PROSPECTUS DATED 6 MAY 2015

CIS General Insurance Limited

(Incorporated as a registered society in England and Wales with Registered no. 29999R)

£70,000,000 Callable Dated Deferrable Tier Two Notes due 2025

Issue price: 100 per cent.

The £70,000,000 Callable Dated Deferrable Tier Two Notes due 2025 (the **Notes**) will be issued by CIS General Insurance Limited (**CISGIL** or the **Issuer**) and constituted by a trust deed to be dated on or about 8 May 2015 (as amended or supplemented from time to time, the **Trust Deed**) between the Issuer and the Trustee (as defined in "Terms and Conditions of the Notes" (the **Conditions**, and references herein to a numbered **Condition** shall be construed accordingly)).

Application has been made to the Financial Conduct Authority (the **FCA**) in its capacity as competent authority under the Financial Services and Markets Act 2000 (the **UK Listing Authority** and the **FSMA**, respectively) for the Notes to be admitted to the official list of the UK Listing Authority (the **Official List**) and to the London Stock Exchange plc (the **London Stock Exchange**) for the Notes to be admitted to trading on the London Stock Exchange's regulated market. The London Stock Exchange's regulated market is a regulated market for the purposes of Directive 2004/39/EC (the **Markets in Financial Instruments Directive**). This document (hereinafter referred to as the **Prospectus**) comprises a prospectus for the purposes of Directive 2003/71/EC, as amended (the **Prospectus Directive**) and has been approved by the UK Listing Authority for the purposes of Article 5.4 of the Prospectus Directive.

The Notes will bear interest from (and including) 8 May 2015 (the **Issue Date**) to (but excluding) 8 May 2020 (the **Call Date**) at the rate of 12 per cent. per annum, payable (subject to the following proviso) quarterly in arrear on 8 August, 8 November, 8 February and 8 May in each year commencing on 8 August 2015. For the Reset Period (as defined herein), the Notes will bear interest at the Reset Rate of Interest (as defined herein). The Issuer will be required to defer any payment of interest which is otherwise scheduled to be paid if (i) such payment cannot be made in compliance with the solvency condition described in Condition 2.2 (the **Solvency Condition**) or (ii) a Regulatory Deficiency Interest Deferral Event (as defined herein) has occurred and is continuing, or would occur if such interest payment were made as more particularly set out in Condition 4.1. Any interest so deferred shall, for so long as the same remains unpaid, constitute **Arrears of Interest**. Arrears of Interest will not themselves bear interest, and will be payable as provided in Condition 4.2.

Unless previously redeemed or purchased and cancelled, the Notes will mature on 8 May 2025 (the **Maturity Date**) and shall, subject to the satisfaction of the Solvency Condition and to no Regulatory Deficiency Redemption Deferral Event (as defined herein) having occurred, be redeemed on the Maturity Date. Prior to any notice of redemption before the Maturity Date or any substitution, variation or purchase of the Notes, the Issuer will be required to have complied with relevant legal or regulatory requirements including as to notifications to, or consent or non-objection from, (in each case, if and to the extent required) the Relevant Regulator (as defined herein) and to be in continued compliance with Regulatory Capital Requirements (as defined herein) applicable to it and in the case of a redemption or purchase prior to the fifth anniversary of the Issue Date, to be funded out of the proceeds of a new issuance of capital of at least the same quality as the Notes and being otherwise permitted under the Relevant Rules. Subject to the foregoing, to the Relevant Rules implementing Solvency II (as each such term is defined herein), to satisfaction of the Solvency Condition and to no Regulatory Deficiency Redemption Deferral Event having occurred all, but not some only, of the Notes may be redeemed at the option of the Issuer before the Maturity Date (i) on the Call Date or (ii) upon the occurrence of certain specified events relating to taxation or a Capital Disqualification Event (as defined herein) at their principal amount together with any accrued but unpaid interest to (but excluding) the date of redemption and any Arrears of Interest and the Issuer will, upon the occurrence of such events relating to taxation or a Capital Disqualification Event, also have the right to substitute the Notes for, or vary the terms of the Notes so that they remain or become, Qualifying Dated Tier 2 Securities (as defined herein), as described in *"Terms and Conditions of the Notes - Redemption, Substitution, Variation and Purchase"*.

The Notes will be direct, unsecured and subordinated obligations of the Issuer, ranking *pari passu* and without preference amongst themselves, and will, in the event of the winding-up of the Issuer (other than an Approved Winding-up as defined in the Conditions) or in the event of an administrator of the Issuer being appointed and giving notice that it intends to declare and distribute a dividend, be subordinated to the claims of all Senior Creditors (as defined herein) of the Issuer but shall rank at least *pari passu* with all other subordinated obligations of the Issuer which constitute, or would constitute, Pari Passu Securities and shall rank in priority to the claims of holders of Junior Securities (both as defined in Condition 2.1).

The Notes will be issued in registered form in principal amounts of £100,000 and integral multiples of £1,000 in excess thereof. The Notes will be represented by a global certificate in registered form (the **Global Certificate**) registered in the name of a nominee of, and shall be deposited on or about the Issue Date with a common depositary for, Euroclear Bank SA/NV (**Euroclear**) and Clearstream Banking, *société anonyme* (**Clearstream, Luxembourg**). Individual certificates (**Certificates**) evidencing holdings of Notes will be available only in certain limited circumstances - see "*Summary of Provisions relating to the Notes whilst in global form* ".

An investment in the Notes involves certain risks. Prospective investors should have regard to the factors described under the section headed "*Risk Factors*" in this Prospectus. The Notes will not be rated on issue.

Structuring Adviser and Bookrunner

UBS INVESTMENT BANK

The Issuer accepts responsibility for the information contained in this Prospectus. To the best of the knowledge of the Issuer (having taken all reasonable care to ensure that such is the case) the information contained in this Prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information.

No person is or has been authorised to give any information or to make any representation other than those contained in or consistent with this Prospectus in connection with the issue or sale of the Notes and, if given or made, such information or representations must not be relied upon as having been authorised by or on behalf of the Issuer, the Manager (as defined in *"Subscription and Sale"* below) or the Trustee. Neither the delivery of this Prospectus nor the offering or any sale made in connection herewith shall, under any circumstances, imply that the information contained herein concerning the Issuer is correct at any time subsequent to the date hereof, that there has been no change in the affairs of the Issuer since the date hereof or that there has been no adverse change in the financial position of the Issuer since the date hereof or that any other information supplied in connection with the Notes is correct as of any time subsequent to the date on which it is supplied or, if different, the date indicated in the document containing the same.

The Manager and the Trustee have not separately verified the information contained in this Prospectus. Neither the Manager nor the Trustee makes any representation, express or implied, or accepts any responsibility, with respect to the accuracy or completeness of any of the information contained in this Prospectus or any other information provided by the Issuer in connection with the offering of the Notes. Neither the Manager nor the Trustee accepts any liability in relation to the information contained in this Prospectus or any other information provided by the Issuer in connection with the offering of the Notes or their distribution. Neither this Prospectus nor any other information supplied in connection with the offering of the Notes is intended to constitute, and should not be considered as, a recommendation by any of the Issuer, the Manager or the Trustee that any recipient of this Prospectus or any other information supplied in connection with the offering of the Notes should purchase the Notes. Each potential purchaser should make its own independent investigation of the financial condition and affairs and its own approval of the credit worthiness of the Issuer. Each potential purchaser of Notes should determine for itself the relevance of the information contained in this Prospectus and its purchase of Notes should be based upon such investigation as it deems necessary. Neither the Manager nor the Trustee undertakes to review the financial condition or affairs of the Issuer during the life of the arrangements contemplated by this Prospectus nor to advise any investor or potential investor in the Notes of any information coming to their attention.

In the ordinary course of business, the Manager has engaged and may in the future engage in normal banking or investment banking transactions with the Issuer and its affiliates or any of them.

Neither this Prospectus nor any other information provided by the Issuer in connection with the offering of the Notes constitutes an offer of, or an invitation by or on behalf of, the Issuer or the Manager or the Trustee or any of them to subscribe for, or purchase, any of the Notes (see *"Subscription and Sale"* below). This Prospectus does not constitute an offer to sell or the solicitation of an offer to buy the Notes in any jurisdiction to any person to whom it is unlawful to make the offer or solicitation in such jurisdiction. The distribution of this Prospectus and the offer or sale of Notes may be restricted by law in certain jurisdictions. The Issuer, the Trustee and the Manager do not represent that this Prospectus may be lawfully distributed, or that the Notes may be lawfully offered, in compliance with any applicable registration or other requirements in any such jurisdiction, or pursuant to an exemption available thereunder, or assume any responsibility for facilitating any such distribution or offering. In particular, no action has been taken by the Issuer, the Trustee or the Manager or any of them which is intended to permit a public offering of the Notes or the distribution of this Prospectus in any jurisdiction where action for that purpose is required. Accordingly, no Notes may be offered or sold, directly or indirectly, and neither this Prospectus nor any advertisement or other offering material may be distributed or published in any jurisdiction, except under circumstances that will result in compliance with any applicable laws and regulations. Persons into whose possession this Prospectus or any Notes may come must inform themselves about, and observe, any such restrictions on the distribution of this Prospectus and the offering and sale of Notes. In particular, there are restrictions on the distribution of this Prospectus and the offer or sale of Notes in the United States of America (the **U.S.**) and the United Kingdom. Persons in receipt of this Prospectus are required by the Issuer, the Trustee and the Manager to inform themselves about and to observe any such restrictions. For a description of certain further restrictions on offers and sales of Notes and distribution of this Prospectus, see "*Subscription and Sale*" below.

The Notes have not been and will not be registered under the United States Securities Act of 1933, as amended (the **Securities Act**) and are subject to U.S. tax law requirements. Subject to certain exceptions, Notes may not be offered, sold or delivered within the U.S. or to U.S. persons, as defined in Regulation S under the Securities Act (**Regulation S**). For a description of certain restrictions on offers and sales of Notes and on distribution of this Prospectus, see "*Subscription and Sale*" below.

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (1) the Notes are legal investments for it, (2) the Notes can be used as collateral for various types of borrowing and (3) other restrictions apply to its purchase or pledge of the Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Notes under any applicable risk-based capital or similar rules.

In this Prospectus, unless otherwise specified, all references to **pounds**, **sterling**, **£**, **p** or **pence** are to the lawful currency of the United Kingdom.

Forward-Looking Statements

This Prospectus includes certain "forward-looking statements". Statements that are not historical facts, including statements about the beliefs and expectations of the Issuer and its directors or management, are forward-looking statements. Words such as "believes", "anticipates", "estimates", "expects", "intends", "plans", "aims", "potential", "will", "would", "could", "considered", "likely", "estimate" and variations of these words and similar future or conditional expressions, are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend upon future circumstances that may or may not occur, many of which are beyond the control of the Issuer and all of which are based on their current beliefs and expectations about future events. Such forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance or achievements of the Issuer, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such forward-looking statements are based on numerous assumptions regarding the present and future business strategies of the Issuer and the environment in which the Issuer will operate in the future. These forward-looking statements speak only as at the date of this Prospectus.

Except as required by the FCA, the London Stock Exchange, the Listing Rules, the Prospectus Rules, the Disclosure and Transparency Rules or any other applicable law or regulation, the Issuer expressly disclaims any obligations or undertakings to release publicly any updates or revisions to any forward-looking statements contained in this Prospectus to reflect any change in the Issuer's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

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SUPPLEMENTAL PROSPECTUS

Following the publication of this Prospectus a supplement may be prepared by the Issuer and approved by the UK Listing Authority in accordance with Article 16 of the Prospectus Directive.

Statements contained in any such supplement (or contained in any document incorporated by reference therein) shall, to the extent applicable (whether expressly, by implication or otherwise), be deemed to modify or supersede statements contained in this Prospectus. Any statement so modified or superseded shall not, except as so modified or superseded, constitute part of this Prospectus.

The Issuer will, in the event of any significant new factor, material mistake or inaccuracy relating to information included in this Prospectus prior to the Issue Date which is capable of affecting the assessment of the Notes, prepare a supplement to this Prospectus. The Issuer has undertaken to the Manager that it will comply with section 87G of the FSMA.

OVERVIEW OF THE PRINCIPAL FEATURES OF THE NOTES

The following overview refers to certain provisions of the terms and conditions of the Notes and the Trust Deed and is qualified by the more detailed information contained elsewhere in this Prospectus. Terms which are defined in "Terms and Conditions of the Notes" below have the same meaning when used in this overview, and references herein to a numbered "Condition" shall refer to the relevant Condition in "Terms and Conditions of the Notes".

Issue	£70,000,000 Callable Dated Deferrable Tier Two Notes due 2025.
Issuer	CIS General Insurance Limited.
Trustee	BNY Mellon Corporate Trustee Services Limited.
Principal Paying Agent	The Bank of New York Mellon, London Branch.
Registrar and Transfer Agent	The Bank of New York Mellon (Luxembourg) S.A.
Calculation Agent	The Bank of New York Mellon, London Branch.
Status and Subordination	The Notes will constitute direct, unsecured and subordinated obligations of the Issuer and will rank *pari passu* and without any preference among themselves. The rights and claims of the Noteholders against the Issuer will be subordinated in a winding-up of the Issuer in accordance with Condition 2.1 and the provisions of the Trust Deed.
Solvency Condition	Except in a winding-up, all payments under or arising from the Notes (including, without limitation, payments of interest, Arrears of Interest and principal) will be conditional upon the Issuer satisfying the solvency condition described in Condition 2.2 (the **Solvency Condition**), and no amount will be payable under or arising from the Notes unless and until such time as the Issuer can make such payment in compliance with the Solvency Condition.
Interest	The Notes will bear interest on their outstanding principal amount from (and including) the Issue Date at the rate of 12 per cent. per annum, payable (subject as provided under "*Deferral of Interest*" below) quarterly in arrear on each Interest Payment Date to (but excluding) the Reset Date. Thereafter, the interest rate will be reset on the Reset Date by reference to the Reset Reference Rate plus the Margin as described in Condition 3.
Interest Payment Dates	8 May, 8 August, 8 November and 8 February of each year, starting on 8 August 2015.
Deferral of Interest	The Issuer will be required to defer any payments of interest on the Notes which would otherwise be due on any Interest Payment Date if (i) such payment cannot be made in compliance with the Solvency Condition, or (ii) a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or would occur if

such payment of interest was made on such Interest Payment Date.

Regulatory Deficiency Interest Deferral Event means any event (including, without limitation, where an Insolvent Insurer Winding-up has occurred and is continuing and any event which causes any Solvency Capital Requirement applicable to the Issuer, all or part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group) or any Insurance Undertaking within the CISGIL Group to be breached and such breach is an event) which under Solvency II and/or under the Relevant Rules means that the Issuer must defer payment of interest (or, if applicable, Arrears of Interest) in respect of the Notes. See Condition 4.1.

