. Share capital

Full details of the share capital of the Company are set out in note 18 to the consolidated financial statements.

5. Loan capital

Full details of the loan capital of the Company are set out in note 19 to the consolidated financial statements.

6. Current and deferred tax

Current tax

	Asset		Liability	
	2008 £m	2007 £m	2008 £m	2007 £m
To be settled within 12 months	4	26	–	–
To be settled after 12 months	–	–	5	–
	4	26	5	–

Deferred tax assets

The following are the major deferred tax assets recognised by the Company and movements during the year:

	Other temporary differences £m	Reclassification of bonds £m	Accelerated capital allowances £m	Total £m
Deferred tax assets at 1 January 2007	5	22	1	28
Change of rate in deferred tax	–	(2)	–	(2)
Charge to equity for the year	–	(2)	–	(2)
Charge to income for the year	(3)	–	–	(3)
Deferred tax assets at 31 December 2007	2	18	1	21
Charge to equity for the year	–	**(2)**	–	**(2)**
Credit to income for the year	**5**	–	**1**	**6**
Deferred tax assets at 31 December 2008	**7**	**16**	**2**	**25**

At the balance sheet date, the Company has unused tax losses of **£7m** (2007: £7m) available for offset against future profits. No deferred tax asset has been recognised in respect of the tax losses of **£7m** (2007: £7m) due to the unpredictability of future profit streams. The losses may be carried forward indefinitely.

The aggregate current tax relating to items that are credited to equity is **£2m** (2007: £4m).

7. Dividends

Full details of the dividends paid and proposed by the Company are set out in note 7 to the consolidated financial statements.

8. Cash generated from operations

	2008 £m	2007 £m
Net profit for the year before tax	**480**	63
Realised losses	–	21
Foreign exchange loss	**46**	20
Dividends received	**(600)**	–
Changes in operating assets/liabilities	**(13)**	(34)
Cash generated from operations	**(87)**	70

Notes to the separate financial statements continued

9. Related party transactions

RSA Insurance Group plc (incorporated in Great Britain and registered in England and Wales) is the ultimate Parent Company of the RSA group of companies.

The following transactions were carried out with related parties:

Provision of services and benefits

RSA Insurance Group plc provides services and benefits to its subsidiary companies operating within the UK and overseas as follows:

- Provision of technical support in relation to risk management, information technology and reinsurance services. Services are charged for annually on a cost plus basis, allowing for a margin of **5%** (2007: 5%)
- Issue of share options and share awards to employees of subsidiaries. Costs are charged for annually based on the underlying value of the awards granted calculated in accordance with the guidance set out within IFRS 2.

Key management compensation

	2008 £m	2007 £m
Salaries and other short term employee benefits	**5**	4
Bonus awards	**4**	3
Pension benefits	**1**	1
Share based awards	**6**	4
Total	**16**	12

There are no employees with employment contracts with the Company. All employees are employed by subsidiary companies.

A number of the directors, other key managers, their close families and entities under their control have general insurance policies with subsidiary companies of the Group. Such policies are on normal commercial terms except that executive directors and key managers are entitled to special rates which are also available to other members of staff.

As at 31 December 2008, there was an interest free loan of **£5,000** (2007: £nil) outstanding to a member of the key management team under the standard terms of the Group's UK Car Ownership Scheme, which is open to all UK managers within a qualifying salary band.

Other transactions

Year end balances with related parties are set out below:

	2008 £m	2007 £m
Receivable from related parties:		
Receivable from subsidiaries, interest bearing loans	**1,595**	995
Receivable from subsidiaries, non interest bearing	**366**	278
Total receivable from related parties	**1,961**	1,273
Payable to related parties:		
Payable to subsidiaries, interest bearing loans	**345**	131
Payable to subsidiaries, non interest bearing	**91**	101
Total payable to related parties	**436**	232

Interest is charged on interest bearing loans, which are repayable on 24 hours written notice, at three months LIBOR plus 0.6%.

Additional loans to subsidiaries of **£379m** (2007: £379m) as disclosed within note 2 have been made. Of this, **£294m** (2007: £294m) and **£78m** (2007: £78m) are subordinated loans on which interest is charged at 8.5% and 6.701% respectively with the remaining loan balance interest free with no specified repayment date.

Royal & Sun Alliance Insurance plc (RSAI), a subsidiary of the Company, has provided guarantees to the Company's creditors for amounts arising from its loan capital agreements (as set out in note 19 to the consolidated financial statements) and for amounts arising from its committed credit facilities (as set out in note 22 to the consolidated financial statements). The guarantees relating to the loan capital agreements are subordinated to all other creditors of RSAI.

