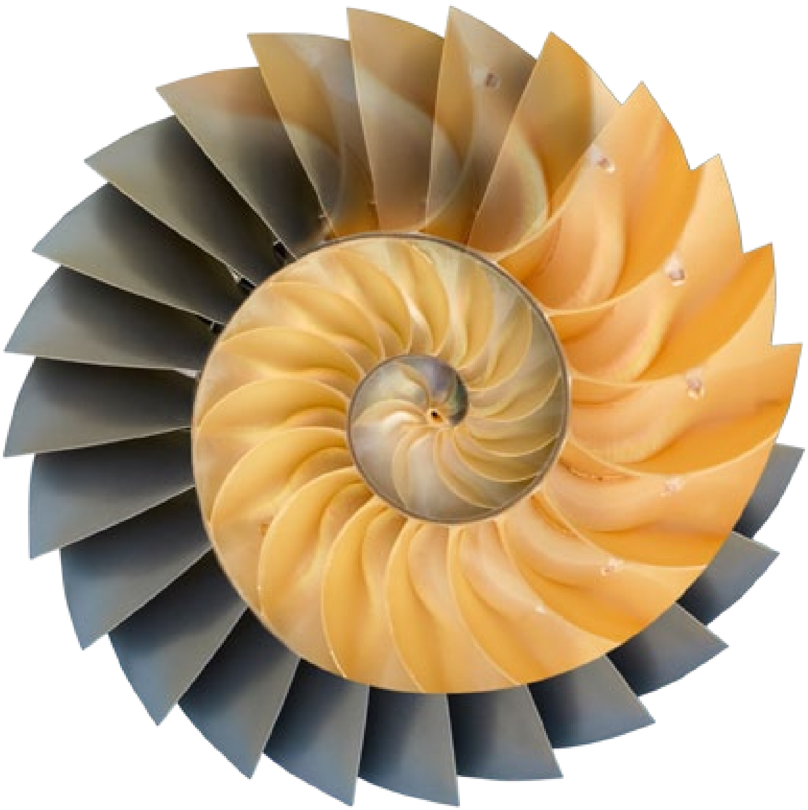
CONSTANT EVOLUTION CAREFUL INNOVATION

ANNUAL REPORT 2012



CONTENTS

Pages 8 to 52 (excluding 11, 18, 22 and 23) represent a complete reproduction of the annual report and financial statements of the Company. All other pages did not form part of these financial statements and consequently represent unaudited information.

GWP

+26%

Our underwriting expertise and ability to identify and meet market needs helped us achieve strong growth.

NET ASSETS

$706m

Following our tenth consecutive profitable year, our capital and surplus base increased again.

PROFITS

+43%

Despite competitive markets, our careful investments and market selection generated strong returns.

THE SIX YEAR RECORD

GWP (in $000)

LEADING THE MARKET

INTERNATIONAL

Having started to offer Terrorism and War cover back in 2010, our Dubai office has now evolved into a market leader. In fact when BBC Worldwide was looking for an expert to talk about the subject, they chose Elie Bouchaaya, Senior Vice-President and General Manager of Liberty Middle East to interview on screen at length. “Because we were up and running before the Arab Spring, we had the experience and capacity in place when demand arose”, explains Elie, who goes on to comment on how the market has changed. “In countries like Lebanon and Jordan, the focus was on insurance against Terrorism and War. But businesses are now also seeking to protect themselves from damage caused by civil commotion, strikes, riots and malicious damage. We can offer the whole package.”

Meeting growing demand in the Middle East and North Africa

How do they manage the risks? A combination of country-by-country knowledge, local underwriting expertise and the ability to draw on Liberty’s global specialty skills ensures that risks can be carefully assessed, monitored and selected. As a result of rising demand, Event Cancellation was added to the range of products on offer in 2012 and more innovative lines may also come on board with further growth in the region.

BROAD RANGE, SPECIALIST EXPERTISE

Our products are built on proven underwriting ability and extensive sector knowledge.

AVIATION

We provide aviation cover to clients worldwide with a focus on medium-sized airlines including start-up operations and general aviation (fixed wing and rotor wing). Other specialist areas include 'total loss only' and non-critical products liability cover.

CASUALTY/GENERAL LIABILITY

An extensive range of liability products is offered to commercial clients in construction, manufacturing, leisure, motorsport, transportation, film and TV production. These include both primary and excess public and product liability and employers' liability.

COMMERCIAL PROPERTY

Our specialist team has an in-depth understanding and many years of industry experience. Focusing on material damage and business interruption cover, they offer a full-service proposition that combines underwriting, risk engineering and claims expertise.

CONSTRUCTION

Our team of expert construction engineers and underwriters combine technical understanding with significant underwriting experience and market-leading capacity to deliver risk transfer solutions for energy, process and heavy industries, as well as for building, infrastructure and civil engineering projects.

CRISIS MANAGEMENT

We help clients to avoid or, if necessary, manage a major crisis and mitigate the risk of product contamination and product recall for food and non-food sector events. Our kidnap and ransom cover provides governments, international corporations and private individuals around the world with prevention, training and response services.

DIRECTORS & OFFICERS

Both brokers and clients benefit from our first-class service. Areas covered include directors' & officers' liability, pension trustee liability, employment practice liability, commercial crime, and public offering of securities insurance.

ENERGY/POWER GENERATION

We offer an innovative, flexible service closely geared to the needs of the energy sector including onshore, offshore operational and construction, heavy industries and power generation. Our clients benefit from cross-class products and bespoke policy cover from our underwriting, risk engineering and claims teams.

ENVIRONMENTAL

With gaps in pollution cover becoming increasingly apparent under many traditional liability policies, our highly experienced team underwrites a wide range of environmental exposures. Our products provide broad and comprehensive coverage for pollution liability and environmental damage liability.

Chief Underwriting Officers *left to right*: Richard Pursey, Alan Telford, Mike Gosselin, Richard Coxon, Nick Mortimer

EVENT CANCELLATION

Through our operation in Dubai we provide Event Cancellation insurance aimed at event organisers and promoters in the MENA region. Cover includes cancellation, abandonment or postponement of sporting events, trade shows and conferences, as well as non-appearance of key speakers.

FINANCIAL INSTITUTIONS

As a leading insurer in this sector, we offer tailor-made cover for financial institutions. Products include: blanket bonds for banking organisations; specialist coverage for crime, including electronic and computer crime; and professional indemnity for all types of financial institutions.

MARINE

Our specialists cover ocean cargo, project cargo with delay in start-up, marine liabilities, hull and shipbuilders' risks products. We provide tailored risk solutions, capacity and service to our clients through our network of global marine professionals, claims and risk engineering services.

MERGERS AND ACQUISITIONS (M&A)

For companies engaged in buying or selling a business, we can offer Warranty and Indemnity and Litigation Buy-Out insurance to facilitate the transaction by covering some of its potential risks.

PROFESSIONAL INDEMNITY

Our market-leading underwriters can arrange cover on a primary or excess basis for both traditional and emerging professions. These include accountants, architects, brokers, designers, estate agents, property managers, solicitors and independent financial advisers.

STRATEGIC ASSETS

Modern businesses are increasingly dependent on intangible assets and non-physical perils. Our highly experienced team offers innovative, flexible solutions in areas such as cyber and privacy protection, intellectual property, reputation and non-damage business interruption.

SURETY

We provide surety bonds and guarantees predominantly for large quoted or large privately-owned organisations. We specialise in serving the construction, engineering, manufacturing, electronics, defence, shipbuilding, oil and gas, transportation and retail industries.

TERRORISM

Liberty offers an extensive range of war and terrorism cover on a regional and global basis. Key products include: terrorism and sabotage; riots, strikes and civil commotion; malicious damage; insurrection, rebellion, revolution, mutiny and coup d'état; war on land and civil war.

TRADE CREDIT/POLITICAL RISK

We insure trade credit and political risks in emerging markets. Our focus is on insurance against default by individual buyers or suppliers. We also protect against the non-honouring of letters of credit and cover pre-shipment risk, currency inconvertibility, expropriation, and unfair bond calling.

HANDS-ON EXPERIENCE

EUROPE

Liberty Mutual Insurance Europe (LMIE) is leveraging its strength in complex risk areas such as energy, power and heavy industries to build local expertise in continental Europe. "Our specialist casualty lines have been supplemented in Paris and Madrid by investment in first-party lines, enabling us to meet the needs of new and existing brokers and insureds", explains Mike Gosselin. He believes the key has been People and Strategy. "We have put experienced local underwriting and risk engineering talent in place, enabling us to add value and quickly build a strong, differentiated position in the market", Mike adds. This requires a deep understanding of the industries customers operate in, as well as team working that sees underwriters, risk engineers and claims functions combining to deliver outstanding service.

Bringing market-leading specialty expertise to regional markets

"These are markets that can't be served by sitting behind a desk. Businesses are looking for insurers who can build strong relationships by understanding their individual risks and engaging in intelligent dialogue", says Mike. The results demonstrate that the strategy is effective, with revenues rising in both Paris and Madrid offices during the year. The evolution does not stop there, with the potential to gradually increase the number of lines, including cyber and environmental products, and broaden distribution to more European branches.

GLOBAL DISTRIBUTION LOCAL KNOWLEDGE

As we strengthened our teams across all divisions to meet growing demand, revenues increased in every region in which we operate.

LONDON

HEAD OFFICE
LONDON MARKET

Acting as a gateway to the London market and the base for some of the most highly skilled insurance professionals in Europe, our head office offers a full range of specialty products and the flexibility required to meet the needs of our brokers. Our commitment to the London market means that we have the capacity and expertise to underwrite the most complex risks.

+11%

BUSINESS VOLUME

UK/IRELAND MID-MARKET

BIRMINGHAM | BRISTOL | CHELTENHAM | DUBLIN | GLASGOW | LEEDS | LONDON | MANCHESTER

Our investment in expanding our branch network, strengthening our underwriting capabilities and improving the quality and accessibility of our services means we are strongly positioned to support brokers and clients. We provide a wide range of commercial insurance products through independent and national brokers.