Arrears of Interest

Any interest in respect of the Notes not paid on an Interest Payment Date due to the occurrence of a Regulatory Deficiency Interest Deferral Event or due to the operation of the Solvency Condition will, so long as the same remains unpaid, constitute **Arrears of Interest**.

Arrears of Interest may be payable, in whole or in part, at any time at the option of the Issuer (subject to regulatory consent (if then required) and to the Solvency Condition and provided that a Regulatory Deficiency Interest Deferral Event is not subsisting and would not occur upon payment of the same) upon notice to Noteholders, and in any event all Arrears of Interest will (subject, in the case of (i) and (iii) below, to regulatory consent (if then required) and to the Solvency Condition) become payable in whole (and not in part) upon the earliest of the following dates:

(i) the next Interest Payment Date which is not a Mandatory Interest Deferral Date; or

(ii) the date on which an order is made or a resolution is passed for the winding-up of the Issuer (other than an Approved Winding-up) or the date on which any administrator of the Issuer gives notice that it intends to declare and distribute a dividend; or

(iii) the date fixed for any redemption or purchase of Notes by or on behalf of the Issuer or any of its Subsidiaries pursuant to Condition 5.

No interest will accrue on Arrears of Interest. See Condition 4.2.

Redemption at Maturity

The Notes will, subject as provided under "*Deferral of Redemption*", "*Early Redemption at the Option of the Issuer on the Call Date*" and "*Early Redemption at the Option of the Issuer upon the occurrence of a Tax Event or a Capital Disqualification Event*" below, be redeemed on 8 May 2025 at their principal amount together with Arrears of Interest, if any, and any other unpaid interest accrued to (but excluding) the date of redemption in accordance with the Conditions.

Deferral of Redemption

The Issuer will be required to defer any scheduled redemption of the Notes (whether at maturity or if it has given notice of early redemption in the circumstances described below under "*Early Redemption at the Option of the Issuer on the Call Date*" or "*Early Redemption at the Option of the Issuer upon the occurrence of a Tax Event or a Capital Disqualification Event*") if (i) the Notes cannot be redeemed in compliance with the Solvency Condition, (ii) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if the Notes were redeemed or (iii) (if then required) regulatory consent has not been obtained or redemption cannot be made in compliance with the Relevant Rules at such time.

In the event of any deferral of redemption of the Notes as set out above, the Notes will become due for redemption only in the circumstances described in Condition 5.1.

Regulatory Deficiency Redemption Deferral Event means any event (including, without limitation, where an Insolvent Insurer Winding-up has occurred and is continuing and any event which causes any Solvency Capital Requirement applicable to the Issuer, all or part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group) or any Insurance Undertaking within the CISGIL Group to be breached and such breach is an event) which under Solvency II and/or under the Relevant Rules means that the Issuer must defer or suspend repayment or redemption of the Notes.

Early Redemption at the Option of the Issuer on the Call Date

The Issuer may, subject to certain conditions and upon notice to the Noteholders as more particularly set out in Condition 5.3, elect to redeem all, but not some only, of the Notes on the Call Date. The Notes will be redeemed at their principal amount, together with Arrears of Interest, if any, and any other unpaid interest accrued to (but excluding) the date of redemption in accordance with the Conditions.

Early Redemption at the Option of the Issuer upon the occurrence of a Tax Event or a Capital Disqualification Event

The Issuer may, subject to certain conditions and upon notice to Noteholders, at any time elect to redeem all, but not some only, of the Notes, at their principal amount together with Arrears of Interest (if any) and any other accrued and unpaid interest to (but excluding) the date of redemption, if a Tax Event or Capital Disqualification Event has occurred and is continuing.

A **Tax Event** will occur if:

(i) as a result of a Tax Law Change (as defined in Condition 5.4(a)), in making any payments on the Notes, the Issuer has paid or will or would on the next payment date be required to pay Additional Amounts (as defined in Condition 7) on the Notes and the Issuer cannot avoid the foregoing in connection with the Notes by taking measures reasonably available to it; or

(ii) as a result of a Tax Law Change, in respect of the Issuer's obligation to make any payment of interest on the next following Interest Payment Date, (x) the Issuer would not be entitled to claim a deduction in respect of computing its taxation liabilities in the Relevant Jurisdiction, or such entitlement is materially reduced or deferred; or (y) the Issuer would not to any material extent be entitled to have such deduction or losses derived therefrom set against the profits of companies with which it is grouped for applicable tax purposes in the Relevant Jurisdiction (whether under the group relief system current as at the date of the Tax Law Change or any similar system or systems having like effect as may from time to time exist), and in each such case the Issuer cannot avoid the foregoing in connection with the Notes by taking measures reasonably available to it.

A **Capital Disqualification Event** is deemed to have occurred if as a result of any change to (or change to the interpretation by any court or authority entitled to do so of) the Relevant Rules, the Directive or Solvency II the entire principal amount of the Notes is fully excluded from counting as Tier 2 Capital for the purposes of the Issuer or all or any part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group), whether on a solo or group basis, except (in either case) where such non-qualification is only as a result of any applicable limitation on the amount of such capital.

See Conditions 5.2, 5.4 and 5.5.

Substitution and Variation

The Issuer may, subject to certain conditions and upon notice to Noteholders, at any time elect to substitute all (and not some only) of the Notes for, or vary the terms of the Notes so that they remain or become (as applicable), Qualifying Dated Tier 2 Securities if, immediately prior to the giving of the relevant notice to Noteholders, a Tax Event or Capital Disqualification Event has occurred and is continuing.

Purchases

The Issuer and any of its Subsidiaries may, subject to Condition 2.2 and Condition 5.2, at any time purchase Notes in the open market or otherwise at any price. All Notes purchased by or on behalf of the Issuer or any of its Subsidiaries may (at the option of the Issuer or the relevant Subsidiary) be held, reissued, resold or surrendered for cancellation.

Meetings of Noteholders

The Conditions and the Trust Deed contain provisions for calling meetings of Noteholders to consider matters affecting their interests. These provisions permit defined majorities to bind all Noteholders including Noteholders who did not attend and vote at the relevant meeting and Noteholders who voted in a manner contrary to the majority.

Taxation and Additional Amounts	All payments of principal and interest by or on behalf of the Issuer in respect of the Notes will be made free and clear of, and without deduction or withholding for or on account of taxes imposed, levied, collected, withheld or assessed by or on behalf of any Relevant Jurisdiction, unless such withholding or deduction is required by law. In the event that any such withholding or deduction is required by law, the Issuer will pay such additional amounts as shall be necessary in order that the amounts received by the Noteholders after such withholding or deduction shall equal the respective amounts which would have been received in respect of the Notesin the absence of any such withholding or deduction (**Additional Amounts**), subject to some exceptions, as described in Condition 7.
Events of Default and Enforcement	If default is made for a period of 14 days or more in the payment of any interest (including, without limitation, Arrears of Interest) or principal due in respect of the Notes or any of them, the Trustee in its discretion may, and if so requested by Noteholders of at least one quarter in principal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution shall (subject in each case to it having been indemnified and/or secured and/or prefunded to its satisfaction), institute proceedings for the winding-up of the Issuer and/or prove in the winding-up or administration of the Issuer and/or claim in the liquidation of the Issuer for such payment, but may take no further or other action to enforce, prove or claim for any such payment. No payment in respect of the Notes or the Trust Deed may be made by the Issuer pursuant to Condition 9.1, nor will the Trustee accept the same, otherwise than during or after a winding-up of the Issuer or after an administrator of the Issuer has given notice that it intends to declare and distribute a dividend, unless the Issuer has given prior written notice (with a copy to the Trustee) to, and received consent or non-objection from, the Relevant Regulator which the Issuer shall confirm in writing to the Trustee.
Form	The Notes will be issued in registered form and represented upon issue by a registered global certificate (the **Global Certificate**) which will be registered in the name of a nominee for a common depositary (the **Common Depositary**) for Clearstream Banking, *société anonyme* (**Clearstream, Luxembourg**) and Euroclear Bank S.A./N.V. (**Euroclear**) on or about the Issue Date. Save in limited circumstances, Notes in definitive form will not be issued in exchange for interests in the Global Certificate.
Denomination	The Notes will be issued in denominations of £100,000 and integral multiples of £1,000 in excess thereof.
Listing	Application has been made for the Notes to be admitted to the Official List of the UK Listing Authority and for the Notes to be admitted to trading on the London Stock Exchange's regulated market.

Ratings	The Notes will be unrated on issue and the Issuer does not currently intend to seek a rating in respect of the Notes.
Governing Law	The Notes and the Trust Deed, and any non-contractual obligations arising out of or in connection therewith, will be governed by and construed in accordance with English law.

RISK FACTORS

The Issuer believes that the following factors may affect its ability to fulfil its obligations under the Notes. All of these factors are contingencies which may or may not occur and the Issuer is not in a position to express a view on the likelihood of any such contingency occurring.

Any of these risk factors, individually or in the aggregate, could have an adverse effect on the Issuer and the impact each risk could have on the Issuer is set out below.

Factors which the Issuer believes may be material for the purpose of assessing the market risks associated with the Notes are also described below.

The Issuer believes that the factors described below represent the principal risks inherent in investing in the Notes, but the Issuer may be unable to pay interest, principal or other amounts on or in connection with the Notes for other reasons, and the Issuer does not represent that the statements below regarding the risks of holding the Notes are exhaustive. Prospective investors should also read the detailed information set out elsewhere in this Prospectus and reach their own views prior to making any investment decision.

FACTORS THAT MAY AFFECT THE ISSUER'S ABILITY TO FULFIL ITS OBLIGATIONS UNDER THE NOTES

Strategic and Business Risks

The Issuer may be unable to implement its strategic plan effectively

The Issuer has identified a series of strategic initiatives following a review of its business during 2014. These initiatives include a focus on existing customers of the Co-operative Group (as defined in "*Business Description - Overview*"); building strong data and analytical capabilities through the use of new technologies to utilise and leverage data captured by the Co-operative Group; developing key distribution partnerships; and reducing risk to diversify income (and volatility) and reduce regulatory capital requirements as further detailed in "*Business Description - Strategy*".

These initiatives will take several years to implement fully and there is a risk that the execution of the strategy may take longer than expected due to failure to define and manage delivery of the initiatives to the expected time, cost and quality. If losses are incurred by the Issuer on the core insurance business, there may be inadequate capital resources to support the costs of the initiatives. These losses could arise from any increases in the cost of transformation of the Issuer's business or existing operations, greater competition further reducing premiums or adverse claims experience.

As part of its comprehensive strategic review in 2014 (the **2014 Strategic Review**), the Issuer identified that its information technology (**IT**) infrastructure and operations were too inflexible and expensive to enable it to effectively compete in the changing general insurance market. The lack of flexibility inherent in the Issuer's IT processes and legacy systems has meant that, while business levels have been falling, there are significant costs, including but not limited to IT and staff costs, within the business that cannot simply and immediately be reduced in proportion to the falling business levels and this has resulted in a commission and expense ratio in the financial year to 31 December 2014 (**FY 2014**) of 40.2 per cent. compared to 31.1 per cent. in the financial year to 31 December 2013 (**FY 2013**), which is significantly higher than the Issuer's competitors and not sustainable. The commission and expense ratio is used as this mitigates any issues arising from changes in mix between in house and externally sourced activities. The Issuer concluded during the period of the 2014 Strategic Review that, while it would be possible to improve performance by taking actions in the identified areas under the existing operating model, to fully deliver its strategic goals it would be necessary to establish a programme to transform its technology capabilities, the success of which is integral to the continued success of the business.

To implement successfully the building of strong data and analytical capabilities to utilise and leverage data captured by the Co-operative Group, the Issuer relies on a third-party supplier to provide the underlying technology. There is the risk that the new technology solution takes longer to implement or is more costly than expected, or that it fails to fully deliver the efficiencies or functionality expected resulting in lower than expected profitability and competitiveness. This may arise through incorrect selection of the technology suppliers, inadequate contract and service agreements with the suppliers, failure to manage the suppliers during delivery, or a failure of the supplier to deliver to time, cost and quality.

The Issuer's access to the Co-operative Group's distribution partnerships, brand and membership data is dependent on its position within the Co-operative Group. There is a risk that if this position changes in the future the Issuer would not have such access, which would reduce potential pricing advantages and lead to lower profitability and reduced competitiveness.

There is the risk that the expected benefits of using Co-operative Group membership data cannot be fully realised. This may be due to being unable to utilise the data effectively in pricing through inadequate capability, regulatory or other restrictions on the use of such data, changes in the usefulness of the data due to changes in the profile of membership or demographic trends. Failure to realise the benefits of using membership data would reduce potential pricing advantages and lead to lower profitability and reduced competitiveness.

There is a risk that the Issuer is not able to successfully develop distribution partnerships, including the creation of a panel of underwriters, thereby failing to improve the competitive position and underwriting footprint of the Issuer as expected, which could have a material adverse effect on the Issuer's profitability and financial strength.

In light of the extensive nature of the 2014 Strategic Review, there is a risk that there will be insufficient management time or focus to both deliver the review and continue with the effective management of the ongoing business. An inadequate governance structure for the transformation programme may lead to the programme being improperly designed, the time taken to deliver the programme being extended or even the failure of the programme to achieve the strategic aims. If management is focused on the transformation programme, it may not take the actions required to ensure the business, continuing under the existing operating model, is properly run which may have an adverse impact on the profitability of the existing business and an increase in the risk associated with the transformation programme. The Issuer has established a transformation governance structure, more details of which can be found in "*Business Description - Strategy*".

The ability of the Issuer to implement successfully, and achieve the expected benefits of, its initiatives may be impacted by both internal and external factors, including factors not within the Issuer's control, such as regulatory factors, further deterioration in claims, experience related to weather and catastrophe events, the impact of softening rates in certain lines of business, interest rate and competition. The benefits of these strategic actions are expected to be realised over the medium term but the Issuer may not achieve the expected benefits in the envisaged time frames, or at all. Failure to do so would be likely to have a material adverse effect on the Issuer's financial strength and capital position, as well as its business, results of operations and financial condition.

The Issuer's business is highly dependent upon the successful functioning of its computer and data processing systems, failure of which could adversely affect the Issuer's business and damage its customer relationships

The Issuer relies on IT systems for critical elements of its business processes. These systems, which include complex computer and data processing platforms, may be disrupted by events including terrorist acts, natural disasters, telecommunications and network failures, power losses, physical or electronic security breaches, fraud, identity theft, process failures, computer viruses, computer hacking, malicious employee attacks or similar events. In addition, the Issuer may identify, and has identified, weaknesses in its computer and data processing systems, as well as the control environment for these systems. The failure of IT systems could interrupt the Issuer's operations or materially impact its ability to conduct business. Material flaws or damage to the system, particularly if sustained or repeated, could result in the loss of existing or potential business relationships, compromise the Issuer's ability to pay claims in a timely manner and/or give rise to regulatory implications, which could result in a material adverse effect on the Issuer's reputation, financial condition and results of operations.

Design and implementation of upgrades to these systems can be complex and may not always deliver all the intended benefits according to the original timescales and budgets for doing so.