10. Share based payments

Full details of share based payment plans are provided in note 27 to the consolidated financial statements.

Shareholder information

Registered Office and Group Corporate Centre

9th Floor, One Plantation Place, 30 Fenchurch Street,
London EC3M 3BD. Telephone: +44 (0)20 7111 7000.
Registered in England and Wales No. 2339826.

Company website

The Annual Report and Accounts, Interim Management Statements, Half Year Report and other useful information about the Company, such as the current share price, is available on the website **www.rsagroup.com**. Frequently asked questions and answers in respect of shareholding matters are detailed on the Company's website.

Registrar

The Company's share register is maintained by Equiniti Limited. Queries regarding your shareholding should be addressed to Equiniti at the following address:

Equiniti Limited
Aspect House
Spencer Road
Lancing
West Sussex
BN99 6DA
Telephone: +44 (0)871 384 2048

Overseas callers should use +44 (0)121 415 7064.
Shareholders with a text phone facility should use
+44 (0)871 384 2255.

Please quote the company reference number 0059 and your shareholder account number (on your share certificate and dividend tax vouchers) when contacting or corresponding with Equiniti. (Calls are charged at 8p per minute from a BT landline. Other telephone provider costs may vary.)

Annual General Meeting

Ordinary shareholders are invited to attend the Company's Annual General Meeting (AGM), which will be held at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE at 11.00am on 18 May 2009. Ordinary shareholders who are unable to attend the AGM to ask a question in person are invited to send the Chairman an email via the Company's website or to write to the Chairman at the Registered Office address above.

Electronic communications

Following the adoption of electronic communication provisions into the Company's Articles of Association in May 2008, RSA now provides the majority of information to shareholders via the Company's website. Receiving the Company's communications electronically allows the Company to communicate with its shareholders in a more environmentally friendly, cost effective and timely manner. Shareholders are encouraged to elect to receive notifications of shareholder communications by registering with Shareview (**www.shareview.co.uk**).

Scrip Dividend Scheme

RSA offers shareholders the opportunity to use their dividends to buy more ordinary shares in the Company by participating in the Company's Scrip Dividend Scheme. The Scheme applies to both interim and final dividends and enables shareholders to increase their holding in the Company without incurring dealing costs or stamp duty. If you wish to receive a scrip dividend instead of a cash dividend for future dividends on which a scrip alternative is offered, please contact Equiniti.

Share ownership

RSA is listed on the London Stock Exchange under the code RSA. The average total daily trading volume during 2008 was approximately 18m ordinary shares. The opening market price of an ordinary share on 2 January 2008 was 148.5p and closing market price on 31 December 2008 was 138.1p. The highest daily closing price of an ordinary share was 165.8p on 19 September 2008 and lowest daily closing price was 116.3p on 20 October 2008. Further details of the ordinary and preference shares are found in note 18 on pages 103 to 104.

Shareholdings by size

No of shares	Shareholders	%	Shares	%
1 – 24,999	46,039	96.88	108.6m	3.26
25,000 – 99,999	675	1.42	31.2m	0.94
100,000 – 499,999	335	0.70	80.2m	2.41
500,000 – 999,999	164	0.35	116.8m	3.51
1,000,000 – 1,999,999	104	0.22	142.6m	4.28
2,000,000 and above	205	0.43	2,850.0m	85.60
Total	**47,522**	**100.00**	**3,329.4m**	**100.00**

Distribution of shares by geography

65%	UK
13%	EUROPE
13%	USA & CANADA
9%	ASIA & OTHERS

Analysis of investors

19%	PENSION FUNDS
13%	INSURANCE
43%	UNIT TRUSTS/ MUTUAL FUNDS
11%	PRIVATE/RETAIL
14%	OTHERS

Shareholder information continued

Managing your shareholding

Share register fraud: protecting your investment

It is required by law that our shareholder register is available for public inspection and we are unable to control the use of information obtained by persons inspecting the register. Please treat any approaches purporting to originate from RSA with caution. RSA will never contact its shareholders directly to provide recommendation or advice regarding your shareholding and neither does it appoint third parties to do so.

Tips on protecting your shares

- Keep any documentation that contains your shareholder reference number in a safe place and destroy any documentation which you no longer need by shredding it
- Inform Equiniti promptly when you change your address
- Be aware of dividend payment dates and contact the registrars if you do not receive your dividend cheque, or better still, make arrangements to have the dividend paid directly into your bank account and
- Consider holding your shares electronically in a CREST account via a nominee.