+33%

BUSINESS VOLUME

CONTINENTAL EUROPE

COLOGNE | THE HAGUE | HAMBURG | MADRID | MILAN | PARIS | ZURICH

Through independent brokers we offer a growing suite of insurance products in Europe's key strategic markets. Our customers are medium and large-sized companies operating in a wide range of industry sectors, who benefit from our technical expertise and deep understanding of their needs.

+13%

BUSINESS VOLUME

INTERNATIONAL

DUBAI | HONG KONG | MALAYSIA | SINGAPORE

Our extensive network gives local brokers and insurance companies the capacity to meet demand from some of the world's fastest growing markets. With experience of the local trading environment and a wide product offering, our highly qualified teams have the underwriting authority and expertise to meet customer needs in a variety of sectors.

+16%

BUSINESS VOLUME

PRESIDENT'S STATEMENT

Despite competitive market conditions our business performed strongly in 2012, with Gross Written Premium (GWP) up 26% to $931m and pre-tax profit rising 43% to $99m. Even without the positive impact of the specialty mobile communications insurance contract (see Directors' Report) on our profit and loss account during the reporting period, GWP growth still exceeded 15%. We were also able to reduce our combined ratio from 98.5% in 2011 to 96.2% in 2012.

This excellent performance was built on our careful investment in market sectors where we identified growth potential, and supported by both a conservative approach to risk and strong underwriting expertise. Evidence of our ability to carefully manage costs at the same time as investing in growth can be seen in the fact that, although GWP rose by more than a quarter, our expense base went up by only 9%.

Our strong capital base grew again and our net assets now stand at $706m, well above the levels of capital required to support our business. We maintained a conservative stance on the management of our investments, achieving overall returns in 2012 of 5.5%, compared to 4.0% in 2011. Current market conditions meant that real investment yield fell slightly to 3.2%, reflecting our continued focus on high-quality fixed interest stocks.

As a result of this strong overall financial performance, we are pleased to announce dividend payments totalling $51m this year (further details in the Directors' Report).

DIFFICULT MARKETS

Although there was no repeat of the high number of catastrophes and risk losses seen in the market during the previous reporting period, the impact of one major event, Hurricane Sandy, was significant. As we expected, market losses proved higher than initial industry forecasts, with liabilities set to exceed $25bn. Our exposure was limited and the necessary reserves have been put in place.

While action by the European Central Bank did a lot to ease market fears over economic fragility and sovereign debt default in the Eurozone, concern over FI liabilities continued to impact the market as banking sector uncertainties remain. Perhaps surprisingly, given the heightened risks, we have seen very little signs of any significant or sustained rate increases. We continue to carefully monitor the situation and remain well provisioned against any potential liabilities in this sector.

In terms of other specific markets, Aviation was notably competitive, with rates being forced down as new capacity joined the market. In contrast, rates increased in the UK Independent Financial Adviser (IFA) book and PowerGen also saw some hardening.

Going back to the broader market, the overall picture is one of oversupply in most sectors with more capacity looking to enter the market. This is keeping prices down and competition strong, making risk selection and careful underwriting essential to success.

“All our regions grew revenue during the year, helping us succeed in our strategy of adding diversification to our London specialty business.”

STRONG REGIONS

All our regions grew revenue during the year, helping us succeed in our strategy of adding diversification to our London specialty business, which now accounts for less than half our revenues, compared to three-quarters five years ago. We strengthened our continental Europe operations, opening a new office in Milan and seeing our recently formed Madrid Energy team perform well. Our core Paris operations went from strength to strength as their broad product offering attracted good demand, helping Europe-wide revenues to rise by 13.4%. While many of our current European markets are well established and mature, we have been increasing our focus on growing Eastern Europe, working alongside Liberty’s local operations to better access the Russian, Polish and Czech markets where we believe there is significant appetite for our specialty products.

In our International region, servicing the Far East, Middle East and North Africa, GWP rose 16% as our Oil & Gas offering continued to be well received by the broker community and we launched our terrorism product line in the region. New underwriting expertise was put in place during the year and we remain well positioned for growth, particularly as the Construction market picks up.

A GROWING CORPORATE MID-MARKET

Our mid-market corporate activity grew strongly, with GWP up 33% as the investments we put in place during 2011 paid off. We opened our Leeds office during 2012, which quickly established a presence in the market with brokers and insureds being particularly impressed with the online claims reporting capability. Foundations have already been laid for the opening of a Glasgow office in 2013, which will add further distribution opportunities for our products and services.

The launch of our online mid-market Casualty platform during 2012 demonstrated our commitment to service enhancements for the corporate sector and we are well on our way to the completion of the Property and Combined platform. These provide added consistency and efficiency to the underwriting process while allowing management to increase visibility and control over operations. Our Property lines performed notably well this year, with strong growth and low liabilities despite 2012 being one of the wettest years on record for the UK.

While we expect our investments in this sector to continue to drive growth, it is unlikely to be at the rapid rate seen over the last two years as we are now a larger, more established player in what remains a competitive market.

INNOVATION IN SPECIALTY

Our London-based specialty business, which serves customers around the world, also achieved good growth. GWP rose 11% with all specialty lines (excluding Aviation) increasing revenue. In Aviation, despite highly competitive markets and management turnaround, we were able to defend our position and attract well-known market names with a good reputation for leading business, leaving us well positioned for future growth.

A new Heavy Industries unit was established and has already demonstrated its ability to win business. Newer lines such as Strategic Assets and Marine gained good traction and we continue to benefit from an innovative approach that puts us at the cutting edge of the market in growing areas such as Cyber Protection and Product Recall.

And late in the year we were provided an opportunity to offer capacity to the specialty casualty operations of Dual, the world’s largest

“This excellent performance was built on our careful investment in market sectors where we identified growth potential, and supported by both a conservative approach to risk and strong underwriting expertise.”

specialist underwriting agency, which after careful investigation we agreed to pursue. We expect that this will be a major driver of growth in our business in 2013.

STAFF AND SPONSORSHIP

Liberty Mutual Insurance Europe (LMIE) is committed to developing the talents of our employees so that they can fulfil their potential and, by doing so, help the company to succeed in the future. Courses aimed at building middle-management skills were well received during the year and will be extended in 2013.

We also backed the development of sporting talent, most notably through our commitment to four UK athletes during 2012. These included Luke Campbell, who won a boxing gold medal, and Paralympian discus thrower Dan Greaves, who achieved silver at London 2012. We continued to back up-and-coming racing drivers and were pleased to see one of our sponsored drivers take a big step forward by being picked to join a leading Formula 1 team.

This year saw us build on our support for the community local to our London head office. As part of the ‘Serve with Liberty’ initiative launched in 2012, staff were encouraged to give their time to valuable causes. The year saw them work on a number of local projects including volunteering at the Tower Hamlets Foodbank, gardening for INUF (a user-led mental health charity), and helping children at a local school to improve their literacy and numeracy skills.

Our commitment to innovation was further demonstrated by our sponsorship of the Insurance Times 2012 “International Broker Innovation of the Year Award”.

DIRECTION AND CONTROL

I am pleased to welcome three new appointments to the Board, John McCammon, our Chief Operating Officer, and, in non-executive capacities, Chris Peirce and Frank Robinson, respectively President and Chief Financial Officer of Liberty Mutual’s Global Specialty business unit. With their diverse skills, experience and background, we are confident they will make significant contributions to the future success of the company.

OUTLOOK

Market conditions are expected to remain similarly challenging in 2013, with oversupply keeping competition high and pricing low. LMIE has, however, already demonstrated an ability to grow in such markets through broadening our product range and distribution, while carefully focusing our investments on those areas that we consider have potential for growth. The success of this strategy over past years gives us confidence that, while maintaining our cautious attitude towards risk, we can still continue to grow our business in 2013. This, of course, would not be possible without the efforts of our management and staff, and I would like to thank them all for their hard work during 2012.

S P ROCKS, DIRECTOR – PRESIDENT AND MANAGING DIRECTOR | 27 MARCH 2013

Liberty Mutual Insurance Europe Limited

PROTECTING INTANGIBLE ASSETS

LONDON SPECIALTY

"It is estimated that three-quarters of the value of most mid-sized enterprises derives from intangible assets such as intellectual property and reputation", explains Matthew Hogg, Vice President, Strategic Assets. "Businesses are also operating in an economic environment that is increasingly subject to non-physical perils. With the reliance upon IT networks and outsourced business processes, the need for companies to protect themselves from damage, whether through malicious attacks or otherwise is clear", he adds. Joining LMIE in 2010 to establish the Strategic Assets division, Matthew brought a combination of legal, technology and insurance expertise to bear on what is a highly complex area. But he believes that the 'old-fashioned' values of efficient service and strong relationships are also vital to supporting brokers and insureds. Considerable resources are devoted to understanding client needs on an individual basis, and to ensuring that the team is always up to date with new and emerging areas of technology, regulation and law.

Developing new products and services for the digital age

Early entry into the market has enabled LMIE to establish a strong position, and as demand has grown, so has the Strategic Assets team. Now a full suite of Cyber, IP, Reputation and Non-Physical Damage Business Interruption lines are available, with many of these distributed globally through LMIE's UK mid-market Corporate, Continental Europe and International branches. Looking ahead, Matthew believes that the European Commission proposals to reform its Data Protection Directive may be a major driver of growth, as will businesses' increasing awareness of IP and cyber-related losses.

Executive Directors. *Left to right*: John McCammon, Sean Rocks (President LMIE), David Prince

DIRECTORS' REPORT

Increasing our presence in the UK mid-market and Continental Europe

The directors have pleasure in submitting their report, together with the audited financial statements of the company, for the year ended 31 December 2012.

PRINCIPAL ACTIVITY AND REVIEW OF THE BUSINESS

The company underwrites marine, non-marine and aviation insurance and reinsurance business from its head office in London and its branches across Europe, the Middle East and Asia.

The company's principal business lines are Casualty, Specialty Casualty, Aviation, Property, Trade Credit, Surety and Marine, Energy and Engineering. Company strategy continues to be to offer a diverse and growing range of specialty and commercial insurance products to markets in Europe, the Middle East and the Far East.