In addition, certain key elements of the Issuer’s platform are legacy systems that are not fully integrated into the overall platform and may require increased manual input, which increases the risk of error. The Issuer intends to invest in the upgrade and replacement of its legacy systems. In addition to the costs associated with such upgrade and replacement, any resulting dislocation or future upgrades of other systems could result in the overall platform being more susceptible to inefficiencies or disruptions. The Issuer’s own insurance cover might not adequately compensate it for material losses that could occur due to disruptions in its service as a result of computer and data processing systems failure and electronic attacks.

Certain of the Issuer’s IT and operational support functions are outsourced to parties within the Co-operative Group. These support functions remain critical to the Issuer’s business, such as the provision of its operating platform and provision of HR, legal and some shared finance services. The Issuer is reliant in part on the continued performance, accuracy, compliance and security of these internal service providers. If the contractual arrangements with these internal parties are terminated, the Issuer may not find an alternative provider or supplier for the services, on a timely basis, on equivalent terms or without significant expense or at all. Any of the foregoing could have a material adverse effect on the Issuer’s business, financial condition and results of operations.

The Issuer receives legacy IT services that are shared with other members of the Co-operative Group and other external third parties. A programme is currently underway to separate the Issuer’s IT services. The separation, which involves extraction and transferral of information to such third parties, presents risks to the Issuer, including disruption to services and associated reputational impact.

In addition, certain of the Issuer’s IT and operational support functions are outsourced to third parties. These support functions are important to the Issuer’s business, such as the development and maintenance of its operating platform and the provision of loss adjusting services. The Issuer is reliant in part on the continued performance, accuracy, compliance and security of all these service providers. If the contractual arrangements with any third party providers are terminated, the Issuer may not find an alternative outsource provider or supplier for the services, on a timely basis, on equivalent terms or without significant expense or at all. Any of the foregoing could have a material adverse effect on the Issuer’s business, financial condition and results of operations.

The Issuer operates in a highly competitive environment

The Issuer operates in a highly competitive environment (in particular, the motor insurance market) that is subject to cyclical patterns. In addition, the growth of price comparison websites has increased price competition to acquire customers, new market entrants have implemented aggressive pricing policies and growth targets and certain competitors have greater financial resources than the Issuer. Developments in the general insurance industry, in particular the rapid growth of price comparison websites, have made it easier for consumers to compare the prices and terms offered by various insurance providers.

Price comparison websites have also enabled the entry into the market of small and niche private motor and home insurers by allowing them to reach a large number of potential customers without incurring significant up-front marketing costs.

Beyond regulatory considerations, including raising and maintaining adequate levels of capital for its underwriting activities (including additional capital expected to be required by the Solvency II Directive), there are relatively few barriers to entry for businesses seeking to compete with the Issuer's private motor and home insurance product lines.

The overall importance of price comparison websites (in particular, as the predominant retail distribution channel for motor insurance policies and as an increasingly important retail distribution channel for home insurance policies) has led to increased price competition to retain and acquire targeted customers. If competitive pressures compel the Issuer to reduce prices, its operating margins and underwriting results may be materially adversely affected. The experience of the UK motor insurance market over the recent years has been that competitive pressures have depressed prices and profitability, although there are signs as at the date of this Prospectus that these pressures may be easing.

Whilst the Issuer has already taken steps to achieve profitability, as at 31 December 2014 the Issuer recognised a loss and any future profitability remains highly dependent upon market conditions.

The Solvency II Directive, which will impose new risk-based capital requirements on European-domiciled insurance companies, may, when implemented, require an increase in the Issuer's capital

The Solvency II Directive (2009/138/EC) (**Solvency II**), an insurance industry regulation agreed by the European Parliament in 2009, will require European domiciled insurers to move to more risk-based capital requirements.

The Solvency II Directive was amended by the European Parliament in 2014, which included extending the implementation date to 1 January 2016.

There is continued uncertainty regarding the impact of Solvency II on insurance companies. Although the delegated acts (which set out certain detailed provisions of the Solvency II regime) were published in the Official Journal on 17 January 2015 and entered into force on 18 January 2015, certain binding technical standards and guidance setting out the final rules have not yet been adopted, and the European Commission and the European Insurance and Occupational Pensions Authority (**EIOPA**) will continue to finalise certain aspect of the Solvency II regime during 2015.

Since the requirements of Solvency II are still being finalised, there is a risk that the final Solvency II requirements may differ from the draft legislation as at the date of this Prospectus. Consequently, there is a risk that this could lead to increases in the capital the Issuer is required to maintain to support its insurance business, or decreases to the excess of the Issuer's assets over its liabilities, in each case, compared with the Issuer's current expectations. In particular, details in relation to the standard formula for calculating solvency capital requirements have not been finalised and changes may lead to higher capital requirements than the Issuer currently anticipates.

Regulators may issue guidance and other interpretations of applicable requirements, which could require the Issuer to make further adjustments to its calculations of applicable requirements in the future. In addition, there is considerable uncertainty relating to the imposition of capital add-ons by regulators for insurers both as to regulatory practice surrounding the application of capital add-ons, and the amount of such capital add-ons.

The Issuer expects to use the standard formula (a prescribed methodology used to calculate solvency capital requirements) initially under Solvency II, but may subsequently apply for permission to use an approved internal model which may improve risk-based decision-making and capital efficiency, and simplify internal operations and reporting.

The Prudential Regulation Authority (**PRA**) may require Co-operative Banking Group Limited (**CBGL**) to submit a group submission under Solvency II. As CBGL is not a regulated entity, the Issuer will be responsible for ensuring that the group submission is prepared. This could lead to increased complexity and costs for the Issuer to assess capital requirements and regulatory capital and produce reporting both as a stand-alone entity and on a group basis. The cost and complexity of preparing the group submission is not expected to be materially greater than the cost and complexity of preparing the Issuer's entity level submission alone.

Failure to maintain adequate capital could have a variety of negative regulatory and operational implications for the Issuer

Insurance companies such as the Issuer are required to maintain a minimum level of assets in excess of the value of their liabilities (referred to as regulatory capital) to comply with a number of regulatory requirements relating to the Issuer's solvency and reporting bases. The Issuer's regulatory capital requirements have in the past both increased and decreased, and may from time to time in the future increase and decrease for a number of reasons. The Issuer's capital position may also be assessed by its regulators and may change as a result of evolving regulatory views on capital adequacy. This may result in an increased capital requirement in the form of individual capital guidance (**ICG**) from the PRA over and above the Issuer's individual capital assessment (**ICA**).

Under the General Prudential Sourcebook (**GENPRU**), individual companies permitted to carry on insurance business in the UK are required to maintain a minimum level of capital resources (the "minimum capital requirement" or **MCR**) consistent with the EU insurance directives. Detailed rules in GENPRU and the Prudential Sourcebook for Insurers (**INSPRU**) define how to calculate the capital resources requirement and what constitutes capital for these purposes.

The ICA is a forward-looking economic risk-based assessment of the capital requirements of the Issuer, based on its assessment of the risks to which it is exposed. The Chief Risk Officer and the Issuer's Risk department have responsibility for the overall design and governance of the Issuer's capital model, which is developed and operated within the actuarial team. Capital model methodology and results are reviewed and approved by the Issuer's Model Governance Committee, Executive Risk Committee (**ERC**) and Board. Outputs from the capital model are used in areas such as investment and reinsurance decisions, determining the risk in the business plans with regard to risk appetite and return on capital in pricing.

As noted above, the PRA can review the ICA if it disagrees with the Issuer's calculation and, if it deems necessary, an 'add-on' can be applied to reflect risks that were inadequately captured by the ICA.

See "*Business Description – Summary Financial Information*" for information on the Issuer's published capital position for the years ended 31 December 2013 and 2014. Capital requirements under the ICA and the ICG are significantly in excess of the published MCR as they are set at a higher confidence level and reflect the specific risk-profile of the Issuer. As at 31 December 2014, the ICG was £341m and the economic capital resources, which can be used to meet the ICG, and are calculated using various adjustments to regulatory capital for the purposes of calculating the ICG coverage ratio, were £402m, resulting in an ICG coverage ratio of 118 per cent. The ICG is a point in time assessment by the PRA of the amount of capital that is required to be held by the Issuer. The PRA assessment may change over time including as a result of at least an annual assessment and supervisory review of the Issuer's capital model. As a result there is a risk that the Issuer may be required from time to time to hold more capital.

To mitigate the risk of breaching its regulatory capital requirements, the Issuer sets its capital risk appetite, which defines how much additional capital (**buffer capital**) the Issuer should hold over and above its most onerous regulatory capital requirement. The Issuer's current risk appetite is to aim to hold a buffer at least sufficient to allow the Issuer to continue to meet its regulatory capital requirement following a 1-in-6 year event and to target a buffer sufficient to allow the Issuer to continue to meet its regulatory capital requirement following a 1-in-10 year event. Based on this risk appetite, the Issuer currently aims to hold buffer capital equivalent to at least 31 per cent. of the ICA with a target equivalent to 38 per cent. of the ICA. The risk appetite is reviewed periodically and while it is anticipated that the buffer capital thresholds referred to above will remain constant, the actual required buffer capital may change in the future as the Issuer's economic model is updated, including to reflect changes in the Issuer's risk exposure, and as the Issuer moves from an ICA basis to Solvency II.

While the Board is responsible for reviewing and setting its risk appetite on a regular basis, it is nevertheless anticipated that the 1-in-6 year event and 1-in-10 year event capital buffer thresholds as set out above will be maintained under the Solvency II regime to set and measure the Issuer's risk appetite. Projections carried out as part of the strategic planning process and incorporating the new capital to be raised through the issue of the Notes and any alternative sources of financing (together, the **New Capital**), using the capital buffer thresholds referred to above, indicate that the Issuer will be above the 1-in-6 year event and 1-in-10 year event risk appetite measures for its Solvency II regulatory capital requirements throughout the 2015-2019 plan period. The strategic planning process using the Solvency II standard formula (as described in "*Recent and future developments – Solvency II*") (unadjusted for any possible regulatory add-ons) produces an estimated ratio of Eligible Own Funds (prior to the New Capital) to Solvency Capital Requirement (**SCR**) at 31 December 2014 of approximately 160 per cent. With the New Capital but with the costs of transformation this ratio is anticipated to fall in a range over the next two years of between approximately 165 and 190 per cent.

Since September 2014, the Issuer's capital level has fallen below its 1-in-6 year event risk appetite buffer capital requirement but it has maintained its capital above all its regulatory requirements. The Issuer's management have, in addition to seeking to raise the New Capital, identified a number of potential actions to improve the Issuer's capital position, as described in "*Business description – Risk Reduction and Capital Management*".

See "*The Solvency II Directive, which will impose new risk-based capital requirements on European-domiciled insurance companies, may, when implemented, require an increase in the Issuer's capital*" for further information on the risk of a material increase in the Issuer's capital requirements following the introduction of Solvency II on 1 January 2016.

Any inability to meet regulatory capital requirements in the future would be likely to lead to intervention by the PRA. In these circumstances, the PRA, in the interests of policyholder security, could be expected to require the Issuer to take steps to restore regulatory capital to acceptable levels, for example by requiring the Issuer to cease to write or reduce writing new business. The Issuer may also need to increase premiums, increase its reinsurance coverage or divest additional parts of its business and investment portfolio, any of which may be difficult or costly or result in a significant loss, particularly in cases where such measures need to be undertaken in a short time frame.

Failure of the Issuer to maintain adequate levels of capital could have a material adverse effect on the Issuer's business, prospects, financial condition and results of operations and the ability of the Issuer to make payments under the Notes. See "*Payments of interest on, and redemption of, the Notes must in certain circumstances be deferred by the Issuer*" below.

The Issuer's capital position and exposure to risk can be adversely affected by a number of factors, including factors which erode the Issuer's capital resources

The Issuer's capital position can be adversely impacted by a number of factors, in particular factors that erode the Issuer's capital resources and could impact the quantum of risk to which the Issuer is exposed. Such factors include lower than expected earnings and accumulated negative market impacts (such as pension deficit movements and asset valuation). In addition, any event that erodes current profitability and/or is expected to reduce future profitability or make profitability more volatile could impact the Issuer's capital position.

The Issuer is undertaking a variety of measures to strengthen its capital position in light of emerging trends in capital adequacy as well as to provide the Issuer with the flexibility to operate with fewer concerns over capital constraints. Failure to achieve and maintain adequate capital buffers could have an adverse impact on growth prospects for the Issuer.

Changes to EU IFRS generally or specifically for insurance companies may materially adversely affect the reporting of the Issuer's financial results

Changes to EU International Financial Reporting Standards (**IFRS**) for insurance companies have been proposed in recent years and further changes may be proposed in the future. The International Accounting Standards Board published proposals that would introduce significant changes to the statutory reporting of insurance entities that prepare financial statements according to EU IFRS. The accounting proposals, which are not expected to become effective before 2016, will change the presentation, disclosure requirements and measurement of insurance contracts, including the effect of technical reserves and reinsurance on the value of insurance contracts. It is uncertain whether and how the proposals may affect the Issuer should they become definitive standards. Current proposals may have an adverse effect on the manner in which the Issuer reports provisions and therefore identifies and reports revenues and costs and could also have an effect on the Issuer's financial performance through changes affecting the calculation of taxation. These and any other changes to EU IFRS that may be proposed in the future, whether or not specifically targeted at insurance companies, could materially adversely affect the Issuer's reported results of operations and its financial position. The Issuer prepares accounts under IFRS.

The Issuer could be adversely affected by the loss of one or more key employees or by an inability to attract, retain and properly incentivise, or obtain UK regulatory approval for, senior personnel

The future success of the Issuer is substantially dependent on the continued services and continuing contributions of its directors, senior underwriters, senior management and other key personnel. While the Issuer has entered into employment contracts or letters of appointment with such key personnel, the retention of their services cannot be guaranteed.

There is a risk that the Issuer is unable to recruit and retain employees of suitable skill and experience, in particular those with financial, IT, underwriting, actuarial, claims, Solvency II and other specialist skills. The Issuer competes with other financial services groups for skilled personnel, primarily on the basis of its reputation, financial position, remuneration policies and support services, and may incur significant costs to recruit and retain appropriately qualified individuals. The Issuer has recently strengthened its Board and executive team, including recent appointments of new non-executive directors with business transformation and/or finance experience and continues the recruitment process for two executive roles of IT Transformation Director and Chief Operating Officer. The Issuer retains a number of employees on a contract basis including several key roles within the business, such as the Interim Chief Finance Officer and Interim IT Director. Such contractor employment arrangements have an increased employee retention risk.

In addition, the PRA and FCA also have the power to regulate individuals in the UK who have significant influence over the key functions of an insurance business, such as governance, finance, audit, compliance and management functions. The PRA and FCA may not approve individuals for such functions unless they are satisfied that they have appropriate qualifications and/or experience and are fit and proper to perform those functions, and may withdraw their approval for individuals whom they deem no longer fit and proper to perform those functions.