Amalgamation of accounts

Shareholders who receive duplicate sets of Company mailings owing to multiple accounts in their name should write to Equiniti to request that their account be amalgamated.

Low cost share dealing facilities

A telephone and internet dealing service is available through Equiniti which provides a simple way of buying and selling RSA shares. Commission is 1.5% with a minimum charge of £25 for telephone dealing and 1% with a minimum charge of £20 for internet dealing. For telephone sales call +44 (0)845 6037 037 between 8.30am and 4.30pm, Monday to Friday, and for internet sales log on to **www.shareview.co.uk/dealing**. You will need your shareholder reference number as shown on your share certificate. Share dealing services are also widely provided by other organisations.

ShareGift

Shareholders with a small number of shares, the value of which makes it uneconomic to sell them, may wish to consider donating them to charity through ShareGift, a registered charity administered by The Orr Mackintosh Foundation, registered charity number 1052686.
The relevant share transfer form can be obtained from Equiniti.
Further details can be obtained from **www.sharegift.org** or by calling +44 (0)20 7930 3737.

Capital gains tax

The market value at 31 March 1982 of each post consolidation ordinary share of 27.5p in the Company, for capital gains tax purposes after relevant adjustments, was 146.41p (25p shares 133.1p) for former Royal Insurance shareholders and 57.97p (25p shares 52.7p) for former Sun Alliance shareholders. An adjustment to tax cost is required to take account of the 2003 rights issue, according to whether the rights were taken up or sold. Similarly, for former Royal Insurance shareholders an adjustment to tax cost is required to take account of the 1993 rights issue, according to whether the rights were taken up or sold.

Disabled shareholders

RSA is committed to providing a quality service to all of its shareholders. An induction loop is installed at the AGM venue. Please contact the Company Secretary's department at the registered office, detailed on page 131, if you require particular assistance.

Financial calendar

26 February 2009
Announcement of the full year results for 2008, the ordinary final dividend for 2008 and the first preference dividend for 2009

4 March 2009
Ex dividend date for the ordinary final dividend for 2008 and the first preference dividend for 2009

6 March 2009
Record date for the ordinary final dividend for 2008 and the first preference dividend for 2009

12 March 2009
Announcement of the scrip dividend price for the ordinary final dividend for 2008

1 April 2009
Payment date for the first preference dividend for 2009

7 May 2009
Deadline for the receipt of scrip dividend mandates by Equiniti in relation to the ordinary final dividend for 2008

18 May 2009
Annual General Meeting

5 June 2009
Payment date for the ordinary final dividend for 2008 (subject to shareholder approval at the AGM)

6 August 2009*
Announcement of the half year results for the six months ended 30 June 2009, the ordinary interim dividend for 2009 and the second preference dividend for 2009

12 August 2009*
Ex dividend date for the ordinary interim dividend for 2009 and the second preference dividend for 2009

14 August 2009*
Record date for the ordinary interim dividend for 2009 and the second preference dividend for 2009

20 August 2009*
Announcement of the scrip dividend price for the ordinary interim dividend for 2009

1 October 2009*
Payment date for the second preference dividend for 2009

30 October 2009*
Deadline for the receipt of scrip dividend mandates by Equiniti in relation to the ordinary interim dividend for 2009

27 November 2009*
Payment of the ordinary interim dividend for 2009

* provisional date

Important disclaimer
This document contains 'forward looking statements' (as defined in the US Private Securities Litigation Reform Act of 1995) with respect to certain of the Company's plans and its current goals and expectations relating to its future financial condition, performance and results. These statements are often, but not always, made through use of words or phrases such as 'will likely result', 'are expected to', 'will continue', 'believe', 'is anticipated', 'intends', 'plans', 'seeks', 'protection', 'outlook', and 'aims'. By their nature, all forward looking statements involve risk and uncertainty because they relate to future events and circumstances which are beyond the Company's control, including amongst other things, UK domestic and global economic business conditions, market related risks such as fluctuations in interest rates and exchange rates, the policies and actions of regulatory authorities (including changes related to capital and solvency requirements), the impact of competition, inflation, deflation, the timing impact and other uncertainties of future acquisitions or combinations within relevant industries, as well as the impact of tax and other legislation and other regulations in the jurisdictions in which the Company and its affiliates operate. As a result, the Company's actual future financial condition, performance and results may differ materially from the plans, goals and expectations set forth in the Company's forward looking statements. The Company undertakes no obligation to update any forward looking statements save in respect of any requirement under applicable law or regulation.

www.rsagroup.com

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