During 2012, the company continued to focus on extending its geographical presence in the UK mid-market corporate sector, and in addition opened a branch in Italy in order to enhance its presence in Continental Europe. The mobile communications business was expanded significantly, particularly in France, and in the final quarter LMIE expanded its offering of Specialty Casualty business, both geographically and by business sector, providing capacity to a specialist underwriting agency.

The company's key financial performance indicators during the year were as follows:

	2012 $'000	2011 $'000	Change %
Gross written premiums	931,420	740,931	25.7
Profit before taxation	98,674	69,112	42.8
Net assets	705,573	700,147	0.8
Combined ratio	96.24%	98.5%	

The increase in the gross written premiums reflects organic growth across the business, including the impact of increasing volumes of business written through the mobile communications contracts.

Non-Executive Directors. *Left to right*: Daniel Forsythe (US), Gordon McBurney (US), Chris Peirce (US), Frank Robinson (US), Dr Jonathan Spencer, Malcolm McKenzie

The combined ratio is calculated as total technical charges excluding change in the equalisation provision over earned premiums, net of reinsurance. The combined ratio reflects a benefit taken from prior year claims overprovisions of 0.5% (2011: 2.1% benefit).

The reduction in combined ratio is largely attributable to a reduction in the expense ratio, attributable to the growth in net earned premium exceeding the growth in the company's expense base.

Investment income, excluding net gains and losses on the realisation of investments, was consistent with the previous year, driven by lower investment yields, but offset by higher invested asset values arising from strong operational cashflows. Total investment returns of 5.5% (2011: 4.0%) reflected further increases in the market value of the company's bond investments as market yields continued to decline.

The company made net realised gains on its investment portfolio of $29,700,000 (2011: gain of $6,430,000).

The company operates in international markets and recorded a net loss of $14,338,000 during 2012 (2011: gains of $2,613,000) on the translation of non-USD currencies into USD. In accordance with the company's accounting policies, a loss of $15,084,000 (2011: gain of $2,084,000), being that part of the total loss relating to the retranslation of the company's principal operating currencies GBP, Euro and USD, is reflected in the Statement of Total Recognised Gains and Losses, and not in the profit and loss account.

Net assets increased by $5,426,000, attributable to the profit for the year of $73,345,000, other recognised net losses of $16,919,000 for the year, and an interim dividend of $51,000,000 paid during the year. The directors do not recommend payment of a final dividend (2011: Nil).

PRINCIPAL RISKS AND UNCERTAINTIES

The Board sets risk appetite annually as part of the company's business planning process.

Risk management is currently undertaken on three levels:

- Risk ownership – risk owners identify risks and are responsible for establishing and maintaining appropriate controls over those risks.

- Risk control – exercised by the Risk Committee which is responsible for oversight of the operation of the risk management strategy; and by the Executive Committee, which is responsible for the management of risk in accordance with the risk appetites set by the Board. Measures of risk are monitored against risk appetite on a quarterly basis.The Risk Committee is assisted by the advisory and monitoring functions of Risk Management and Compliance. Risk Management defines and prescribes the financial and operational risk assessment processes for the business, maintains the risk registers, and undertakes regular reviews of these risks with the risk owners. Compliance advises on all areas of regulatory principles, rules and guidance, and undertakes monitoring activity on key areas of regulatory risk.

• Risk assurance – conducted by the Internal Audit function under the control and direction of the Audit Committee. Internal audit conducts a programme of audits covering all aspects of risk ownership and risk control.

The principal risks and uncertainties facing the company are considered below.

INSURANCE RISK

Insurance risk includes the risks that a policy will be written for too low a premium or will provide inappropriate cover (underwriting risk), that the frequency or severity of insured events will be higher than expected (claims risk), and that estimates of claims subsequently prove to be insufficient (reserving risk). The Board manages insurance risk by agreeing its appetite for these risks annually through the business plan, which sets out targets for volumes, pricing, line sizes and retention by class of business.

Risk appetite is updated as necessary on a quarterly basis to ensure that it remains relevant and reflective of the changing needs and capabilities of the company. External events or changing market conditions that lead to a strategic shift in, for example, the company's product mix and capacity, may also trigger a review of the quantitative or qualitative appetite.

In situations where the company delegates certain aspects of first line risk ownership to external parties, such as through the delegation of underwriting or claims handling authorities, the company has put in place additional controls to ensure that these are and will continue to be controlled and monitored with the same degree of rigour as is applied in the rest of the business.

The Executive Committee of the Board then monitors performance against the business plan monthly through the year. Reserve adequacy is monitored by the Reserving Committee which meets quarterly to establish and review the held reserves. A key element of this consideration is review of the quarterly report by the company's actuary, which includes the actuarial estimate of required reserves together with documentation supporting the material judgements and assumptions made in arriving at this estimate.

CREDIT RISK

The company's principal credit risk exposure is the risk of non-performance by one or more of the company's reinsurers.

A key part of the company's risk management strategy is the purchase of effective reinsurance across all lines. The company purchases both proportional and non-proportional reinsurance locally and through participation in Liberty Mutual Group global treaties. There are a limited number of reinsurers worldwide with the capacity or capability to participate in these global treaties. A consequence of this is a degree of concentration of exposure with the major reinsurers.

The company has established a Reinsurance Committee which approves all reinsurance treaties and assesses and is required to approve all new reinsurers before business is placed with them. Carriers must be A rated or better. Reinsurer exposure is reviewed quarterly. The company uses a default risk model to determine a need for specific provisions against reinsurer non-performance which are adjusted on a quarterly basis. Changes in the amount of the provisions are reflected in the profit and loss account.

MARKET RISK

Market risk is defined as the risk of loss to the company arising from fluctuations in the values of its assets, the amount of its liabilities, or the income from its assets. Sources of market risk for the company include movements in interest rates, equity values, and exchange rates. Such movements would potentially affect the value of the company's cash and investment portfolio and the income therefrom. The company underwrites insurance policies in several currencies and consequently has an exposure to retranslation gains and losses arising from the impact of changes in exchange rates on technical assets and liabilities denominated in foreign currencies.

The company has delegated management of its investment portfolio to Liberty Mutual Group Asset Management Inc, the specialist investment management arm of Liberty Mutual Group. The portfolio is managed in accordance with investment guidelines established on behalf of the company by the Investment Committee. These guidelines set out limits on asset quality, counterparty exposure, asset concentration, and geographical concentration, compliance with which, alongside investment performance, is monitored by the Committee on a quarterly basis.

The portfolio comprises a broad spread of investment grade instruments, including bonds issued by Eurozone sovereign states collectively known as the "PIIGS" states. Total value of exposure to PIIGS sovereign debt is less than $34m within an overall portfolio valued at in excess of $1.6bn. The performance of PIIGS bonds is currently subject to monthly review and reporting to the Executive Committee of the Board, and to formal review at a strategic level with the investment managers through the Investment Committee.

The company follows a policy of matching foreign currency denominated assets and liabilities so as to minimise the impact of exchange rate movements. Shareholder surplus is currently held in USD. Thus overall the company holds limited net assets in non USD currencies and consequently this restricts balance sheet exposures to exchange rate movements.

LIQUIDITY RISK

Liquidity risk is the risk of loss to the company arising from the company being insufficiently liquid to meet all cashflow commitments as and when they fall due. It is company policy that all funds are held in cash or in readily-marketable instruments.

This requirement is reflected in the investment guidelines. The duration of investment instruments is matched to the anticipated duration of liabilities to policyholders and the currency of investment instruments is matched to the currency of anticipated liabilities to policyholders. Shorter term needs are anticipated through a process of cashflow forecasting with the backing of a bank loan facility which can be drawn upon if needed to cover immediate requirements.

The directors believe that these actions provide assurance that the company will be able to continue to meet its obligations as and when they fall due. In making this assessment, the directors have fully considered the effect of current market conditions on asset values and asset marketability.

OPERATIONAL RISK

Operational risk is defined as the risk of loss to the company arising from inadequate or failed internal processes, people, and systems. The company manages operational risk through the three mechanisms of risk ownership, risk control and risk assurance described above.

Through recent and planned business developments, the company has experienced and expects to continue to experience growth in business volumes. The company's risk management framework is under constant review and development to ensure this growth is appropriately managed, with commensurate investment in people, systems and related reporting and monitoring processes.

FUTURE DEVELOPMENTS

The company intends to continue its strategy of geographical diversification in Continental Europe and in the UK Corporate Mid-Market, and to explore opportunities to enhance its product offering and presence in these markets as well as in the London Market and International operations.

DIRECTORS' INTERESTS

The directors of the company during the year and up to the date of signing the financial statements were:

S P Rocks	Chairman – President and Managing Director
J F McCammon	Director – Chief Operating Officer (Appointed 4 January 2013)
D R Oates	Director (Resigned 11 June 2012)
D J Prince	Director – Chief Financial Officer
D T N Forsythe (USA)	Non-Executive Director
G J McBurney (USA)	Non-Executive Director
J P Spencer	Non-Executive Director
M G McKenzie	Non-Executive Director
C L Peirce (USA)	Non-Executive Director (Appointed 7 January 2013)
F W Robinson (USA)	Non-Executive Director (Appointed 22 January 2013)

According to the Register of Directors' Interests, no director has any beneficial interest in the issued share capital of the company.

FIXED ASSETS

The changes in the company's fixed assets for the year are set out in Note 12.

DONATIONS

During the year the company made charitable donations of $12,349 (2011: $30,435) and made no political donations (2011: nil).

EMPLOYEES

During the year an average number of 480 (2011: 454) staff were employed. The total aggregate remuneration of employees amounted to $89.5m (2011: $83.4m).

The company operates a framework for employee information and consultation which complies with the requirements of the Information and Consultation of Employees Regulations 2004. The policy is principally operated through the company's intranet, in which employees are provided with regular information regarding the company's performance, and are encouraged to present suggestions and raise questions regarding the company's performance. In addition, periodic meetings are held with management. The company operates discretionary performance-related remuneration schemes which enable employees to share in the success of the company and to be rewarded for good service and incentivised for future performance. The company invests in staff training to develop the skills of employees to maximise the service levels provided to customers and business partners.