The loss of the services of one, or some of, the senior management or other key personnel or the inability to recruit, retain, motivate and train staff of suitable quality who are approved by the regulators could adversely affect the ability of the Issuer to continue to conduct its business and maintain its competitive position, which could have a material adverse effect on the Issuer's results of operations and financial condition.

Reputation Risk

Loss of business reputation or negative publicity could negatively impact the Issuer's business and results of operations and implementation of its strategy

The Issuer's success and results of operations are dependent on the strength and reputation of the Issuer and the wider Co-operative Group. The Issuer is vulnerable to adverse market perception because it operates in an industry where integrity and customer trust and confidence are paramount. The Issuer is exposed to the risk that litigation, employee misconduct, operational failures, regulatory or other investigations or actions, press speculation and negative publicity, whether or not well founded, could damage its brands or reputation. The Issuer's reputation may also be adversely affected by negative publicity associated with those that it insures. In addition, claims management companies and consumer protection groups could increase their focus on the insurance industry, which may negatively impact the Issuer. Any damage to the Issuer's brands or reputation could cause existing customers, partners or intermediaries to withdraw their business from the Issuer and potential customers, partners or intermediaries to elect not to do business with the Issuer and could also make it more difficult for the Issuer to attract and retain qualified employees. Such damage to the Issuer's or the wider Co-operative Group reputation could cause disproportionate damage to the Issuer's business, even if the negative publicity is factually inaccurate or unfounded.

During 2013 and 2014, the Co-operative Group brand suffered reputational damage due to the situation regarding the Co-operative Bank p.l.c. (the **Co-operative Bank**) solvency position and the corporate governance of the Co-operative Group through a complicated membership committee structure. This impacted the Issuer's new business volumes during 2014 contributing to the reduction in overall business volume. Reputational damage suffered by the Issuer as a result of a weakened Co-operative brand could negatively impact the Issuer's premiums and incomes in the future as the reputational damage to the wider Co-operative brand may take a number of years to overcome. A degree of the brand dependency risk previously attributed to the Co-operative Bank has been addressed as the Co-operative Bank has been recapitalised and is now independent from the Co-operative Group, which as of the date of this Prospectus has only a 20 per cent. holding in Co-operative Bank. However, the reputation of the Co-operative Bank may continue to impact the Issuer's business until such time as existing and potential future customers fully acknowledge the separation of the Co-operative Bank.

There is a programme underway to separate the IT operations of the Issuer from the Co-operative Bank which will further reduce the Issuer's dependency on the Co-operative Bank. See "*The Issuer's operations, results and implementation of strategy may be impacted where services are currently provided by other entities in the Co-operative Group*" below. In addition the Co-operative Group has approved significant changes to the governance of the Co-operative Group with the implementation of a professional independent board.

Despite the reputational damage suffered during 2013 and 2014, research has shown that the Co-operative brand still resonates strongly with consumers. The reputation and brand of the Issuer and the wider Co-operative Group is a key feature that the Issuer intends to leverage to support its strategy to focus on the existing Co-operative Group customers and be "the go to insurance provider for Co-operative members". Further damage to such reputation could have a material adverse effect on the ability of the Issuer to implement its strategy and consequently on its results of operations and financial condition.

Conduct Risk

Unfair treatment of customers could negatively impact the Issuer's reputation and/or result in regulatory intervention

Unfair treatment of customers could negatively impact the Issuer's business reputation through negative publicity, which could negatively impact the Issuer's business and results of operations and may require significant costs to redress those customers affected.

Conduct risk is a key area of focus across the financial services industry, with increasing scrutiny from the FCA. Failure to meet the FCA's expectations in terms of customer treatment could lead to regulatory investigative, disciplinary or enforcement actions.

Regulatory Risk

The Issuer's regulated business is subject to extensive regulatory supervision in the UK

The conduct of the Issuer's business is subject on an on-going basis to significant regulatory supervision. Insurance underwriting is highly regulated in the UK and such regulation is largely based on requirements contained in relevant EU directives. To carry out such activities, the Issuer is required to hold and maintain certain licences, permissions and authorisations and to comply on an on-going basis with applicable rules and regulations.

The PRA and FCA have wide powers to supervise and intervene in the affairs of insurance companies and have broad supervisory powers dealing with all aspects of the business activities of such entities including, among other things, the authority to grant and, in specific circumstances, to vary or cancel authorisations. The PRA and the FCA have the power to undertake a range of investigative, disciplinary or enforcement actions, including public censure, restitution, fines or sanctions and to require firms to pay compensation.

The PRA and FCA may, from time to time, make enquiries of the Issuer regarding its compliance with particular regulations governing the operation of its business. The Issuer faces the risk that the PRA or the FCA could find that it has failed to comply with applicable regulations or has not undertaken corrective action as required. The impact of the Issuer being found to be non-compliant by any such enquiry and/or investigation is difficult to assess or quantify. The PRA or FCA (as applicable) may, among other things, seek to vary the Issuer's permissions, impose a fine or require the Issuer to undertake customer redress in such circumstances. In addition, such enquiries or investigations could result in adverse publicity for, or negative perceptions regarding, the Issuer. Such enquiries or investigations could also affect the Issuer's relations with current and potential customers, as well as divert management's attention away from the day-to-day management of the Issuer's business.

The Issuer believes that it dedicates sufficient resources to its compliance programme for each of its regulated business activities. The Issuer endeavours to respond to regulatory enquiries in an appropriate way and to take corrective action when warranted.

Where matters of public policy are concerned, the PRA and the FCA may intervene directly to provide redress to customers. Issues and disputes may arise from time to time from the way in which the insurance industry has sold or administered an insurance policy or other product or in the way in which they have treated policyholders or customers, either individually or collectively, which may result in investigative, disciplinary or enforcement actions by the FCA or PRA or require the making of redress to customers.

The Issuer will not always be able to predict the impact of future legislation or regulation or changes in the interpretation or operation of existing legislation or regulation on the Issuer's business, results of operations and financial condition.

Changes in government policy, legislation or regulatory interpretation applying to companies in the financial services and insurance industries in any of the markets in which the Issuer operates, which may be applied retrospectively, may adversely affect its product range, distribution channels, capital requirements, dividends payable by Subsidiaries (if any) and, consequently, results and financing requirements.

The Issuer may face increased compliance costs due to the need to set up additional compliance controls or the direct cost of such compliance because of changes to financial services legislation or regulation.

A change of law or regulation or changes in the interpretation or operation of existing legislation or regulation may adversely affect the Issuer's business, results of operations and financial condition

The Issuer will not always be able to predict the impact of future legislation or regulation or changes in the interpretation or operation of existing legislation or regulation on its business, results of operations and financial condition. Changes in government policy, legislation or regulatory interpretation applying to companies in the financial services and insurance industries in any of the markets in which the Issuer operates, which may be applied retrospectively, may adversely affect its capital requirements, its ability to meet its obligations in respect of the Notes and, consequently, results and financing requirements.

The Issuer may also face increased compliance costs due to the need to set up additional compliance controls because of changes to financial services legislation or regulation.

Certain insurance activities, including insurance activities carried on by the Issuer, have been subject to competition review and investigation

In the UK, the Competition Commission has been investigating the private motor insurance industry, the provisional findings of which were that there were certain features of the market that it had reasonable grounds to suspect were preventing, restricting or distorting competition and leading to higher insurance premiums for customers. The Competition and Markets Authority published its final report on the private motor industry on 24 September 2014. The proposed measures in the report include:

- a ban on agreements between price comparison websites and insurers which stop insurers from making their products available more cheaply on other online platforms;
- better information for consumers on the costs and benefits of no-claims bonus protection; and
- a recommendation that the FCA reviews how insurers inform consumers about other products sold as add-ons to car insurance policies.

The Competition and Markets Authority published a draft order on 7 January 2015 setting out how changes resulting from its investigation into private motor insurance will be introduced. The final order was published on 18 March 2015. Certain provisions in the final order will not come into force immediately. Whilst the Issuer is still investigating the implementation of the measures, the Issuer is not anticipating any material impact to current practices.

In addition, in March 2014, the FCA investigated add-ons in the general insurance industry and found that they tend to represent poor value for money for customers and proposed a series of measures intended to change market practice. These measures included requiring subsequent confirmations from purchasers of certain add-ons, banning pre-ticked boxes, requiring firms to publish claims ratios to highlight low-value products and improving the way in which add-ons are offered through price comparison websites. The FCA's final report was published on 24 July 2014. As stated in the FCA's Business Plan 2015/16 the FCA intends to consult on the proposed remedies. The FCA has only commenced consultations on some measures, however, the impact on the Issuer's current practices is not anticipated to be of a material nature.

As a result of a decision of the European Court of Justice on gender equality, there is a risk that the exemption from the age discrimination provisions under the Equality Act 2010 (which allows insurers to take age into account in the assessment of risk) may be open to challenge. The Issuer's ability to price risk effectively and accurately may be affected if the use of age as a factor in risk assessment is prohibited. The impact of this may be heightened by the fact that, following the 2011 decision of the European Court of Justice, ruling that gender-related factors could not be used in determining premiums and benefits under insurance policies, the Issuer is no longer able to use gender as a factor in pricing risk. This prohibition came into effect in the United Kingdom on 21 December 2012 by means of an amendment to the Equality Act 2010.

Insurance Risk

The cyclical nature of the general insurance market may lead to fluctuations and volatility in the Issuer's results of operations or financial condition

The general (and, in particular, motor) insurance industry is subject to cyclical patterns, some of which are unpredictable. This causes significant fluctuations and volatility in the results of operations of general insurers. Many of the factors contributing to these cyclical patterns are beyond the control of any insurer, such as changes in the economic environment (including an economic downturn), the timing, location or severity of weather-related and catastrophic events, increases or decreases in the levels of insurance and reinsurance underwriting capacity in the industry and increases or decreases in levels of competition. The Issuer is exposed to the cyclical effects of such developments, including the need to increase or decrease policy prices to remain profitable and/or competitive, which could have a material adverse effect on the Issuer's business and the Issuer's results of operations or financial condition. Cyclicality may be made more acute if such developments coincide with each other.

The financial performance of the private motor insurance industry in particular has tended to fluctuate in cyclical patterns characterised by periods of significant competition in pricing and underwriting terms and conditions, which is known as a 'soft' insurance market, followed by periods of lessened competition and increasing premium rates, which is known as a 'hard' insurance market. Although an individual company's financial performance is dependent on its own specific business characteristics, the profitability of most private motor insurance companies tends to follow this cyclical market pattern, with profitability generally increasing in hard markets and decreasing in soft markets. The market is currently in a 'soft' phase of the insurance market pricing cycle in which pricing levels produce low profitability results or operating losses. If the private motor insurance industry continues to soften significantly over the short to medium term, the Issuer's profitability may be materially adversely affected. Over the longer term, the unpredictability and competitive nature of the motor and home insurance industries may lead to significant period-to-period and year-to-year volatility in the Issuer's results of operations and financial condition.

The use of inaccurate assumptions in pricing and reserving for insurance business and/or inadequate underwriting procedures may have an adverse effect on the Issuer's business profitability

The Issuer is required to make a number of assumptions in relation to the business being written. These assumptions include the costs of writing the business and settling claims, and the frequency and severity of claims.

The assumptions may turn out to be incorrect, thereby adversely impacting on the Issuer's profit. The Issuer's underwriting procedures and criteria may be inadequate to correctly price the risk being written, which may also adversely impact the Issuer's profit.

Large bodily-injury claims arising on motor insurance policies, which may result in periodic payment orders, are difficult to predict with a high degree of accuracy. These would also have an adverse impact on the Issuer's profit due to higher than expected claims.

Furthermore, outstanding claims provisions for the general insurance business are based on the best estimate ultimate cost of all claims incurred but not settled at a given date, whether reported or not, together with related claims handling costs. Any provisions for incurred but not reported and potential future re-opened claims are also included.

A range of methods, including stochastic projections, may be used to determine these provisions. Underlying these methods are a number of explicit or implicit assumptions relating to the expected settlement amount and settlement pattern of claims.

If the assumptions underlying the reserving basis were to prove incorrect, the Issuer might have to increase the amount of the general insurance provisions, which would adversely impact its financial condition or results of operations.

Natural catastrophe events, which are often unpredictable by nature, could result in material losses

The frequency and severity of claims incurred by the Issuer is affected, amongst other things, by the incidence of adverse weather events and catastrophes.

Severe weather events like rainstorms, windstorms, snowstorms, hailstorms and freeze events represent a material risk to the Issuer and may cause significant damage to vehicles and homes, particularly in heavily populated areas where there is a commensurate concentration of risk. In severe cold weather, water pipes may freeze and burst, leading to water damage and a consequent increase in the number and value of home insurance claims. A period of prolonged or frequent rainstorms may cause increased levels of flood damage, whereas prolonged periods of dry and hot weather may lead to increased levels of subsidence, each of which can lead to an increase in the frequency and severity of home insurance claims. Similarly, in prolonged periods of wet or icy conditions, there is likely to be an increase in the number of motor accidents, increasing the frequency and severity of motor insurance claims suffered by the Issuer.

Weather-related events cannot be predicted with accuracy, and UK weather patterns and conditions in recent years have created additional unpredictability and uncertainty about risk exposure and future trends. As a result of the uncertainty and unpredictability of weather patterns and climatic conditions, the Issuer's assumptions regarding weather-related events may turn out to be incorrect in the future. Since the Issuer's assumptions on weather-related events and climatic conditions are a factor in the pricing of policy premiums and in its reserving policies and reinsurance arrangements, an increased incidence of such events in any one year or over a number of years could have a material adverse effect on the Issuer's business and on the Issuer's results of operations or financial condition.

The Issuer's results of operations, financial condition, profitability and liquidity may be impacted by the availability of reinsurance arrangements

An important element of the Issuer's risk management strategy is to purchase reinsurance, thereby transferring exposure to certain risks to others through reinsurance arrangements. The

Issuer currently uses the reinsurance markets primarily to limit its risk, to support its growth and to manage its capital efficiently. The Issuer is exposed to concentrations of risk with individual reinsurers due to the nature of the reinsurance market and the restricted range of reinsurers that have acceptable credit ratings. The Issuer operates a policy to manage its reinsurance counterparty exposures, by limiting the reinsurers that may be used and applying strict limits to each reinsurer. Reinsurance exposures are aggregated with other exposures to ensure that the overall risk is within appetite.

Reductions in risk appetite among reinsurers may result in changes in price or willingness to reinsure certain risks, which could have a material adverse effect on the Issuer's results of operations or financial condition. If reinsurers do not offer to renew their products and services, in whole or in part, for any reason, there is a risk that the Issuer may be unable to procure replacement cover for any reinsurance agreements terminated at rates equivalent to those of the terminated cover and that the Issuer may be exposed to un-reinsured losses during any interim period between termination of the existing agreements and the start of any replacement cover.