Full and fair consideration is given to the recruitment of disabled people and to the offering of proper training, career development and promotion opportunities for them. Every effort is made to retain, in suitable employment, any member of staff who becomes disabled whilst employed by the company. Where this is not possible, a permanent health insurance scheme is in place for those staff who are unable to return to suitable employment.

GOING CONCERN

The financial statements have been prepared on a going concern basis. In assessing whether the going concern basis is appropriate, the directors have considered the information contained in the financial statements, the company's latest business plan, and the company's current solvency calculations. The directors are satisfied that the company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

DISCLOSURE OF INFORMATION TO THE AUDITORS

So far as each person who was a director of the company at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with its report, of which the auditor is unaware. Having made enquiries of fellow directors of the company and the company's auditor, each director has taken all the steps that he/she is obliged to take as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information.

AUDITORS

Ernst & Young LLP are deemed to be reappointed in accordance with an elective resolution made under Section 485 of the Companies Act 2006. Consequently, the company has dispensed with the requirement to hold an Annual General Meeting and re-appoint the auditors. Ernst & Young LLP have expressed their willingness to continue in office and so have been invited to do so.

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

S P ROCKS, DIRECTOR – PRESIDENT AND MANAGING DIRECTOR | 27 MARCH 2013
COMPANY NUMBER: 1088268

Registered office and advisers

Directors
S P Rocks
J F McCammon
D J Prince
D T N Forsythe
G J McBurney
M G McKenzie
C L Peirce
F W Robinson
J P Spencer

Company Secretary
N J Davenport

Registered Office
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Company Number
1088268

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Independent Auditors
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London SE1 2AF

IMPROVING EFFICIENCY AND SERVICE

UK

Opening a new office in Leeds was just one example of our continued investment in the mid-market corporate sector during 2012. As well as broadening the regional distribution of product lines, we introduced new technology designed to further improve service to brokers and insureds.

Meeting the needs of corporate clients across the UK

“The new system increases our service levels by cutting the time it takes to issue quotes and policy wordings”, explains David Stein, Chief Operating Officer, Commercial. The platform went live for Casualty in 2012 and Commercial Combined and Property will follow in 2013. “As well as improving efficiency for customers, the system upgrade also improves management information and visibility across operations”, adds David.

In a highly competitive sector, differentiation is essential. Mark Stephenson, Head of Business Development and Market Relations (pictured), believes that the integrated approach “with risk management, underwriting, claims, actuaries and business development functions all based locally and working together” is key. It enables customers to benefit from local expertise and provides the capacity for LMIE to assess risks on an individual basis, adding value in a market that has become more commoditised. The strategy has been successful, with strong growth recorded in 2012, and LMIE continues to innovate in order to anticipate and meet the needs of the market.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those financial statements, the directors are required to:

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

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF LIBERTY MUTUAL INSURANCE EUROPE LIMITED

We have audited the financial statements of Liberty Mutual Insurance Europe Limited for the period ended 31 December 2012 which comprise the Profit and Loss Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet, and the related notes 1 to 32. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), having regard to the statutory requirement for insurance companies to maintain equalisation provisions. The nature of equalisation provisions, the amounts set aside at 31 December 2012, and the effect of the movement in those provisions during the year on shareholders' funds, the balance on the general business technical account, and profit before tax, are disclosed in note 30.

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

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

As explained more fully in the Directors' Responsibilities Statement set out on page 19, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report and Financial Statements to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OPINION ON FINANCIAL STATEMENTS

In our opinion the financial statements:

- Give a true and fair view of the state of the company's affairs as at 31 December 2012 and of its profit for the year then ended;
- Have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- Have been prepared in accordance with the requirements of the Companies Act 2006.

OPINION ON OTHER MATTER PRESCRIBED BY THE COMPANIES ACT 2006

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

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

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

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

Stuart Wilson (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP,
Statutory Auditor
London

28 March 2013

SUSTAINABLE THINKING RESPONSIBLE ACTION

As one of Liberty's key priorities is achieving sustainable growth, it is important that we carry out our activities in a way that reflects this long-term focus. That means conserving precious resources, acknowledging that we are part of a wider community and behaving responsibly in all our business activities.

We are committed to reducing waste in a number of ways. For example, in our London offices we use motion-sensitive lighting and virtual servers to ensure that energy use is minimised. In addition we not only recycle office paper and general material, we have also introduced measures to recycle printer toner, back-up tapes and computer hardware.

In the wider community, we contribute to a number of charities each year, both through direct donations and by supporting staff who are involved in fundraising.

SERVE WITH LIBERTY

As well as encouraging our staff to raise money, we also give them the opportunity to volunteer for valuable causes. We are a member of the Lloyd's Community Programme which aims to help build a stronger local community through projects in London's East End.

As part of the 'Serve with Liberty' initiative launched in 2012, staff can volunteer twice a year for such projects and undertake practical tasks such as tidying community gardens, painting internal areas of charity/community centres or sorting food and preparing food boxes. Recent projects have included working with INUF (a user-led mental health charity) at their headquarters in Newham to clear garden/internal areas, and with Tower Hamlets' Foodbank preparing food boxes for those in need.

Also through the Programme, a number of employees from Liberty's London office have been working with children from a local school in Whitechapel, helping them to get to grips with literacy and numbers.

These are just some of the ways in which sustainable thinking is benefiting our business, the environment and the wider community.

SPONSORSHIP

Our commitment to outstanding performance was reflected in Liberty Mutual Insurance Europe's support for four British athletes at London 2012. We are pleased to report that their hard work, talent and commitment were rewarded with two medals: Luke Campbell won a boxing Gold in the 56kg Bantamweight division, while Paralympian Dan Greaves secured a Silver medal in the F44 discus. In motor racing we continued to support up-and-coming drivers as they begin their careers in the sport as well as those who are more established.

Above, left to right:
Louisa Richards,
Jess Edwards,
Stephen Hill,
Amanda Chorley,
John McCammon,
Janet Dowdell,
Molly Edwards,
Jean-Pierre Wan,
Amanda Sellek,
Evie Dowdell

Luke Campbell

Dan Greaves

FINANCIAL STATEMENTS

for the year ended 31 December 2012

Profit and Loss Account

for the year ended 31 December 2012

Technical Account - General Business	NOTES	2012 $000	2011 $000
Gross premiums written	3	931,420	740,931
Outward reinsurance premiums		(472,403)	(341,138)
Net premiums written		459,017	399,793
Change in the unearned premium			
- gross amount	2	(54,117)	(60,474)
- reinsurers' share	2	33,005	28,307
- net amount	2	(21,112)	(32,167)
Earned premiums, net of reinsurance	2	437,905	367,626
Allocated investment return transferred from the non-technical account		70,353	51,426
Total Technical Income		**508,258**	**419,052**
Claims paid			
- gross amount		(362,199)	(196,124)
- reinsurers' share		189,781	72,863
- net of reinsurance		(172,418)	(123,261)
Change in the provision for claims			
- gross amount	28	(157,954)	(234,382)
- reinsurers' share	28	73,438	144,942
- net of reinsurance	28	(84,516)	(89,440)
Claims incurred net of reinsurance		(256,934)	(212,701)
Net operating expenses	4	(164,299)	(149,521)
Change in the equalisation provision	30	(8,680)	(7,871)
Total Technical Charges		(429,913)	(370,093)
Balance on the Technical Account for General Business		**78,345**	**48,959**

Profit and Loss Account
for the year ended 31 December 2012 *(continued)*

Non-technical Account	NOTES	2012 $000	2011 $000
Balance on the Technical account for General Business		**78,345**	**48,959**
Investment income and gains on realisation of investments	5	92,316	73,383
Investment expenses and charges	6	(2,380)	(2,333)
Foreign exchange gains		746	529
Allocated investment return transferred to the general business technical account		(70,353)	(51,426)
Profit on ordinary activities before tax	7	**98,674**	**69,112**
Tax on profit on ordinary activities	8	(25,329)	(21,121)
Profit on ordinary activities after tax	21	**73,345**	**47,991**

All the amounts above are in respect of continuing operations.

The notes on pages 28 to 52 form part of these financial statements.

Statement of Total Recognised Gains and Losses
for the year ended 31 December 2012

	NOTES	2012 $000	2011 $000
Profit on ordinary activities after tax	21	**73,345**	**47,991**
(Losses)/gains arising from the effect of retranslation of assets and liabilities denominated in GBP and Euro	21	(15,084)	2,084
Pension scheme – Actuarial (loss)/gain, net of tax	21	(1,835)	2,209
Total recognised gains relating to the year	22	**56,426**	**52,284**

The notes on pages 28 to 52 form part of these financial statements.

Balance Sheet as at 31 December 2012

ASSETS	Notes	2012 $000	2012 $000	2011 $000	2011 $000
Investments					
Investments in subsidiary undertakings	11	728		1,846	
Other financial investments	13	1,806,651		1,769,928	
Deposits with ceding undertakings		26,481		19,089	
			1,833,860		1,790,863
Reinsurers' share of technical provisions					
Provision for unearned premiums	2	240,754		202,374	
Claims outstanding	28	929,784		841,484	
			1,170,538		1,043,858
Debtors					
Debtors arising out of direct					
insurance operations	15	276,181		226,279	
Debtors arising out of					
reinsurance operations		64,528		38,174	
Other debtors	10	14,505		10,057	
			355,214		274,510
Other assets					
Tangible assets	12	3,385		3,556	
Cash at bank and in hand		82,657		61,302	
			86,042		64,858
Prepayments and accrued income					
Accrued interest		19,812		22,686	
Gross deferred acquisition costs	4	67,626		56,486	
Other prepayments	16	3,423		2,888	
			90,861		82,060
Total assets excluding pension assets			3,536,515		3,256,149
Pension asset	26		-		1,302
Total assets			**3,536,515**		**3,257,451**

The notes on pages 28 to 52 form part of these financial statements.

Balance Sheet as at 31 December 2012 *(continued)*

LIABILITIES	Notes	2012 $000	2012 $000	2011 $000	2011 $000
Capital and reserves					
Called up share capital	20	290,225		290,225	
Profit and loss account	21	415,348		409,922	
			705,373		700,147
Technical provisions					
Provision for unearned premiums	2	522,887		457,486	
Gross claims outstanding	28	1,987,904		1,798,001	
Equalisation provision	30	37,546		27,981	
			2,548,337		2,283,468
Creditors					
Creditors arising out of direct insurance operations	15	4,688		3,376	
Creditors arising out of reinsurance operations		131,037		107,209	
Other creditors including taxation and social security	18	69,079		86,453	
			204,804		197,038
Accruals and deferred income	19		77,801		76,798
Total liabilities			**3,536,515**		**3,257,451**

The financial statements were approved by the Board of Directors on 27 March 2013 and were signed on its behalf by:

S P Rocks
Director – President and Managing Director

The notes on pages 28 to 52 form part of these financial statements.

Notes to the Financial Statements

1 ACCOUNTING POLICIES

(a) Disclosure requirements
The financial statements have been prepared in compliance with the special provisions relating to insurance companies in Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

(b) Standard accounting practice
The financial statements comply with applicable accounting standards and the revised ABI Statement of Recommended Practice issued in December 2005 as amended in December 2006.

The company has adopted Financial Reporting Standard No.1 (Revised 1996), and is therefore exempt from the requirement to prepare a cash flow statement as it is a 100% owned subsidiary of Liberty International Holdings Incorporated, and its cash flows are included within the consolidated cash flow statement of Liberty International Holdings Inc. As allowed under Financial Reporting Standard No. 8, the company has not disclosed all related party transactions with group undertakings on the basis that the company is a subsidiary undertaking with 100% voting rights controlled within a group which produces publicly available consolidated financial statements in which the company is included.

(c) Basis of accounting
The annual basis of accounting has been applied to all classes of business written by the company.

(d) Subsidiary undertakings
The company has claimed exemption from the production of consolidated financial statements under the Companies Act 2006 s.400 as it is a subsidiary undertaking whose ultimate parent company produces consolidated accounts in a manner equivalent to financial statements drawn up under the provisions of the EU 7th Council Directive 83/349/EEC of 13 June 1983 based on Article 54(3) g of the Treaty on Consolidated Accounts.

Investments in subsidiary undertakings are held at cost less accumulated impairment losses, if any.

(e) Premiums
Gross written premiums represent premiums receivable for the whole period of cover under contracts incepting during the financial year, together with adjustments arising in the financial year to business written in previous financial years and are stated before commissions but net of taxes, duties levied on premiums and other deductions. Outward reinsurance premiums are accounted for in the same accounting period as the premiums for the related direct insurance or inwards reinsurance business.

(f) Unearned premiums
For business accounted for on an annual basis, the proportion of the premiums written in a year relating to the period of risk from 1 January to the subsequent dates of expiry of policies is carried forward as a provision for unearned premiums. The provision is calculated on the 365ths method, or, in respect of engineering / course of construction business, is calculated using an earnings profile based on the construction and maintenance period of specific policies.

(g) Unexpired risks
Provision is made for any anticipated shortfall of the provision for unearned premiums for claims and administrative expenses likely to arise after the end of the year from contracts concluded before that date. The overall assessment of whether a provision is necessary is made on the basis of all categories of business. No account is taken of future investment income.

(h) Deferred acquisition costs
Commission costs which vary with, and are primarily related to, the acquisition of new insurance contracts and the renewal of existing insurance contracts are deferred to the extent that they are attributable to premiums unearned at the balance sheet date.

(i) Investments
Investments, other than debt securities and other fixed interest securities, are stated at their current value. Listed investments are stated at bid price market value at close of business on the balance sheet date, or on the last stock exchange trading day before the balance sheet date.

1 ACCOUNTING POLICIES (continued)

(i) Investments (continued)

Redeemable fixed interest securities, held as a portfolio of such securities intended to be held on an ongoing basis, are valued at amortised cost. The amortisation is calculated so as to write off the difference between the purchase price and the maturity value over the life of the security.

Redeemable fixed interest securities are reviewed for any permanent diminution in value periodically on a holding by holding basis. Where a permanent diminution is identified, the carrying value of the security is adjusted to its fair value at that time and the difference between this value and the security's amortised cost is recorded as a realised investment loss in the profit and loss account.

(j) Investment income, expenses and charges

Investment income and expenses are accounted for on an accruals basis. In accordance with Financial Reporting Standard 16 "Current Tax", dividends are recognised at the amount receivable without any attributable tax credit. Investment income (which includes the amortisation charge in respect of investments carried at amortised cost), realised gains and losses arising from the disposal of investments, and unrealised gains and losses are dealt with through the non-technical account and then reallocated in part to the technical account to reflect that proportion of the investment return arising on technical provisions.

Realised gains or losses represent the difference between net sales proceeds (or fair value in the case of impairments) and purchase price, or in the case of debt securities and other fixed interest securities, amortised cost.

(k) Unrealised gains and losses on shares and other variable yield securities and units in unit trusts

Unrealised gains and losses on shares and other variable yield securities and units in unit trusts represent the difference between the market value at the balance sheet date and their purchase price, or if they have been previously revalued, the valuation at the last balance sheet date.

The movement in unrealised gains and losses on shares and other variable yield securities and units in unit trusts disclosed in the profit and loss account includes any reversal for previously recognised unrealised gains and losses on shares and other variable yield securities and units in unit trusts, which were disposed of in the accounting period.

(l) Outstanding claims

Full provision is made on an individual case basis for the estimated cost of claims notified but not settled by the balance sheet date after taking into account handling costs and settlement trends. A provision for claims incurred but not reported is established from statistical analysis undertaken by the company's actuaries. The methods used and the estimates made are reviewed regularly. Whilst the directors consider that the gross provision for claims and the related reinsurance recoveries are fairly stated on the basis of the information currently available to them, the ultimate liability will vary as a result of subsequent information and events. Any differences between provisions and subsequent settlements are dealt with in the technical accounts of later years.

In calculating the estimated cost of unpaid claims the company uses a variety of estimation techniques, generally based upon statistical analyses of historical experience, which assumes that the development pattern of current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which may cause the cost of unsettled claims to change when compared with the cost of previously settled claims including:

- changes in company processes which might accelerate or slow down the development and/or recording of paid or incurred claims compared with the statistics from previous periods
- changes in the legal environment
- the effects of inflation
- changes in the mix of business
- the impact of large losses
- movement in industry benchmarks

1 ACCOUNTING POLICIES (continued)

(l) Outstanding claims (continued)

A component of these estimation techniques is usually the estimation of the cost of notified but not paid claims. In estimating the cost of these the company has regard to claim circumstances as reported, and information available from loss adjusters and information on the cost of settling claims with similar characteristics in previous periods.

Large claims impacting each relevant business class were assessed separately where appropriate, being measured on a case-by-case basis or projected separately in order to allow for the possible distortive effect of the development and incidence of the large claims.

The provision for claims outstanding is based on information available at the balance sheet date and it is estimated to give a result within a normal range of outcomes. To the extent that the ultimate cost falls outside this range, for example where assumptions over claims inflation may alter in future, there is a contingent liability in respect of this uncertainty. Provisions are calculated allowing for reinsurance recoveries and a separate asset is recorded for the reinsurers' share, having regard to collectability.

(m) Claims management expenses

Claims management expenses have been determined by an apportionment of employment costs.

(n) Equalisation provisions

Equalisation provisions have been established in accordance with the requirements of the Prudential Sourcebook for Insurers and included as the equalisation provision within technical provisions.

(o) Deferred taxation

Financial Reporting Standard 19 "Deferred Tax" requires full provision to be made for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation.

Deferred tax is recognised as a liability or asset if the transactions or events that give the entity an obligation to pay more tax in the future or a right to pay less or receive more tax in the future have occurred by the balance sheet date. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

(p) Exchange rates

Assets and liabilities are translated into US dollars at the exchange rates prevailing at the balance sheet date. Income and expense transactions are translated using the rate prevailing at the date of transactions or an appropriate average rate.

Principal exchange rates used were as follows:

	Average	Closing
USD: GBP	1.58730	1.61815
USD: EUR	1.28706	1.31745

The company maintains separate currency ledgers for US dollars, £ sterling and Euro business. These separate foreign currency ledgers are considered by management to represent foreign branches. Exchange gains and losses arising from the retranslation into US dollars of the balance sheets of these branches using the rates of exchange prevailing at the balance sheet date, and the retranslation into US dollars of the profit and loss accounts of these branches using the average rates of exchange for the year, have been recorded in the statement of total recognised gains and losses.

Ledgers are held in US dollars in respect of the overseas branches in the Far East and Euros in respect of the overseas branches in Europe. Exchange gains and losses arising from the retranslation of the European overseas branches to US dollars continue to be recorded directly in the statement of total recognised gains and losses.

All other foreign exchange gains and losses continue to be recorded in the non-technical account.

1 ACCOUNTING POLICIES (continued)

(q) Fixed assets
Expenditure on leasehold improvements, software, computer equipment, motor vehicles, fixtures, fittings and office equipment is capitalised and depreciated over the estimated useful economic lives of the assets on a straight line basis.

The periods used to depreciate such assets are as follows:-

Leasehold improvements	Remaining lease term
Software	3 years
Computer equipment	3 years
Motor vehicles	4 years
Fixture, fittings and office equipment	5 - 10 years

Depreciation is included as part of administrative expenses.

(r) Pension costs
The company participates in a group contributory pension scheme. Contributions to the scheme are charged to the profit and loss account so as to spread the cost of pensions over employees' working lives with the company. Variations arising from actuarial surpluses are spread over the average remaining service lives of members to the extent that the resulting credit does not exceed the regular cost.

Defined Benefit Pension Scheme
The company has fully adopted accounting standard FRS17 "Retirement Benefits".

The difference between the fair value of the assets held in the company's defined benefit pension scheme and the scheme's liabilities measured on an actuarial basis using the projected unit method are recognised in the company's balance sheet as a pension scheme asset or liability as appropriate.