The Issuer could be adversely affected by emerging trends in claims, pricing and coverage and changes in the legal environment

As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect the Issuer's business by either requiring the Issuer to extend coverage beyond its underwriting intent or increasing the number or size of claims. Examples of emerging claims and coverage issues include:

- adverse changes in loss trends;
- judicial expansion of policy coverage and the impact of new theories of liability;
- growth of claims culture;
- legislative or judicial action that affects policy coverage or interpretation, claim quantification, or pricing;
- a growing trend of plaintiffs targeting property and casualty insurers in purported class action litigation relating to claims-handling and other practices;
- new causes of liability or mass claims;
- claims in respect of directors' and officers' coverage, professional indemnity and other liability covers; and
- climate change-related litigation.

The effects of these and other unforeseen emerging claim and coverage issues are inherently difficult to predict, but could result in an increase in either or both the number and the magnitude of claims, and may therefore have a material adverse effect on the Issuer's business, financial condition and results of operations.

The Issuer's exposure to asbestos and noise-induced hearing loss claims may lead to an increase in its claims provisions

The Issuer has exposure to asbestos and noise-induced hearing loss claims arising from legacy employer's liability policies. The Issuer continues to receive claims from policies written in prior years asserting in particular damages from asbestos-related and noise-related exposures. The estimation of provisions for the ultimate cost of claims for asbestos and noise exposure is subject to a range of uncertainties that is generally greater than those associated with other lines of business. As a result, it is not possible to determine the future development of asbestos and environmental claims with the same degree of reliability as with other types of claims.

As with other lines of business, insufficient claims provisions in respect of asbestos and noise-induced hearing loss claims (or any other classes of personal injury claims which may emerge) could have an adverse effect on the Issuer's financial condition, results of operations and cash flows, though the effect could be greater than in respect of such other lines of business.

Market Risk

The Issuer is exposed to risks in relation to its investments and the financial markets

The Issuer is exposed to market risk (which includes the risk of potential losses from adverse movements in market rates and prices including interest rates, credit spreads, equity prices, property prices and foreign currency exchange rates) and credit risk (which includes non-performance of contractual payment obligations on invested assets and changes in the creditworthiness of invested assets such as exposures to issuers or counterparties for bonds, equities on its invested assets and indirectly through its exposure to the Co-operative Group's defined benefit pension scheme (see "*The Issuer may have increased costs or capital requirements as a consequence of revised valuation and/or changes in the treatment of the Co-operative Group pension schemes*"). The level of risk associated with the Issuer's portfolio is expected to remain relatively low, as the Issuer's investment strategy is to achieve acceptable returns, while minimising exposure to equities and other volatile instruments. Currently, the Issuer only invests in sterling-denominated UK government and highly-rated corporate bonds, and short-term sterling deposits with financial institutions. The value of, or income from, assets held is subject to volatility from changes in both market interest rates and spreads related to the specific credit-worthiness of the relevant issuer and this could have a material adverse effect on the Issuer's financial condition, results of operations and cash flows. In the short-term, the most material market risk impacting solvency is an increase in the spreads on corporate bonds, as the impact of changes in interest rates on the market value of bonds is largely offset by corresponding changes in liabilities valued on a discounted basis. The Issuer has no direct exposure to equities or property, although there is some indirect exposure to these assets through the Co-operative Group's defined benefit pension schemes.

Fluctuations in interest rates affect returns on and the market values of the Issuer's fixed income investments. Interest rates are typically subject to factors beyond the Issuer's control. Generally, investment income will be reduced during sustained periods of lower interest rates as higher yielding fixed income securities are redeemed prior to their maturity date, mature or are sold and the proceeds reinvested at lower rates. Low interest rates prevailing over the last few years have made it more difficult for insurance companies, such as the Issuer, to maintain investment returns and the persistence of the low interest rate environment will continue to put downward pressure on the Issuer's investment returns.

While the Issuer does not directly invest in equity securities or property, it has exposure indirectly through assets held by the Co-operative Group's defined benefit pension scheme. Moreover, the Issuer in the future could reassess its asset mix and elect to invest directly in equity securities, property or other asset-types which are generally subject to greater risks and more volatility than fixed income securities.

Low investment returns, caused in the current economic environment largely by low interest rates, may continue to impact the Issuer's earnings and solvency capital.

A lack of pricing transparency, market liquidity, declines in bond and/or equity prices, alone or in combination, could have a material adverse effect on the Issuer's results of operations and financial condition through realised losses, impairments or changes in unrealised gains positions.

In the future, the Issuer may use hedging, forward contracts and derivative instruments to reduce its exposure to adverse fluctuations in interest rates, credit-spreads on corporate bonds and equity markets. Any failure by any of the Issuer's counterparties to discharge their obligations or to provide adequate collateral if and when required could have a material adverse effect on the Issuer's financial condition, results of operations and cash flows.

Operational Risk

Operational risks, such as those arising from the failure or improper operation of internal processes, are inherent in the Issuer's business

The Issuer's financial, accounting, data processing or other operating systems and facilities may fail to operate properly or become disabled as a result of events that are wholly or partially beyond its control, such as natural disasters, power losses, network failures, increased transaction volume, terrorist attacks, process failures or similar events. Any failure, termination or constraint in respect of its systems could adversely affect the Issuer's ability to effect transactions, service its clients, manage its exposure to risk or expand its businesses or result in financial loss or liability to its clients, impairment of its liquidity, disruption of its businesses, regulatory intervention or reputational damage. In addition, the Issuer has outsourced its investment management function to an asset management company and is dependent on their systems and controls in respect of the portfolios they manage.

A key assumption used in the pricing of the Issuer's insurance products, as well as the provisions for claims, is the relative time and efficiency with which claims will be notified, processed and paid. Efficient and effective claims management depends, among other things, on well-trained personnel making accurate and timely decisions with respect to claims handling. Inefficiencies and inaccuracies in managing and paying claims can lead to issues such as inaccurate indemnity decisions, inappropriate claims reserving and/or payment decisions, an increase in undetected fraud and inaccurate management information for reserving and pricing, resulting in additional claims costs and claims handling-related expenses as well as increased risk that technical reserves and/or pricing models will be inappropriate or inaccurate. This risk is particularly acute where the time lag between claim and payment is large. If the Issuer's claims management processes prove to be inefficient or ineffective or it otherwise suffers from costs or expenses above expected levels, the Issuer could be forced to refine its pricing models, potentially resulting in a loss of business, and increase its technical reserves. Such additional costs or inflation effects could harm the Issuer's profitability, which could have an overall adverse effect on the Issuer's business, prospects, results of operations and financial condition.

Liquidity Risk

The Issuer may incur losses if it is forced to liquidate assets

The Issuer holds a significant portfolio of assets that are available to generate funds through either outright sale or sale and repurchase arrangements with other market participants and depositories. The Issuer may be forced to liquidate assets in the event of a catastrophe event that results in a sudden and unexpected large number of claims. While the Issuer may reclaim some or all of these claims from its reinsurers, there may be a time-delay between the claims arising and being paid to customers, and the recovery payment being received from reinsurers.

The Issuer's ability to meet liquidity needs may also be constrained by regulations that require it to maintain or increase regulatory capital, or by the fact that certain assets may be encumbered or otherwise non-tradable.

Additionally, the Issuer's ability to access funding sources on favourable economic terms or to liquidate its assets to satisfy claims or for other purposes (for example, to refinance existing indebtedness at call dates or at maturity) is dependent on a variety of factors, including a number of factors that are outside its control, such as general market conditions and confidence in the global banking system. The capital and credit markets may be subject to periods of extreme volatility and disruption, which could cause the Issuer's liquidity and credit capacity to be constrained.

Credit Risk

The Issuer may incur losses due to failure of reinsurance counterparties

While reinsurance makes the assuming reinsurer liable to the Issuer to the extent of the risk ceded, it does not discharge the Issuer from its primary obligation to pay under an insurance policy for losses incurred. The Issuer is therefore subject to credit risk with respect to its current and future reinsurers, as the ceding of risk to reinsurers does not relieve the Issuer of liability to its customers regarding the portion of the risk that has been reinsured, if the reinsurers fail to meet their payment obligations for any reason. The insolvency of any reinsurers or their inability or refusal to pay claims under the terms of any of their agreements with the Issuer could therefore have a material adverse effect on the Issuer. Collectability of reinsurance is largely a function of the solvency of reinsurers. Significant reinsurance purchases are reviewed annually to ensure that the levels of protection being bought reflect any developments in exposure and the risk appetite of the Issuer.

Pension Risk

The Issuer may have increased costs or capital requirements as a consequence of revised valuation and/or changes in the treatment of the Co-operative Group pension scheme

The Issuer has an agreement with CFS Management Services Limited (**CFSMS**) to pay pension costs in relation to staff currently and previously employed by CFSMS and assigned to work for the Issuer. This means that the Issuer is exposed to pension risk through the Co-operative Pension Scheme (**PACE**). The PACE trustee, in consultation with The Co-operative Group, is responsible for the risk management arrangements for PACE, agreeing suitable contribution rates, investment strategy and for taking professional advice as appropriate. Consultation with PACE is at the Co-operative Group level.

The Issuer is exposed to potential future increases in required pension contributions and capital set aside for pension risk. Costs arise through future accrual contributions, deficit repair contributions, expenses and potential employer debt under Section 75 of the Pensions Act. In FY 2014 these costs totalled in aggregate £5.9m (FY 2013; £7.6m) of which the contribution to the PACE deficit funding was £1.9m (FY 2013; £2.0m). The impact of any potential changes to contributions is assessed under the Issuer's risk management framework and internal economic assessment of solvency, including the ICA.

The Issuer's share of annual deficit contributions to PACE was reviewed and re-set in 2014. The annual cost of approximately £2m is not expected to alter materially in the near future. However, in circumstances, which may be outside the control of the Issuer, where other employers in PACE cease to participate in the pension scheme without satisfying their liabilities (for example due to insolvency) the Issuer's share of the deficit could increase to include liabilities that relate to those other employers.

Additionally, while the Issuer is not a participating employer in PACE, it has provided an additional guarantee to the PACE Trustee to meet its share of the pension obligations of CFSMS in the event of default by CFSMS.

Significant liabilities may arise for the Issuer as the guarantor of CFSMS upon the happening of an event, such as the winding up of the scheme or the insolvency of CFSMS. The liability triggered in these circumstances will be the Issuer's share of CFSMS's portion of the deficit at the time, calculated on the most conservative basis (i.e. the cost of buying out the scheme's liabilities in the insurance marker).

Consequently, increases in required contributions would reduce the Issuer's results of operations. Increases in the pension scheme deficit, or the Issuer's share of deficit contributions, the winding up of PACE or a default by CFSMS on its pension obligations, could adversely impact the Issuer's financial condition.

Group Risk

The Issuer's operations, results and implementation of strategy may be impacted where services are currently provided by other entities in the Co-operative Group

The Issuer is vulnerable to adverse market perception of the wider Co-operative Group and specific entities within the Co-operative Group. Changes which are undertaken within the Co-operative Group to address business issues have the potential to create significant strategic, reputational, regulatory, financial and operational risks for the Issuer.

The Issuer is provided with a number of services from entities within the Co-operative Group. The separation of entities and shared services from the Co-operative Group, (including the Co-operative Bank and Co-operative Insurance Society Life & Savings), has presented a number of risks to the Issuer including; continuity of service, technology service provision, data access, assets allocation, governance structures of CFSMS and the Co-operative Banking Group Limited, management of material service providers from within the Co-operative Group and contracts with third parties and treatment of stranded costs. All these have the potential to cause disruption to the Issuer's existing operations. The Issuer's ability to influence the separation of entities from the Co-operative Group is limited, in particular, in respect of the Co-operative Bank separation.

The Issuer currently shares with the Co-operative Bank (which is no longer part of the Co-operative Group) some IT services and the Co-operative Bank provides a limited number of IT services for the Issuer. There is a programme underway to separate IT operations, pursuant to which the Co-operative Bank is extracting relevant information and transferring such information to its own system. This presents a number of risks including disruption to services and associated reputational impacts.

The Issuer has an agreement to pay pensions contributions relating to staff employed by CFSMS that are assigned to work for the Issuer. This means that the Issuer is exposed to pension risk through PACE. The Issuer is exposed to the risk of CFSMS becoming insolvent. This would lead to operational disruption and financial loss for the Issuer in order to re-establish the services that had been previously supplied by CFSMS. In addition, if the insolvency of CFSMS were related to being unable to meet pension liabilities, then this could lead to increased pension costs for the Issuer, resulting in financial loss. See "*The Issuer may have increased costs or capital requirements as a consequence of revised valuation and/or changes in the treatment of the Co-operative Group pension scheme*" for further information on the pension risk.

FACTORS WHICH ARE MATERIAL FOR THE PURPOSE OF ASSESSING THE MARKET RISKS ASSOCIATED WITH THE NOTES

Risks relating to the structure of the Notes

The Notes are subject to early redemption at the option of the Issuer and an investor may not be able to reinvest the redemption proceeds at as effective a rate of return as that in respect of the Notes

The Notes may, subject as provided in Condition 5, be redeemed at the option of the Issuer on the Call Date and upon the occurrence of certain specified events relating to taxation (as more particularly specified in Condition 5.4(a) and (b)) or following the occurrence of a Capital Disqualification Event, in each case at their principal amount together with interest accrued but unpaid to (but excluding) the date of redemption and any Arrears of Interest.

The definition of Capital Disqualification Event is complex and includes circumstances where the Notes cease to qualify as Tier 2 Capital of the Issuer or all or any part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group), whether on a solo or group basis.

As discussed in further detail in the section of this Prospectus entitled "*Regulatory Overview – Recent and Future Developments*", the Solvency II framework for insurance companies will take effect from 1 January 2016. Although the delegated acts (which set out certain detailed provisions of the Solvency II regime) were published in the Official Journal on 17 January 2015 and entered into force on 18 January 2015, certain binding technical standards and guidance setting out the final rules have not yet been adopted, and the European Commission and the European Insurance and Occupational Pensions Authority (**EIOPA**) will continue to finalise certain aspect of the Solvency II regime during 2015.

Accordingly, there is a risk that, upon implementation of Solvency II in the United Kingdom or following any other change to the Relevant Rules, a Capital Disqualification Event may occur, which would entitle the Issuer to redeem the Notes early at their principal amount together with interest accrued but unpaid to (but excluding) the date of redemption and any Arrears of Interest.

The cash paid to investors upon such a redemption may be less than the then current market value of the Notes or the price at which investors purchased the Notes. Subject to the contractual and regulatory restrictions on doing so set out in the Conditions, the Issuer might be expected to redeem the Notes when its cost of borrowing for an instrument with a comparable regulatory capital treatment at the time is lower than the interest payable on them. At those times, an investor generally would not be able to reinvest the redemption proceeds at an effective interest rate as high as the interest payable on the Notes being redeemed and may only be able to do so at a significantly lower rate. Potential investors should consider reinvestment risk in the light of other investments available at that time.