The carrying value of any resulting pension scheme assets is restricted to the extent that the company is able to recover the surplus either through reduced contributions in the future or through refunds from the scheme. The pension scheme balance is recognized net of any related deferred tax balance.

When a settlement or a curtailment occurs the change in the present value of the scheme liabilities and the fair value of the plan assets reflects the gain or loss which is recognised in the profit and loss account. Losses are measured at the date that the employer becomes demonstrably committed to the transaction and gains when all parties whose consent is required are irrevocably committed to the transaction

Changes in the defined benefit pension scheme asset or liability from factors other than cash contribution by the company are charged to the Profit and Loss account or the Statement of Total Recognised Gains and Losses in accordance with FRS17 "Retirement Benefits".

Employees joining on or after 1 January 2002 became members of the company defined contribution pension schemes. Contributions are charged in the profit and loss account as they become payable in accordance with the rules of the schemes.

(s) Leases
Assets held under finance leases and hire purchase contracts are capitalised at their fair value on the inception of the leases and depreciated over their estimated useful lives. The finance charges are allocated over the period of the lease in proportion to the capital amount outstanding.

Rentals under operating leases are charged to the profit and loss account in equal annual instalments over the period of the lease.

Notes to the Financial Statements *(continued)*

1 ACCOUNTING POLICIES (continued)

(t) Salvage and subrogation recoveries

Anticipated salvage and subrogation recoveries are calculated on an individual case basis. The level of recovery estimated is set on the basis of information which is currently available, including potential outstanding claims advices and case law. Salvage and subrogation recoveries are included in claims incurred in the profit and loss account.

2 EARNED PREMIUMS NET OF REINSURANCE

2012	Gross $000	Reinsurance $000	Net $000
Premiums written	931,420	(472,403)	459,017
Unearned premiums carried forward	(522,887)	240,754	(282,133)
Unearned premiums brought forward	457,486	(202,374)	255,112
Exchange difference on brought forward	11,284	(5,375)	5,909
Movement per Technical Account	(54,117)	33,005	(21,112)
Premiums earned	877,303	(439,398)	437,905

2011	Gross $000	Reinsurance $000	Net $000
Premiums written	740,931	(341,138)	399,793
Unearned premiums carried forward	(457,486)	202,374	(255,112)
Unearned premiums brought forward	400,625	(176,400)	224,225
Exchange difference on brought forward	(3,613)	2,333	(1,280)
Movement per Technical Account	(60,474)	28,307	(32,167)
Premiums earned	680,457	(312,831)	367,626

3 ANALYSIS OF PREMIUMS WRITTEN, CLAIMS, OPERATING EXPENSES AND REINSURANCE BALANCE

Information required by the Companies Act 2006 by class of business is as follows:

2012	Gross premium written $000	Gross premium earned $000	Gross claims incurred $000	Gross operating expenses $000	Reinsurance balance $000	Total $000	Net technical provision $000
Direct							
Marine, Aviation & Transport	209,008	208,311	(35,736)	(60,925)	(59,546)	52,104	208,163
Primary Direct & Fac Property	84,070	76,300	(56,074)	(24,104)	3,284	(594)	66,729
Primary Direct Commercial Financial	179,424	170,385	(121,675)	(57,870)	2,189	(6,971)	109,178
Primary Direct Commercial Liability	457,614	421,027	(314,211)	(125,877)	(16,441)	(35,502)	891,392
Total Direct	930,116	876,023	(527,696)	(268,776)	(70,514)	9,037	1,275,462
Total Non-Prop & Prop R/I Treaty Business	1,304	1,280	7,543	(782)	(406)	7,635	53,876
Totals	931,420	877,303	(520,153)	(269,558)	(70,920)	16,672	1,329,338

2011	Gross premium written $000	Gross premium earned $000	Gross claims incurred $000	Gross operating expenses $000	Reinsurance balance $000	Total $000	Net technical provision $000
Direct							
Marine, Aviation & Transport	194,050	183,277	(166,127)	(62,580)	42,801	(2,629)	219,200
Primary Direct & Fac Property	61,479	47,467	(60,513)	(14,833)	22,582	(5,297)	61,747
Primary Direct Commercial Financial	86,591	78,886	(72,550)	(28,030)	2,111	(19,583)	88,962
Primary Direct Commercial Liability	396,363	368,398	(135,341)	(115,988)	(90,752)	26,317	772,574
Total Direct	738,483	678,028	(434,531)	(221,431)	(23,258)	(1,192)	1,142,483
Total Non-Prop & Prop R/I Treaty Business	2,448	2,429	4,025	(590)	729	6,593	61,691
Totals	740,931	680,457	(430,506)	(222,021)	(22,529)	5,401	1,204,174

3 ANALYSIS OF PREMIUMS WRITTEN, CLAIMS, OPERATING EXPENSES AND REINSURANCE BALANCE (continued)

The company operates its business in the following divisions:

2012	Gross premium written $000	Gross premium earned $000	Gross claims incurred $000	Gross operating expenses $000	Reinsurance balance $000	Total $000	Net technical provision $000
London Market	414,803	402,081	(235,933)	(112,566)	(45,381)	8,201	817,829
UK and Ireland Commercial	174,305	155,668	(93,496)	(53,270)	(5,616)	3,286	188,000
Continental Europe	215,464	207,173	(111,466)	(59,547)	(30,898)	5,262	187,494
International	126,848	112,381	(79,258)	(44,175)	10,975	(77)	136,015
Totals	931,420	877,303	(520,153)	(269,558)	(70,920)	16,672	1,329,338

2011	Gross premium written $000	Gross premium earned $000	Gross claims incurred $000	Gross operating expenses $000	Reinsurance balance $000	Total $000	Net technical provision $000
London Market	374,619	365,303	(248,345)	(101,005)	(2,555)	13,398	773,214
UK and Ireland Commercial	130,697	107,935	(65,308)	(41,224)	(8,063)	(6,660)	155,565
Continental Europe	126,150	115,958	(66,848)	(39,507)	(9,721)	(118)	160,362
International	109,465	91,261	(50,005)	(40,285)	(2,190)	(1,219)	115,033
Totals	740,931	680,457	(430,506)	(222,021)	(22,529)	5,401	1,204,174

Commissions payable in respect of direct insurance amounted to $104,952,000 (2011: $73,266,000). Net Technical Provisions include Gross Deferred Acquisition Costs and Deferred Reinsurance Commissions.

Notes to the Financial Statements *(continued)*

4 NET OPERATING EXPENSES

2012	Gross $000	Reinsurance $000	Net $000
Acquisition costs	132,899	(111,644)	21,255
Deferred acquisition costs carried forward	(67,626)	56,711	(10,915)
Deferred acquisition costs brought forward	56,486	(49,031)	7,455
Exchange difference on brought forward	1,398	(1,295)	103
Change in deferred acquisition costs	(9,742)	6,385	(3,357)
Incurred acquisition costs	123,157	(105,259)	17,898
Administrative expenses			146,401
			164,299

2011	Gross $000	Reinsurance $000	Net $000
Acquisition costs	95,899	(81,286)	14,613
Deferred acquisition costs carried forward	(56,486)	49,031	(7,455)
Deferred acquisition costs brought forward	49,022	(40,856)	8,166
Exchange difference on brought forward	(627)	614	(13)
Change in deferred acquisition costs	(8,091)	8,789	698
Incurred acquisition costs	87,808	(72,497)	15,311
Administrative expenses			134,210
			149,521

5 INVESTMENT INCOME AND GAINS ON REALISATION OF INVESTMENTS

	2012 $000	2011 $000
Income from other financial investments	62,616	66,953
Net gains on the realisation of investments	29,700	6,430
	92,316	73,383

Notes to the Financial Statements *(continued)*

6 INVESTMENT EXPENSES AND CHARGES

	2012 $000	2011 $000
Investment management expenses including interest	2,380	2,333

7 PROFIT AND LOSS ACCOUNT

Profit on ordinary activities before tax is stated:

	2012 $000	2011 $000
After charging		
Depreciation	1,417	1,270
Operating lease rentals:		
Motor vehicles and equipment	1,011	878
Land and buildings	7,540	7,969
Impairment charge on Investment in subsidiary undertakings	1,161	-

	2012 $000	2011 $000
Auditors' remuneration:		
Fees payable to the company's auditor for the audit of the company's annual accounts	672	660
The audit of the company's subsidiaries, pursuant to legislation	152	168
Fees payable to the company's auditors and its associates for other services:		
Audit-related assurance services	149	121
Tax compliance services	328	323
Fee in respect of the audit of the group pension scheme	11	11

Notes to the Financial Statements *(continued)*

7 PROFIT AND LOSS ACCOUNT (continued)

	2012 $000	2011 $000
Directors' Remuneration		
Emoluments	2,797	4,419

	2012	2011
Number of directors who: Were members of a defined benefit pension scheme during the period	1	1

	2012 $000	2011 $000
Highest paid director's remuneration: Aggregate of emoluments and awards under long term incentive schemes, including $34,822 of pension contributions	1,522	1,406

8 TAXATION

(a) Analysis of charge in period

	2012 $000	2011 $000
Current tax		
Current year:		
Overseas taxation	(2,257)	(449)
UK taxation	(24,693)	(18,798)
Prior periods	2,383	(785)
Total current tax (see Note 8(b))	(24,567)	(20,032)
Deferred tax		
Origination and reversal of timing differences	(274)	(548)
Rate change adjustment	(488)	(541)
Total deferred tax	(762)	(1,089)
Tax charge on profit on ordinary activities	(25,329)	(21,121)

8 TAXATION (continued)

(b) Factors affecting tax charges for period

The tax charged for the period is higher than the standard effective rate of corporation tax in the UK (24.5%). The differences are explained below:

	2012 $000	2011 $000
Profit on ordinary activities before tax	98,674	69,112
Profit on ordinary activities multiplied by standard effective rate of corporation tax in the UK of 24.5% (2011: 26.5%)	(24,178)	(18,315)
Effects of:		
Unrelieved overseas tax losses and withholding taxes	(2,257)	(449)
Effect of disallowable items	(515)	(479)
Tax over/(under) provided in previous years	2,383	(789)
Current tax charge for year (see Note 8(a))	(24,567)	(20,032)

(c) Factors that may affect future tax charges

The previously enacted corporation tax rate reduction from 26% to 25% was reflected in the deferred tax calculations as at 31 December 2011. A further reduction to the corporation tax rate to 23%, with effect from 1 April 2013, was enacted by Finance Act 2012 in July 2012. The effect of this reduction in the tax rate to 23% has been reflected in the deferred tax balances recognised at 31 December 2012.

On 5 December 2012, the Chancellor announced as part of the autumn statement his intention to make a further 2% reduction in the tax applicable from 1 April 2014. In addition to this, in the Budget on 20 March 2013 the Chancellor also announced his intention to make a further reduction in the rate of UK Corporation tax to 20% from April 2015. The reductions down to 21% and 20% were not substantively enacted at 31 December 2012 and are therefore not reflected in the amounts recognised at that date. The impact of the announced rate change from 23% to 20% on the deferred tax asset is estimated to be a reduction of approximately $786,000.

Based on current business plans, the company expects to make sufficient taxable profits in the next three financial years to support the recoverability of the deferred tax asset recognised at 31 December 2012.

9 STAFF NUMBERS AND COSTS

The average number of persons employed by the company (including executive directors) during the year, analysed by category, was as follows:

	2012	2011
Underwriting	309	289
Claims	48	49
Administration	123	116
	480	454

The aggregate payroll costs of these persons were as follows:

	2012 $000	2011 $000
Wages and salaries	73,663	68,445
Social security costs	9,378	8,346
Other pension costs	6,489	6,566
	89,530	83.357

Included in Other pension costs are $7,069,000 (2011: $6,258,000) in respect of defined contribution schemes and a net profit of $580,000 (2011: $308,000) in respect of the defined benefit scheme.

10 OTHER DEBTORS

	2012 $000	2011 $000
Deferred taxation (see Note 17)	5,856	6,623
Amounts due from group undertakings	402	65
Other debtors	8,247	3,369
	14,505	10,057

Notes to the Financial Statements *(continued)*

11 INVESTMENTS IN SUBSIDIARY UNDERTAKINGS

Details of the company's investments in subsidiary undertakings, all of which produce their financial statements at 31 December each year, are as follows:

Name	Type of Business	Class of Shares Held (all held directly)	Percentage of nominal value and voting rights held by the company	Country of incorporation and operation
Vision Underwriting Limited	Underwriting Agency	Ordinary	100%	UK
Vision Employment Health and Safety Limited	Health and Safety Services	Ordinary	100%	UK
Vision Risk Management Limited	Risk Management	Ordinary	100%	UK

Reconciliation of movement in Investments in subsidiary undertakings:

	2012 $000	2011 $000
Balance at 1 January 2012	1,846	1,812
Revaluation	43	34
Impairment charge	(1,161)	-
Balance at 31 December 2012	728	1,846

12 TANGIBLE ASSETS

	Leasehold Improvements $000	Fixtures, fittings & equipment $000	Total $000
Cost:			
At 1 January 2012	3,334	10,711	14,045
Revaluation	87	251	338
Additions	193	958	1,151
Disposals	(75)	(36)	(111)
At 31 December 2012	3,539	11,884	15,423
Accumulated depreciation:			
At 1 January 2012	2,032	8,457	10,489
Revaluation	58	188	246
Charge for the year	333	1,084	1,417
Disposals	(68)	(46)	(114)
At 31 December 2012	2,355	9,683	12,038
Net book value at 31 December 2012	1,184	2,201	3,385
Net book value at 31 December 2011	1,302	2,254	3,556

Notes to the Financial Statements *(continued)*

13 OTHER FINANCIAL INVESTMENTS

	2012 $000	2011 $000
Market valuations		
Debt securities and other fixed income securities	1,700,783	1,684,824
Deposits with credit institutions	195,281	155,996
Total Market Value of Other Financial Investments	1,896,064	1,840,820
Original cost		
Debt securities and other fixed income securities	1,621,173	1,623,201
Deposits with credit institutions	195,281	155,996
Total Original Cost of Other Financial Investments	1,816,454	1,779,197
Carrying value		
Debt securities and other fixed income securities at amortised cost	1,611,370	1,613,932
Deposits with credit institutions at original cost	195,281	155,996
Total Carrying Value of Other Financial Investments	1,806,651	1,769,928

Included in the above market valuations were investments:

	2012 $000	2011 $000
Listed on the UK Stock Exchange	241,832	222,169
Listed on other investment exchanges	945,935	969,009
	1,187,767	1,191,178

The maturity value of debt securities and other fixed income securities is $1,590,499,711 (2011: $1,591,886,410) and the unamortised premium amounts to $20,869,877 (2011: $22,046,382).

14 AMOUNTS DUE TO AND FROM GROUP UNDERTAKINGS

The following amounts due (to) and from group undertakings are included within:

	2012 $000	2011 $000
Deposits with ceding undertakings	23,171	16,329
Reinsurers' share of technical provisions	136,286	106,884
Debtors arising out of reinsurance operations	7,247	995
Gross deferred acquisition costs	740	561
Technical provisions	(30,601)	(27,747)
Creditors arising out of reinsurance operations	(14,581)	(9,085)
Accruals and deferred income	(7,410)	(4,046)
Other creditors	(20,977)	(33,982)
	93,875	49,909

15 DEBTORS AND CREDITORS ARISING OUT OF DIRECT INSURANCE OPERATIONS

All amounts are owed to or due from intermediaries.

16 OTHER PREPAYMENTS

	2012 $000	2011 $000
Prepayments	3,423	2,888

17 DEFERRED TAXATION

	2012 $000	2011 $000
Other timing differences	5,856	6,189
Asset at start of year	6,189	7,986
Timing differences arising in period	(274)	(548)
Effect of reduction in tax rate	(488)	(541)
Deferred tax (charge)/credit in profit and loss account	(762)	(1,089)
Effect of foreign currency translation	-	28
Taxation recognised in the Statement of Total		
Recognised Gains and Losses	429	(736)
Asset at end of year	5,856	6,189
Deferred tax asset included in Other debtors	5,856	6,623
Deferred tax (liability)/asset deducted from Pension liability	-	(434)
	5,856	6,189

18 OTHER CREDITORS INCLUDING TAXATION AND SOCIAL SECURITY

	2012 $000	2011 $000
Premium taxes payable	18,484	23,291
Corporation taxes payable	10,200	11,245
Social security	1,947	2,394
Other creditors	38,448	49,523
	69,079	86,453

19 ACCRUALS AND DEFERRED INCOME

	2012 $000	2011 $000
Deferred reinsurance commissions	56,711	49,031
Other accruals	21,090	27,767
	77,801	76,798

20 SHARE CAPITAL

	2012 $000	2011 $000
Issued and fully paid:		
290,225,000 (2011: 290,225,000) ordinary shares of $1 each	290,225	290,225

21 RESERVES

	Profit & loss Account Excluding Pension Liability $000	Pension Liability $000	Total Profit & loss Account $000
Balance at 1 January 2012	405,279	4,643	409,922
Profit for financial year	72,896	450	73,345
Interim dividend paid in the financial year	(51,000)	-	(51,000)
Change in FRS17 "Retirement Benefits", net of tax	-	(1,835)	(1,835)
Gains and losses arising from the retranslation of assets and liabilities denominated in GBP and EUR	(14,635)	(450)	(15,084)
Balance at 31 December 2012	412,540	2,808	415,348

22 RECONCILIATION OF MOVEMENTS IN SHAREHOLDER'S FUNDS

	2012 $000	2011 $000
Total recognised gains relating to the year	56,426	52,284
Opening shareholder's funds	700,147	690,348
Dividend paid	(51,000)	(42,485)
Closing shareholder's funds	705,573	700,147

23 COLLATERAL DEPOSITS

Debt securities and deposits with credit institutions amounting to $80,831,825 (2011: $79,326,619) have been pledged as security in connection with certain of the company's overseas liabilities.

24 OTHER COMMITMENTS

Annual commitments at 31 December under non-cancellable operating leases are shown below:

	2012 Land and Buildings $000	2011 Land and Buildings $000
Operating leases expiring within two to five years	6,923	6,723
Operating leases expiring after five years	79	81

During 2013, the company entered into an agreement to lease office space with effect from March 2014 under a 17.7 year lease, at an annual cost of $5,699,000.

25 CONTINGENT LIABILITY

The company has entered into a letter of credit in favour of the Institute of London Underwriters ("ILU") for certain potential liabilities in respect of the Institute's building in Leadenhall Street, London EC3. During 2012 drawings on the letter of credit amounted to $nil (2011: $78,425) and its value at 31 December 2012 was $541,991 (2011: $524,871).

On 14 February 2008, the company provided a guarantee on behalf of a fellow group undertaking, Liberty Syndicate Management Limited, in respect of that company's financial obligations related to a property tenancy expiring on 22 February 2017. The maximum potential obligation of the company under the guarantee is dependent, inter alia, on future rent reviews but is estimated by the company to be $8,220,000.

The company has provided to the Labuan Offshore Financial Services Authority an irrevocable and unconditional guarantee that it will meet all of the company's obligations relating to its insurance operations in Labuan, Malaysia.

26 DEFINED BENEFIT PENSION SCHEME

The company participated in a funded group defined benefit scheme in the UK, together with fellow subsidiaries of Liberty Mutual Holding Company Inc. The scheme closed to future accrual on 1 July 2012 with active members of the scheme becoming deferred pensioners in the Scheme from 2 July 2012. As such there is no future service liability, and no asset in relation to refund of surplus recognised on the balance sheet. The information disclosed below is in respect of Liberty Mutual Insurance Europe Limited's participation in the scheme.

The valuation used for FRS 17 disclosures has been based on a full assessment of the liabilities of the Scheme as at 1 July 2010. The present values of the defined benefit obligation were measured using the projected unit credit method.

Actuarial gains and losses have been recognised in the period in which they occur, through the Statement of Recognised Gains and Losses (STRGL).