The Notes are unsecured and subordinated obligations of the Issuer. On a winding-up of the Issuer, investors in the Notes may lose their entire investment in the Notes

The Issuer's payment obligations under the Notes will be unsecured and will be subordinated (i) on a winding-up of the Issuer and (ii) in the event that an administrator is appointed to the Issuer and gives notice that it intends to declare and distribute a dividend and, in each case, will rank junior to the claims of all policyholders and other unsubordinated creditors of the Issuer and to claims in respect of any subordinated indebtedness of the Issuer other than indebtedness which ranks, or is expressed to rank, *pari passu* with or junior to the Notes. Accordingly, the assets of the Issuer would be applied first in satisfying all senior-ranking claims in full, and payments would be made to holders of the Notes, *pro rata* and proportionately with payments made to holders of any other *pari passu* instruments (if any), only if and to the extent that there are any assets remaining after satisfaction in full of all such senior-ranking claims. If the Issuer's assets are insufficient to meet all its obligations to senior-ranking and *pari passu* creditors in full, the holders of the Notes will lose all or some of their investment in the Notes.

There is no restriction on the amount of securities which the Issuer may issue and which rank senior to, or *pari passu* with, the Notes and, accordingly, the Issuer may at any time incur further obligations (including by issue of further debt securities) which rank senior to, or *pari passu* with, the Notes. Consequently there can be no assurance that the current level of senior or *pari passu* debt of the Issuer will not change. The issue of any such securities may reduce the amount (if any) recoverable by Noteholders on a winding-up of the Issuer.

If the Issuer's financial condition deteriorates such that there is an increased risk that the Issuer may be wound-up or enter into administration, such circumstances can be expected to have a material adverse effect on the market price of the Notes. Investors in the Notes may find it difficult to sell their Notes in such circumstances, or may only be able to sell their Notes at a price which may be significantly lower than the price at which they purchased their Notes. In such a sale, investors may lose some or substantially all of their investment in the Notes, whether or not the Issuer is wound up or enters into administration.

Although the Notes may pay a higher rate of interest than comparable notes which are not subordinated, there is a material risk that an investor in the Notes will lose all or some of its investment should the Issuer become insolvent.

Payments by the Issuer are conditional upon the satisfaction of solvency requirements

All payments under or arising from the Notes and the Trust Deed (other than payments made to the Trustee in its personal capacity under the Trust Deed) shall be conditional upon the Issuer being solvent (as that term is described in Condition 2.2) at the time for payment by the Issuer, and no amount shall be payable under or arising from the Notes and the Trust Deed unless and until such time as the Issuer could make such payment and still be solvent immediately thereafter (the "**Solvency Condition**").

If any payment of interest, Arrears of Interest and/or principal cannot be made by the Issuer in compliance with the Solvency Condition, payment of such amounts will be mandatorily deferred by the Issuer, and non-payment of the amounts so deferred shall not constitute a default under the Notes or the Trust Deed for any purpose, including enforcement action against the Issuer.

Payments of interest on the Notes must in certain circumstances be deferred by the Issuer

The payment obligations of the Issuer under the Notes are conditional upon (i) there being no breach of the Solvency Condition (as described in Condition 2.2) at the time of such payment and no such breach occurring as a result of such payment and (ii) in the case of the payment of interest, there being no Regulatory Deficiency Interest Deferral Event (as defined in Condition 17) at the time of such payment and no such event occurring as a result of such payment. Any amounts of principal, interest, Arrears of Interest and any other amounts in respect of the Notes which cannot be paid on the scheduled payment date by virtue of such provisions must be deferred by the Issuer, and non-payment of the amounts so deferred shall not constitute a default under the Notes or the Trust Deed for any purpose, including enforcement action against the Issuer.

Any interest in respect of the Notes so deferred will, so long as the same remains unpaid, constitute Arrears of Interest. Arrears of Interest will not themselves bear interest. The holders of the Notes have no right to require payment of Arrears of Interest, and Arrears of Interest will become payable only at the discretion of the Issuer or upon the earliest of the dates set out in Condition 4.2 (a) to (c) (*Arrears of Interest*).

The definition of Regulatory Deficiency Interest Deferral Event is complex and includes not only circumstances relating to the solvency position of the Issuer under Solvency II but also circumstances where an insurance undertaking within the CISGIL Group is in an insolvent winding-up or administration or is in breach of its solvency capital requirement under Solvency II and the requirements of Solvency II and/or the Relevant Rules (as defined in Condition 17), which themselves are subject to finalisation and subsequent amendment.

Any actual or anticipated deferral of interest can be expected to have a material adverse effect on the market price of the Notes. Investors in the Notes may find it difficult to sell their Notes in such circumstances, or may only be able to sell their Notes at a price which may be significantly lower than the price at which they purchased their Notes. In such a sale, investors may lose some or substantially all of their investment in the Notes. In addition, as a result of the deferral provisions of the Notes, the market price of the Notes may be more volatile than the market prices of other securities or instruments that do not require deferral of interest and may be more sensitive generally to adverse changes in the Issuer's financial condition.

Redemption payments under the Notes must in certain circumstances be deferred by the Issuer

The payment obligations by the Issuer under the Notes are conditional upon (i) there being no breach of the Solvency Condition (as described in Condition 2.2) at the time of such payment and no such breach occurring as a result of such payment, (ii) there being no Regulatory Deficiency Redemption Deferral Event (as defined in Condition 17) at the time of such payment and no such event occurring as a result of such payment and (iii) notification to, or consent or non-objection from, the Relevant Regulator (to the extent then required by the Relevant Regulator or the Relevant Rules). Any amounts of principal and any other amounts in respect of the Notes which cannot be paid on the scheduled payment date by virtue of such provisions must be deferred by the Issuer, and non-payment of the amounts so deferred shall not constitute a default under the Notes or the Trust Deed for any purpose, including enforcement action against the Issuer. If redemption of the Notes is deferred, the Notes will only become due for redemption in the circumstances described in Condition 5.1(d) and (e) (*Redemption, Substitution, Variation and Purchase – Redemption*).

The definition of Regulatory Deficiency Redemption Deferral Event is complex and includes not only circumstances relating to the solvency position of the Issuer under Solvency II but also circumstances where an insurance undertaking within the Group is in an insolvent winding-up or administration or is in breach of its solvency capital requirement under Solvency II and the requirements of Solvency II and/or the Relevant Rules, which themselves are subject to finalisation and subsequent amendment.

Any actual or anticipated deferral of redemption can be expected to have a material adverse effect on the market price of the Notes. Investors in the Notes may find it difficult to sell their Notes in such circumstances, or may only be able to sell their Notes at a price which may be significantly lower than the price at which they purchased their Notes. In such a sale, investors may lose some or substantially all of their investment in the Notes. In addition, as a result of the deferral provisions of the Notes, the market price of the Notes may be more volatile than the market prices of other securities or instruments that do not require deferral of principal, and may be more sensitive generally to adverse changes in the Issuer's financial condition.

The terms of the Notes may be modified, or the Notes may be substituted, by the Issuer without the consent of the Noteholders in certain circumstances, subject to certain restrictions

In the event of certain specified events relating to taxation or following the occurrence of a Capital Disqualification Event, the Issuer may (subject to certain conditions) at any time substitute all (but not some only) of the Notes for, or vary the terms of the Notes so that they remain or become (as applicable), Qualifying Dated Tier 2 Securities, without the consent of the Noteholders.

Qualifying Dated Tier 2 Securities must have terms not materially less favourable to holders than the terms of the Notes, as reasonably determined by the Issuer in consultation with an independent investment bank of international standing. However, there can be no assurance that, due to the particular circumstances of a holder of Notes, such Qualifying Dated Tier 2 Securities will be as favourable to each investor in all respects or that, if it were entitled to do so, a particular investor would make the same determination as the Issuer as to whether the terms of the Qualifying Dated Tier 2 Securities are not materially less favourable to holders than the terms of the Notes.

The terms of the Notes may be modified with the consent of specified majorities of the Noteholders at a duly convened meeting, and the Trustee may consent to certain modifications to the Notes, or substitution of the Issuer, without the consent of the Noteholders

The Trust Deed constituting the Notes contains provisions for calling meetings of Noteholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Noteholders, including Noteholders who did not attend and vote at the relevant meeting and Noteholders who voted in a manner contrary to the majority. The Trust Deed constituting the Notes also provides that, subject to the prior consent of the Relevant Regulator being obtained (to the extent that such consent is required), the Trustee may (except as set out in the Trust Deed), without the consent of Noteholders, agree to certain modifications of, or to the waiver or authorisation of any breach or proposed breach of, any of the provisions of the Notes or to the substitution of another company as principal debtor under the Notes in place of the Issuer in the circumstances described in Condition 10.

Restricted remedy for non-payment when due

In accordance with the current requirements for eligible Tier 2 Capital, the sole remedy against the Issuer available to the Trustee or (where the Trustee has failed to proceed against the Issuer as provided in the Conditions) any Noteholder for recovery of amounts which have become due in respect of the Notes will be the institution of proceedings for the winding-up of the Issuer and/or proving in such winding-up or administration and/or claiming in the liquidation of the Issuer. In particular, a deferral of payments as described above shall not constitute a default under the Notes or the Trust Deed for any purpose, including enforcement action against the Issuer.

Risks relating to the Notes generally

Payments on the Notes may be subject to FATCA Withholding

Certain provisions of U.S. law, commonly known as "FATCA", impose a new reporting and withholding regime with respect to (i) certain U.S. source payments, (ii) gross proceeds from the disposition of property that can produce U.S. source interest and dividends and (iii) certain payments made by, and financial accounts held with, entities that are classified as foreign financial institutions for purposes of FATCA. Whilst the Notes are in global form and held within Euroclear or Clearstream, Luxembourg (together, the **ICSDs**), in all but the most remote circumstances, it is not expected that FATCA will affect the amount of any payment received by the ICSDs. However, FATCA may affect payments made to custodians or intermediaries (including any clearing system other than the ICSDs) in the payment chain leading to the ultimate investor if any such custodian or intermediary generally is unable to receive payments free of FATCA withholding. It also may affect payments to any ultimate investor that is a financial institution that is not entitled to receive payments free of withholding under FATCA, or an ultimate investor that fails to provide its broker (or other custodian or intermediary from which it receives a payment) with any information, forms, other documentation or consents that may be necessary for the payments to be made free of FATCA withholding. Investors should choose the custodians or intermediaries with care (to ensure each is compliant with FATCA or other laws or agreements related to FATCA, including any legislation implementing an intergovernmental agreement entered into pursuant to FATCA, if applicable), provide each custodian or intermediary with any information, forms, other documentation or consents that may be necessary for such custodian or intermediary to make a payment free of FATCA withholding. Investors should consult their own tax adviser to obtain a more detailed explanation of FATCA and how FATCA may affect them. The Issuer's obligations under the Notes are discharged once it has paid the Common Depositary for the ICSDs and the Issuer has therefore no responsibility for any amount thereafter transmitted through hands of the ICSDs and custodians or intermediaries.

EU Savings Directive

Under Council Directive 2003/48/EC on the taxation of savings income (the **Savings Directive**), member states of the European Economic Area (**Member States**) are required to provide to the tax authorities of other Member States details of payments of interest or similar income paid or secured by a person established in a Member State to or for the benefit of an individual resident in another Member State or certain limited types of entities established in another Member State.

On 24 March 2014, the Council of the European Union adopted a Council Directive (the **Amending Directive**) amending and broadening the scope of the requirements described above. Member States are required to apply these new requirements from 1 January 2017. The Amending Directive will expand the range of payments covered by the Savings Directive, in particular to include additional types of income payable on securities. The Amending Directive will also expand the circumstances in which payments that indirectly benefit an individual resident in a Member State must be reported. This approach will apply to payments made to, or secured for, persons, entities or legal arrangements (including trusts) where certain conditions are satisfied, and may in some cases apply where the person, entity or arrangement is established or effectively managed outside of the European Union.

For a transitional period, Austria is required (unless during that period it elects otherwise) to operate a withholding system in relation to such payments. The changes referred to above will broaden the types of payments subject to withholding in Austria if it still operates a withholding system when they are implemented.

The end of the transitional period is dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries. A number of other non-EU countries and territories including Switzerland have adopted similar measures (a withholding system in the case of Switzerland).

If a payment were to be made or collected through a Member State which has opted for a withholding system and an amount of, or in respect of, tax were to be withheld from that payment, neither the Issuer nor any Paying Agent as defined in the Conditions nor any other person would be obliged to pay additional amounts with respect to any Note as a result of the imposition of such withholding tax.

The Issuer is required to maintain a Paying Agent in a Member State that is not obliged to withhold or deduct tax pursuant to the Savings Directive.

Change of law

The Conditions are based on English law and regulation in effect as at the date of issue of the Notes. No assurance can be given as to the impact of any possible judicial decision or change to English law, regulation or administrative practice after the date of issue of the Notes.

Integral multiples of less than £100,000

The denomination of the Notes is £100,000 and integral multiples of £1,000 in excess thereof. Accordingly, it is possible that the Notes may be traded in the clearing systems in amounts in excess of £100,000 that are not integral multiples of £100,000. Should Certificates be required to be issued, they will be issued in principal amounts of £100,000 and higher integral multiples of £1,000 but will in no circumstances be issued to Noteholders who hold Notes in the relevant clearing system in amounts that are less than £100,000.

If Certificates are issued, Noteholders should be aware that definitive Notes which have a denomination that is not an integral multiple of £100,000 may be illiquid and difficult to trade.

Investors must rely on the procedures of Euroclear and Clearstream, Luxembourg for transfer, payment and communication with the Issuer

The Notes will be represented by the Global Certificate upon issue. The Global Certificate will be registered in the name of a nominee for the Common Depositary for Euroclear and Clearstream, Luxembourg. Except in the circumstances described in the Global Certificate, investors will not be entitled to receive definitive Notes. Euroclear and Clearstream, Luxembourg will maintain records of the beneficial interests in the Global Certificate. While the Notes are represented by the Global Certificate, investors will be able to trade their beneficial interests only through Euroclear or Clearstream, Luxembourg and will receive and provide any notices only through Euroclear or Clearstream, Luxembourg.

While the Notes are represented by the Global Certificate, the Issuer will discharge its payment obligations under the Notes by making payments to or to the order of the registered holder as nominee for the Common Depositary for Euroclear or Clearstream, Luxembourg for distribution to their accountholders. A holder of a beneficial interest in the Global Certificate must rely on the procedures of Euroclear and Clearstream, Luxembourg to receive payments under the Notes. The Issuer has no responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in the Global Certificate.

Risks related to the market generally

The secondary market generally

The Notes have no established trading market when issued, and one may never develop. If a market does develop it may not be liquid. In addition, the Notes will be unrated on issue, and the Issuer does not expect to seek a credit rating for the Notes at any time, which may limit the liquidity of the Notes in the secondary market. Investors may not be able to sell their Notes easily or at prices that will provide them with a yield comparable to similar investments that have a developed secondary market and/or which are rated. Illiquidity may have a severely adverse effect on the market value of the Notes.