Following the UK Government's announcement in summer 2010, the inflation index to be used to derive statutory pension increases was changed from the Retail Prices Index (RPI) to the Consumer Prices Index (CPI). Due to a number of differences between the indices, including both constituents and construction, CPI is expected to be less than RPI over the long-term, which means that the Scheme liabilities reduced. The change was recognised at October 2010, following the pension trustees' decision to adopt CPI in the determination of Scheme liabilities. Following discussions with our pensions advisors, we recognised the reduction as a negative past service cost - that is, as a change to the constructive obligation to provide certain benefits to Scheme members.

The principal assumptions used by the independent qualified actuaries to calculate the liabilities under FRS 17 are set out below:

At 31 December	2012 %	2011 %	2010 %
Rate of increase in salaries	N/A	4.1	4.5
Rate of increase in pensions in payment where Limited Price Indexation (LPI) applies	2.7	2.9	3.3
Discount rate	4.5	4.9	5.3
Inflation assumption (RPI)	2.9	3.1	3.5
Inflation assumptions (CPI)	2.2	2.2	2.7

The mortality assumptions are based on standard mortality tables which allow for future mortality improvements. The assumptions are that a member currently aged 45 who retires at age 60 will live on average for a further 29.9 years after retirement if they are male and for a further 31.0 years if they are female.

The Company employs a building block approach in determining the long-term rate of return on pension scheme assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with the widely accepted capital market principles. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation for the Scheme at 31 December 2012.

Notes to the Financial Statements *(continued)*

26 DEFINED BENEFIT PENSION SCHEME (continued)

The assets in the scheme and the expected return were:

At 31 December	Long-term rate of return expected at 2012 %	Value at 2012 $000	Long-term rate of return expected at 2011 %	Value at 2011 $000	Long-term rate of return expected at 2010 %	Value at 2010 $000
Equities	7.5	9,524	7.8	6,501	8.2	11,112
Bonds	4.2	10,079	4.6	10,707	5.3	7,067
Other (property, cash etc)	4.0	13,555	4.2	12,981	6.1	8,242
Total market value of assets		33,158		30,189		26,421
Present value of scheme liabilities		(29,913)		(28,453)		(28,093)
Surplus/(deficit) in the scheme		3,245		1,736		(1,672)
Assets not recoverable in the future		3,245		-		-
Net pension asset/(liability) (after adjustment for deferred tax)		-		1,302		(1,220)

Analysis of the amount charged/(credited) to operating profit

	2012 $000	2011 $000
Current service cost	265	563
Curtailment	(640)	-

Analysis of the amount credited / (charged) to net investment income

	2012 $000	2011 $000
Expected return on pension scheme assets	1,573	1,815
Interest on pension scheme liabilities	(1,368)	(1,560)
Net return	205	255

26 DEFINED BENEFIT PENSION SCHEME (continued)

Analysis of amount recognised in statement of total recognised gains and losses (“STRGL”)

	2012 $000	2011 $000
Actual return less expected return on pension scheme assets	195	955
Experience gains and losses arising on the scheme liabilities	176	1,391
Changes in assumptions underlying the present value of the scheme liabilities	(1,303)	599
Total value of items recognised in the STRGL in respect of liabilities	(1,127)	1,990
Change in assets not recoverable in the future	(2,167)	-
Actuarial (loss)/gain recognised in STRGL	(3,099)	2,945

Changes to the present value of the defined benefit obligation

	2012 $000	2011 $000
Opening defined benefit obligation	28,453	28,093
Movement in year:		
Current service cost	270	551
Interest cost	1,395	1,525
Contributions by participants	37	61
Actuarial (gains)/losses on liabilities	2,029	(1,945)
Net benefits paid out	(602)	(358)
Past service costs	-	-
Curtailments	(2,570)	-
Retranslation of opening balance	901	526
Closing defined benefit obligation	29,913	28,453

Notes to the Financial Statements *(continued)*

26 DEFINED BENEFIT PENSION SCHEME (continued)

Changes to the fair value of Scheme assets

	2012 $000	2011 $000
Opening fair value of assets	30,189	26,421
Movement in year:		
Expected return on assets	1,604	1,774
Actuarial gain/(losses)on assets	199	933
Contributions by the employer	777	864
Contributions by participants	37	61
Net benefits paid out	(602)	(358)
Retranslation of opening balance	954	494
Closing fair value of assets	33,158	30,189

History of experience gains and losses

	2012 $000	2011 $000	2010 $000	2009 $000	2008 $000
Total market value of assets	33,158	30,189	26,421	24,939	19,370
Present value of scheme liabilities	(29,913)	(28,453)	(28,093)	(26,783)	(20,310)
Surplus/(deficit) in the scheme	3,245	1,736	(1,672)	(1,844)	(940)
Difference between the expected and actual return on scheme assets:					
Amount	195	955	375	2,013	(1,798)
Percentage of scheme assets	1%	3%	1%	8%	(9%)
Experience gains and losses on scheme liabilities:					
Amount	176	1,391	214	(34)	(172)
Percentage of the present value of the scheme liabilities	1%	5%	1%	0%	(1%)
Total amount recognised in statement of total recognised gains and losses:					
Amount	(3,099)	2,945	(820)	(1,070)	(408)
Percentage of the present value of the scheme liabilities	(11%)	10%	(3%)	(4%)	(2%)

Defined Contribution Scheme

The company operates a defined contribution pension scheme, the Company Pension Scheme, for its employees. The assets of the scheme are held separately from those of the company in an independently administered fund. The unpaid contributions outstanding at the year end, included in Other creditors (Note 18) are $618,514 (2011: $430,950).

Notes to the Financial Statements *(continued)*

27 TRANSACTIONS WITH DIRECTORS AND OFFICERS

Fees of $63,108 (2011: $61,874) in respect of Mr M G McKenzie were paid to McKenzie Consulting Limited, a company controlled by Mr M G McKenzie. There were no other transactions requiring disclosure between Liberty Mutual Insurance Europe Limited and its directors and officers during the year ended 31 December 2012.

28 CHANGE IN THE PROVISION FOR CLAIMS

2012	Gross $000	Reinsurance $000	Net $000
Claims outstanding carried forward	(1,987,904)	929,784	(1,058,120)
Claims outstanding brought forward	1,798,001	(841,484)	956,517
Exchange difference on brought forward	31,949	(14,862)	17,087
Movement per Technical Account	(157,954)	73,438	(84,516)

2011	Gross $000	Reinsurance $000	Net $000
Claims outstanding carried forward	(1,798,001)	841,484	(956,517)
Claims outstanding brought forward	1,564,803	(696,928)	867,875
Exchange difference on brought forward	(1,184)	386	(798)
Movement per Technical Account	(234,382)	144,942	(89,440)

29 PRIOR YEARS CLAIMS

An over-provision of reserves of $2,091,878 (2011: Over-provision $7,799,000) arose between the outstanding claims provision at the beginning of the year, payments made during the year and the provision at the end of the year.

30 EQUALISATION PROVISION

These provisions, which amount to $37,546,000 as at the year end (2011: $27,981,000), are in addition to the provisions required to meet the anticipated ultimate cost of settlement of outstanding claims at the balance sheet date, and are required by Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 to be included within technical provisions in the balance sheet, notwithstanding that it does not represent a liability at the balance sheet date. This has had the cumulative effect of reducing shareholders' funds by $28,723,000 net of tax (2011: $20,146,000). The movement in equalisation provisions during the year resulted in a decrease in the general business technical account result of $8,680,000 (2011: decrease of $7,871,000) and the profit before taxation of $9,566,000 (2011: decrease of $8,241,000).

Notes to the Financial Statements *(continued)*

31 PARENTAL GUARANTEE

On 15 February 2002 the board of Liberty Mutual Insurance Company agreed to grant a guarantee covering the company's insurance obligations. This was ratified by the Massachusetts' Department of Insurance on 10 May 2002. The original guarantee was updated and re-issued on 13 April 2006.

32 ULTIMATE PARENT COMPANY

The ultimate parent company is Liberty Mutual Holding Company Inc. of Boston, 175 Berkeley Street, Boston, Massachusetts 02117, U.S.A. a company incorporated in the United States of America.

The smallest higher group of companies for which group accounts are drawn up and of which this company is a member is Liberty International Holdings Incorporated, a company incorporated and registered in the U.S.A.

The immediate parent company of Liberty Mutual Insurance Europe Limited is Liberty UK and Europe Holdings Limited.

Copies of the group accounts of Liberty International Holdings Incorporated and of Liberty Mutual Holding Company Inc. of Boston are available from the companies' registered office, 175 Berkeley Street, Boston, Massachusetts 02117, U.S.A.

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Liberty Mutual Insurance Europe Limited
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About Liberty International Underwriters (LIU)
Established in 1999, Liberty International Underwriters provides a diverse range of specialty products distributed exclusively through the independent broker network. The LIU staff of over 1,300 professionals offer core products in marine, aviation, energy, engineering, global crisis management, property, casualty, professional liability, directors & officers, environmental, strategic assets, construction, surety bonds, legal expenses and trade credit insurance. Worldwide offices include North America, Europe, Latin America, the Middle East, and Asia Pacific.

About Liberty Mutual Insurance
"Helping people live safer, more secure lives" since 1912, Boston-based Liberty Mutual Insurance is a diversified global insurer and the third largest property and casualty insurer in the U.S. based on 2011 direct premiums written as reported by the National Association of Insurance Commissioners.

Liberty Mutual Insurance also ranks 84th on the Fortune 100 list of largest corporations in the U.S. based on 2011 revenue. As of December 31, 2012, Liberty Mutual Insurance had $120.1 billion in consolidated assets, $101.5 billion in consolidated liabilities, and $36.9 billion in annual consolidated revenue.

Liberty Mutual Insurance offers a wide range of insurance products and services, including personal automobile, homeowners, workers compensation, property, commercial automobile, general liability, global specialty, group disability, reinsurance and surety. Liberty Mutual Insurance (www.libertymutualinsurance.com) employs over 50,000 people in more than 900 offices throughout the world.

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