If the Issuer's financial condition deteriorates such that there is an increased risk that the Issuer may be wound-up or enter into administration, or if at any time there is any actual or anticipated deferral of interest or redemption in accordance with the Conditions, such circumstances can be expected to have a material adverse effect on the market price of the Notes. Investors in the Notes may find it difficult to sell their Notes in such circumstances, or may only be able to sell their Notes at a price which may be significantly lower than the price at which they purchased their Notes. In such a sale, investors may lose some or substantially all of their investment in the Notes.

Exchange rate risks and exchange controls

The Issuer will pay principal and interest on Notes in sterling. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the **Investor's Currency**) other than sterling. These include the risk that exchange rates may significantly change (including changes due to devaluation of sterling or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to sterling would decrease (1) the Investor's Currency-equivalent yield on the Notes, (2) the Investor's Currency-equivalent value of the principal payable on the Notes and (3) the Investor's Currency-equivalent market value of the Notes.

Government and monetary authorities may impose (as some have done in the past) exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal.

Interest rate risks

Prior to the Reset Date the Notes bear a fixed rate of interest, which involves the risk that subsequent increases in market interest rates may adversely affect the market value of Notes.

From and including the Reset Date, the rate of interest will be reset by reference to the mid-swap rates for Swap transactions with a maturity equal to five years (as more particularly described in Condition 3). The reset rate of interest may adversely affect the yield of such Notes and the secondary market for and the market value of the Notes.

TERMS AND CONDITIONS OF THE NOTES

The following (other than paragraphs in italics) are the Terms and Conditions of the Notes, which will be endorsed on the Certificates issued in respect of the Notes.

The £70,000,000 Callable Dated Deferrable Tier Two Notes due 2025 (the "**Notes**", which expression shall, unless the context otherwise requires, include any further notes issued pursuant to Condition 14 and forming a single series with the Notes) of CIS General Insurance Limited (the "**Issuer**") are constituted by a trust deed dated 8 May 2015 (the "**Trust Deed**") between the Issuer and BNY Mellon Corporate Trustee Services Limited (the "**Trustee**", which expression shall include all persons for the time being the trustee or trustees under the Trust Deed) as trustee for the holders of the Notes (the "**Noteholders**"). These terms and conditions (the "**Conditions**") include summaries of, and are subject to, the detailed provisions of the Trust Deed. An Agency Agreement dated 8 May 2015 (the "**Agency Agreement**") has been entered into in relation to the Notes between the Issuer, the Trustee, The Bank of New York Mellon (Luxembourg) S.A. as registrar and transfer agent (the "**Registrar**" and the "**Transfer Agent**" which expressions shall include any successor registrar or successor transfer agent respectively), The Bank of New York Mellon, London Branch as principal paying agent and the calculation agent (the "**Principal Paying Agent**" and the "**Calculation Agent**" which expressions shall include any successor principal paying agents or calculation agents respectively) and any other paying agent(s) for the time being appointed under the Agency Agreement (together with the Principal Paying Agent, the "**Paying Agents**", which expression shall include any successor or additional paying agents). References to "**Agents**" are to the Registrar, the Transfer Agent, the Calculation Agent and the Paying Agents and any reference to an "**Agent**" is to any one of them. Copies of the Trust Deed and the Agency Agreement are available for inspection during usual business hours and upon reasonable notice at the registered office of the Trustee (presently at One Canada Square London, E14 5AL) and at the specified office of each of the Agents.

The Noteholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and are deemed to have notice of those provisions applicable to them of the Agency Agreement.

1. Form, Denomination, Title and Transfer

1.1 Form and Denomination

The Notes are issued in registered form in denominations of £100,000 and integral multiples of £1,000 in excess thereof. A note certificate (each a "**Certificate**") will be issued to each Noteholder in respect of its registered holding of Notes. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the register of Noteholders which the Issuer will procure to be kept by the Registrar (the "**Register**").

1.2 Title

Title to the Notes passes only by registration in the Register. The holder of any Note will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership or writing on it, or the previous theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder. In these Conditions, "**Noteholder**" and (in relation to a Note) "**holder**" means the person in whose name a Note is registered in the Register.

1.3 Transfers

A Note may be transferred by depositing the Certificate issued in respect of that Note, with the form of transfer on the back duly completed and signed, at the specified office of the Registrar or any of the Agents.

1.4 Delivery of new Certificates

Each new Certificate to be issued upon transfer of Notes will, within five Business Days of receipt by the Registrar or the relevant Agent of the duly completed form of transfer endorsed on the relevant Certificate, be mailed by uninsured mail at the risk of the holder entitled to the Note to the address specified in the form of transfer.

Except in limited circumstances described in this Prospectus (see "Summary Of Provisions Relating To The Notes Whilst In Global Form –Registration of Title"), owners of interests in the Notes will not be entitled to receive physical delivery of Certificates.

Where some but not all of the Notes in respect of which a Certificate is issued are to be transferred a new Certificate in respect of the Notes not so transferred will, within five Business Days of receipt by the Registrar or the relevant Agent of the original Certificate, be mailed by uninsured mail at the risk of the holder of the Notes not so transferred to the address of such holder appearing on the Register or as specified in the form of transfer.

1.5 Formalities free of charge

Registration of transfer of Notes will be effected without charge by or on behalf of the Issuer or any Agent but upon payment (or the giving of such indemnity as the Issuer or any Agent may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer.

1.6 Closed Periods

No Noteholder may require the transfer of a Note to be registered during the period of 15 days ending on the due date for any payment of principal or interest on that Note or during the period following delivery of a notice of a voluntary payment of Arrears of Interest in accordance with Condition 4.2 and Condition 15 and ending on the date referred to in such notice as having been fixed for such payment of Arrears of Interest.

1.7 Regulations

All transfers of Notes and entries on the Register will be made subject to the detailed regulations concerning transfer of Notes scheduled to the Trust Deed. The regulations may be changed by the Issuer with the prior written approval of the Registrar and the Trustee. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests one.

2. Status

2.1 Ranking

The Notes constitute direct, unsecured and subordinated obligations of the Issuer and rank *pari passu* and without any preference among themselves. In the event of the winding-up of the Issuer (other than an Approved Winding-up) or the appointment of an administrator of the Issuer where the administrator has given notice that it intends to declare and distribute a dividend, the payment obligations of the Issuer under or arising from the Notes and the Trust Deed, including any Arrears of Interest and any damages awarded for breach of any obligations in respect of the Notes, shall be subordinated in the manner provided in the Trust Deed to the claims of all Senior Creditors of the Issuer, but shall rank at least *pari passu* with all other subordinated obligations of the Issuer which constitute, or would but for any applicable limitation on the amount of such capital constitute, Lower Tier 2 Capital (issued prior to Solvency II Implementation) or Tier 2 Capital (issued on or after Solvency II Implementation) ("**Pari Passu Securities**") and shall rank in priority to the claims of holders of: (i) all obligations of the Issuer which constitute, or would but for any applicable limitation on the amount of such capital constitute, Upper Tier 2 Capital issued prior to Solvency II Implementation; (ii) all obligations of the Issuer which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 1 Capital (including, without limitation, by virtue of the operation of any grandfathering provisions under any Relevant Rules); and (iii) all classes of share capital of the Issuer (together, the "**Junior Securities**").

Nothing in this Condition 2.1 shall affect or prejudice the payment of the costs, fees, charges, expenses, liabilities or remuneration of the Trustee under the Trust Deed or the rights and remedies of the Trustee in respect thereof.

2.2 Solvency Condition

Without prejudice to Condition 2.1 above, all payments under or arising from the Notes and the Trust Deed (other than payments made to the Trustee in its personal capacity under the Trust Deed) shall be conditional upon the Issuer being solvent at the time for payment by the Issuer, and no amount shall be payable under or arising from the Notes and the Trust Deed unless and until such time as the Issuer could make such payment and still be solvent immediately thereafter (the "**Solvency Condition**").

For the purposes of this Condition 2.2, the Issuer will be solvent if (i) it is able to pay its debts owed to Senior Creditors and Pari Passu Creditors as they fall due and (ii) its Assets exceed its Liabilities. A certificate as to solvency of the Issuer signed by two Directors or, if there is a winding-up or administration of the Issuer, by two directors or authorised signatories of, the liquidator or, as the case may be, the administrator of the Issuer shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate without liability to any person.

2.3 Set-off, etc.

Subject to applicable law, no holder of the Notes may exercise, claim or plead any right of set-off, compensation or retention in respect of any amount owed to it by the Issuer arising under or in connection with the Notes and each holder of the Notes shall, by virtue of being the holder of any Note, be deemed to have waived all such rights of set-off, compensation or retention. Notwithstanding the preceding sentence, if any of the amounts owing to any holder of the Notes by the Issuer is discharged by set-off, such holder shall, unless such payment is prohibited by law, immediately pay an amount equal to the amount of such discharge to the Issuer or, in the event of its winding-up or administration, the liquidator or administrator, as appropriate, of the Issuer for payment to the Senior Creditors in respect of amounts owing to them by the Issuer, and, until such time as payment is made, shall hold an amount equal to such amount in trust for the Issuer, or the liquidator or administrator, as appropriate, of the Issuer (as the case may be), for payment to the Senior Creditors in respect of amounts owing to them by the Issuer and accordingly any such discharge shall be deemed not to have taken place.

As used in this Condition 2, the expression "**obligations**" includes any direct or indirect obligations of the Issuer and whether by way of guarantee, indemnity, other contractual support arrangement or otherwise and regardless of name or designation.

On a winding-up of the Issuer, there may be no surplus assets available to meet the claims of the Noteholders after the claims of the parties ranking senior to the Noteholders (as provided in Condition 2) have been satisfied.

3. Interest

3.1 Interest Payment Dates

Subject to Condition 2.2 and Condition 4, each Note bears interest on its outstanding principal amount from (and including) the Issue Date at the applicable Interest Rate payable quarterly in arrear on 8 May, 8 August, 8 November and 8 February of each year, the first payment to be made on 8 August 2015 (each an "**Interest Payment Date**"). The first payment shall be in respect of the period from (and including) the Issue Date to (but excluding) 8 August 2015, and thereafter for each successive period from (and including) an Interest Payment Date to (but excluding) the next Interest Payment Date.

3.2 Interest Accrual

Each Note will cease to bear interest from (and including) its due date for redemption unless, upon due presentation, payment of the principal in respect of the Note is improperly withheld or refused or unless default is otherwise made in respect of payment, in which event interest shall continue to accrue as provided in the Trust Deed.

3.3 Calculation of Interest

Where it is necessary to compute an amount of interest in respect of any Note, such interest shall be calculated on the basis of (a) the actual number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Issue Date) to (but excluding) the relevant payment date divided by (b) four times the actual number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Issue Date) to (but excluding) the next (or first) scheduled Interest Payment Date.

Interest shall be calculated per £1,000 in principal amount of the Notes (the "**Calculation Amount**") by applying the applicable Interest Rate to such Calculation Amount, multiplying the resulting figure by the day count fraction described in the immediately preceding paragraph and rounding the resultant figure to two decimal places (with 0.005 being rounded up). The amount of interest payable in respect of a Note shall be calculated by multiplying the amount of interest per Calculation Amount determined as aforesaid by the specified denomination of such Note and dividing the resulting figure by £1,000.

3.4 Initial Fixed Interest Rate

For the Initial Fixed Rate Interest Period, the Interest Rate will be 12 per cent. per annum[1] (the "**Initial Fixed Interest Rate**").

3.5 Reset Interest Rate

For the Reset Period, the Interest Rate will be reset (the "**Reset Rate of Interest**") in accordance with this Condition 3 on the Reset Date. The Reset Rate of Interest will be determined by the Calculation Agent on the Reset Determination Date as the sum of the Reset Reference Rate plus the Margin, converted from a semi-annual rate to a quarterly rate in accordance with market convention (rounded to three decimal places, with 0.0005 rounded down.

3.6 Determination of Reset Rate of Interest

The Calculation Agent will, as soon as practicable after 11.00 a.m. (London time) on the Reset Determination Date, determine the Reset Rate of Interest in respect of the Reset Period.

3.7 Publication of Reset Rate of Interest

The Issuer shall cause notice of the Reset Rate of Interest determined in accordance with this Condition 3 to be given to the Trustee, the Paying Agents, any stock exchange on which the Notes are for the time being listed or admitted to trading and, in accordance with Condition 15, the Noteholders, in each case as soon as practicable after its determination but in any event not later than the fourth Business Day thereafter.

3.8 Calculation Agent

The name of the initial Calculation Agent appointed by the Issuer and its initial specified office is set out at the end of these Conditions.

The Issuer may, with the prior written approval of the Trustee, from time to time replace the Calculation Agent with another leading investment, merchant or commercial bank or financial institution in London. If the Calculation Agent is unable or unwilling to continue to act as the Calculation Agent or fails duly to determine the Reset Rate of Interest as provided in Condition 3.5 and Condition 3.6, the Issuer shall forthwith appoint another leading investment, merchant or commercial bank or financial institution in London approved in writing by the Trustee to act as such in its place. The Calculation Agent may not resign its duties or be removed without a successor having been appointed as aforesaid.

3.9 Determinations of Calculation Agent Binding

All notifications, opinions, determinations, certificates, calculations, quotations and decisions given, expressed, made or obtained for the purposes of this Condition 3, by the Calculation Agent shall (in the absence of manifest error) be binding on the Issuer, the Calculation Agent, the Trustee, the Paying Agents and all Noteholders and (in the absence of wilful default or negligence) no liability to the Issuer shall attach to the

[1] being the sum of the Margin and the semi-annual mid-swap rate for swap transactions in pounds sterling (with a maturity equal to 5 years) as displayed on the Screen Page at 11.00 a.m. (London time) on 1 May 2015, converted from a semi-annual rate to a quarterly rate in accordance with market convention (rounded to three decimal places, with 0.0005 rounded down)

Calculation Agent in connection with the exercise or non-exercise by it of any of its powers, duties and discretions.

4. Deferral of Payments

4.1 Mandatory Deferral of Interest

Payment of interest on the Notes will be mandatorily deferred on each Mandatory Interest Deferral Date. The Issuer shall notify the Trustee and the Principal Paying Agent in writing and notify the Noteholders in accordance with Condition 15 no later than 5 Business Days prior to an Interest Payment Date (or as soon as reasonably practicable if a Regulatory Deficiency Interest Deferral Event occurs less than 5 Business Days prior to an Interest Payment Date) if a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or if a Regulatory Deficiency Interest Deferral Event would occur on the Interest Payment Date if payment of interest was made, specifying the Regulatory Deficiency Interest Deferral Event that has occurred or would occur if payment were made and stating that interest will not be paid because a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or would occur, (provided that, for the avoidance of doubt, any delay in giving such notice shall not result in such interest becoming due and payable on the relevant Mandatory Interest Deferral Date).

A certificate signed by two Directors confirming that (a) a Regulatory Deficiency Interest Deferral Event has occurred and is continuing, or would occur if payment of interest on the Notes were to be made or (b) a Regulatory Deficiency Interest Deferral Event has ceased to occur and/or payment of interest on the Notes would not result in a Regulatory Deficiency Interest Deferral Event occurring, shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate without liability to any person.

Notwithstanding any other provision in these Conditions or in the Trust Deed, the deferral of any payment of interest on a Mandatory Interest Deferral Date in accordance with this Condition 4.1 or in accordance with Condition 2.2 will not constitute a default by the Issuer and will not give Noteholders or the Trustee any right to accelerate repayment of the Notes or to take any enforcement action under the Notes or the Trust Deed.

4.2 Arrears of Interest

Any interest in respect of the Notes not paid on an Interest Payment Date as a result of the obligation on the Issuer to defer pursuant to Condition 4.1 or due to the operation of the Solvency Condition contained in Condition 2.2, together with any other interest in respect of the Notes not paid on an earlier Interest Payment Date shall, so long as the same remains unpaid, constitute "**Arrears of Interest**". Arrears of Interest shall not themselves bear interest.

Any Arrears of Interest may (subject to Condition 2.2 and (to the extent then required by the Relevant Regulator or the Relevant Rules) to any notifications to, or consent or non-objection from, the Relevant Regulator), be paid in whole or in part at any time (provided that at such time a Regulatory Deficiency Interest Deferral Event is not subsisting and would not occur if payment of such Arrears of Interest was made) upon the expiry of not less than seven days' notice to such effect given by the Issuer to the Trustee and the Principal Paying Agent in writing and to the Noteholders in accordance with Condition 15, and in any event will become due and payable (subject, in the case of (a) and (c) below, to Condition 2.2 and (to the extent then required by the Relevant Regulator or the Relevant Rules) any notifications to, or consent or non-objection from, the Relevant Regulator) in whole (and not in part) upon the earliest of the following dates:

(a) the next Interest Payment Date which is not a Mandatory Interest Deferral Date; or

(b) the date on which an order is made or a resolution is passed for the winding-up of the Issuer (other than an Approved Winding-up) or the date on which any administrator of the Issuer gives notice that it intends to declare and distribute a dividend; or

(c) the date fixed for any redemption or purchase of Notes by or on behalf of the Issuer or any of its Subsidiaries pursuant to Condition 5.

5. Redemption, Substitution, Variation and Purchase

5.1 Redemption

(a) Subject to Condition 2.2, Condition 5.1(b) below and to compliance by the Issuer with regulatory rules including (to the extent then required by the Relevant Regulator or the Relevant Rules) on notification to, or consent or non-objection from, the Relevant Regulator, and provided that such redemption is permitted under the Relevant Rules applicable from time to time to the Issuer, unless previously redeemed or purchased and cancelled as provided below each Note shall be redeemed on the Maturity Date at its principal amount together with Arrears of Interest, if any, and any other interest accrued to (but excluding) the date of redemption in accordance with these Conditions.

(b) No Notes shall be redeemed on the Maturity Date pursuant to Condition 5.1(a) or prior to the Maturity Date pursuant to Condition 5.3, Condition 5.4 or Condition 5.5 if a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if redemption is made on, if Condition 5.1(a) applies, the Maturity Date or, if Condition 5.3, Condition 5.4 or Condition 5.5 applies, any date specified for redemption in accordance with such Conditions.

(c) If the Notes are not to be redeemed on the Maturity Date pursuant to Condition 5.1(a) or on any scheduled redemption date pursuant to Condition 5.3, Condition 5.4 or Condition 5.5 as a result of circumstances where:

   (i) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if the Notes were redeemed on such date;

   (ii) the Solvency Condition would not be satisfied on such date and immediately after the redemption; or

(iii) the Relevant Regulator does not consent to the redemption (to the extent that consent is then required by the Relevant Regulator or the Relevant Rules) or the Relevant Regulator objects to the redemption or such redemption otherwise cannot be effected in compliance with the Relevant Rules on such date,

the Issuer shall notify the Trustee and the Principal Paying Agent in writing and notify the Noteholders in accordance with Condition 15 no later than 5 Business Days prior to the Maturity Date or the date specified for redemption in accordance with Condition 5.3, Condition 5.4 or Condition 5.5, as applicable, that the Notes shall not be redeemed on such date and a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if redemption is made or the circumstances described in Condition 5.1(c)(ii) or (iii) apply, (or as soon as reasonably practicable if the relevant circumstance requiring redemption to be deferred arises, or is determined, less than 5 Business Days prior to the relevant redemption date).

(d) If redemption of the Notes does not occur on the Maturity Date or, as appropriate, the date specified in the notice of redemption by the Issuer under Condition 5.3, Condition 5.4 or Condition 5.5 as a result of Condition 5.1(b) above or the Relevant Regulator does not consent to the redemption (to the extent that consent is then required by the Relevant Regulator or the Relevant Rules) or the Relevant Regulator objects to the redemption or such redemption otherwise cannot be effected in compliance with the Relevant Rules on such date, subject (in the case of (i) and (ii) below only) to Condition 2.2 and (to the extent then required by the Relevant Regulator or the Relevant Rules) to any notifications to, or consent or non-objection from, the Relevant Regulator, such Notes shall be redeemed at their principal amount together with Arrears of Interest, if any, and any other interest accrued to (but excluding) the date of redemption, upon the earliest of:

(i) (in the case of a failure to redeem due to the operation of Condition 5.1(b) only) the date falling 10 Business Days after the date the Regulatory Deficiency Redemption Deferral Event has ceased (unless, on such 10th Business Day, a further Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or redemption of the Notes on such date would result in a Regulatory Deficiency Redemption Deferral Event occurring, in which case the provisions of Condition 5.1(b), Condition 5.1(c) and this Condition 5.1(d) shall apply *mutatis mutandis* to determine the due date for redemption); or

(ii) the date falling 10 Business Days after the Relevant Regulator has agreed to the repayment or redemption of the Notes; or

(iii) the date on which an order is made or a resolution is passed for the winding-up of the Issuer (other than an Approved Winding-up) or the date on which any administrator of the Issuer gives notice that it intends to declare and distribute a dividend.

(e) If Condition 5.1(b) does not apply, but redemption of the Notes does not occur on the Maturity Date or, as appropriate, the date specified in the notice of redemption by the Issuer under Condition 5.3, Condition 5.4 or Condition 5.5 as a result of the Solvency Condition not being satisfied at such time and immediately after such payment, subject (to the extent then required by the Relevant Regulator or the Relevant Rules) to any notifications to, or consent or non-objection from, the Relevant Regulator, such Notes shall be redeemed at their principal amount together with accrued interest and any Arrears of Interest on the 10th Business Day immediately following the day that (i) the Issuer is solvent for the purposes of Condition 2.2 and (ii) redemption of the Notes would not result in the Issuer ceasing to be solvent for the purposes of Condition 2.2, provided that if on such Business Day specified for redemption a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing, or would occur if the Notes were to be redeemed, or if the Solvency Condition would not be satisfied on such date and immediately after the redemption, then the Notes shall not be redeemed on such date and Condition 2.2 and Condition 5.1(d) shall apply *mutatis mutandis* to determine the date of the redemption of the Notes.

(f) A certificate signed by two Directors confirming that (i) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing, or would occur if redemption of the Notes were to be made or (ii) a Regulatory Deficiency Redemption Deferral Event has ceased to occur and/or redemption of the Notes would not result in a Regulatory Deficiency Redemption Deferral Event occurring or (iii) that any of the circumstances described in Condition 5.1(c)(ii) or (iii) apply, shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate without liability to any person.

(g) Notwithstanding any other provision in these Conditions or in the Trust Deed, the deferral of redemption of the Notes in accordance with Condition 2.2 or this Condition 5 will not constitute a default by the Issuer and will not give Noteholders or the Trustee any right to accelerate repayment of the Notes or take any other action under the Notes or the Trust Deed.

5.2 Conditions to Redemption, Substitution, Variation or Purchase

Any redemption, substitution, variation or purchase of the Notes pursuant to this Condition 5 is subject to the Issuer having complied with relevant legal or regulatory requirements including (to the extent then required by the Relevant Regulator or the Relevant Rules) rules on notification to, or consent or non-objection from, the Relevant Regulator and being in continued compliance with the Regulatory Capital Requirements applicable to it at the relevant time and, in the case of a redemption or purchase that is prior to the Call Date, to such redemption or purchase being funded out of the proceeds of a new issuance of capital of at least the same quality as the Notes and being otherwise permitted under the Relevant Rules.

A certificate signed by two Directors confirming such compliance shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct, conclusive and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate without liability to any person.

In the case of a redemption that is prior to the Call Date, the Issuer shall deliver to the Trustee a certificate signed by two Directors stating that it would have been reasonable for the Issuer to conclude, judged at the time of the issue of the Notes, that the circumstance entitling the Issuer to exercise the right of redemption was unlikely to occur. Such certificate shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct, conclusive and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate without liability to any person.

5.3 Redemption at the Option of the Issuer on the Call Date

The Issuer may, subject to Condition 2.2, Condition 5.1(b) and Condition 5.2 and having given not less than 30 nor more than 60 days' notice to the Noteholders in accordance with Condition 15, the Trustee, the Principal Paying Agent and the Registrar (which notice shall be irrevocable), redeem in accordance with these Conditions all, but not some only, of the Notes on the Call Date. The Notes will be redeemed at their principal amount, together with Arrears of Interest, if any, and any other unpaid interest accrued to (but excluding) the date of redemption in accordance with these Conditions.

Upon expiry of such notice the Issuer shall (subject to Condition 2.2, Condition 5.1(b), Condition 5.1(c), Condition 5.1(d) and Condition 5.2) redeem the Notes.

5.4 Redemption, Substitution or Variation Due to Taxation

If immediately prior to the giving of the notice referred to below:

(a) as a result of a change in or proposed change in, or amendment or proposed amendment to, the laws or regulations of the Relevant Jurisdiction (as defined in Condition 7), including any treaty to which the Relevant Jurisdiction is a party, or any change in the application or official interpretation of such laws, including a decision of any court or tribunal, or any interpretation or pronouncement by any relevant tax authority that provides for a position with respect to such laws or regulations that differs from the previously generally accepted position in relation to similar transactions (in respect of securities similar to the Notes and which are capable of constituting Lower Tier 2 Capital under the rules applicable at issuance) or which differs from any specific written confirmation given by a tax authority in respect of the Notes, which change or amendment becomes, or would become, effective, or in the case of a change or proposed change in law if such change is enacted (or, in the case of a proposed change, is expected to be enacted), on or after the Issue Date of the Notes (each a "**Tax Law Change**"), in making any payments on the Notes, the Issuer has paid or will or would on the next payment date be required to pay Additional Amounts on the Notes and the Issuer cannot avoid the foregoing in connection with the Notes by taking measures reasonably available to it; or

(b) as a result of a Tax Law Change, in respect of the Issuer's obligation to make any payment of interest on the next following Interest Payment Date, (i) the Issuer would not be entitled to claim a deduction in respect of computing its taxation liabilities in the Relevant Jurisdiction, or such entitlement is materially reduced or deferred; or (ii) the Issuer would not to any material extent be entitled to have such deduction or losses derived therefrom set against the profits of companies with which it is grouped for applicable tax purposes in the

Relevant Jurisdiction (whether under the group relief system current as at the date of the Tax Law Change or any similar system or systems having like effect as may from time to time exist) and, in each such case, the Issuer cannot avoid the foregoing in connection with the Notes by taking measures reasonably available to it,

then the Issuer may:

(x) subject to Condition 2.2, Condition 5.1(b) and Condition 5.2 and having given not less than 30 nor more than 60 days' notice to the Trustee, the Principal Paying Agent, the Registrar and, in accordance with Condition 15, the Noteholders (which notice shall be irrevocable), redeem in accordance with these Conditions at any time all, but not some only, of the Notes at their principal amount, together with Arrears of Interest, if any, and any other interest accrued to (but excluding) the date of redemption in accordance with these Conditions; provided that, in the case of a Tax Law Change which is a proposed amendment or a proposed change only, no such notice of redemption shall be given earlier than 90 days prior to: (i) the earliest date on which the Issuer would be required to pay such Additional Amounts (in the case of a redemption pursuant to Condition 5.4(a)); or (ii) the first Interest Payment Date on which the eventuality set out in Condition 5.4(b)(i) or Condition 5.4(b)(ii), as applicable, would materialise (in the case of a redemption pursuant to Condition 5.4(b)), as applicable; or

(y) subject to Condition 5.2 (without any requirement for the consent or approval of the Noteholders) and having given not less than 30 nor more than 60 days' notice to the Trustee, the Principal Paying Agent, the Registrar and, in accordance with Condition 15, the Noteholders (which notice shall be irrevocable), substitute at any time all (but not some only) of the Notes for, or vary the terms of the Notes so that they remain or become, Qualifying Dated Tier 2 Securities, and the Trustee shall (subject to the following provisions of this paragraph (y) and subject to the receipt by it of the certificates of the Directors referred to below and in the definition of Qualifying Dated Tier 2 Securities) agree to such substitution or variation. The Trustee shall not be obliged to agree to any such substitution or variation of the Notes for or into Qualifying Dated Tier 2 Securities if the terms of the securities into which the Notes are to be substituted or are to be varied or such substitution or variation impose, in the Trustee's opinion, more onerous obligations or duties upon it or expose it to liabilities or reduce its protections. If the Trustee does not so agree as provided above, the Issuer may, subject as provided above, redeem the Notes as provided above.

Prior to the publication of any notice of redemption, substitution or variation pursuant to this Condition 5.4 the Issuer shall deliver to the Trustee (A) a certificate signed by two Directors stating that the relevant requirement or circumstance referred to in Condition 5.4(a) or Condition 5.4(b) applies and (B) an opinion from a nationally recognised law firm or other tax adviser in the Relevant Jurisdiction experienced in such matters to the effect that the relevant requirement or circumstance referred to in Condition 5.4(a) or Condition 5.4(b) applies. Such certificate and opinion shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct, conclusive and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate and opinion without liability to any person. Upon expiry of such notice the Issuer shall (subject to Condition 5.2 and, in the case of a redemption, to Condition 2.2, Condition 5.1(b), Condition 5.1(c) and Condition 5.1(d)) either redeem, vary or substitute the Notes, as the case may be.

In connection with any substitution or variation in accordance with this Condition 5.4, the Issuer shall comply with the rules of any stock exchange or other relevant authority on which the Notes are for the time being listed or admitted to trading.

5.5 Redemption, Substitution or Variation at the Option of the Issuer due to Capital Disqualification Event

If immediately prior to the giving of the notice referred to below a Capital Disqualification Event has occurred and is continuing, then:

(a) the Issuer may, subject to Condition 2.2, Condition 5.1(b) and Condition 5.2 and having given not less than 30 nor more than 60 days' notice to the Noteholders in accordance with Condition 15, the Trustee and the Principal Paying Agent and the Registrar (which notice shall be irrevocable), redeem in accordance with these Conditions all, but not some only, of the Notes at any time. The Notes will be redeemed at their principal amount, together with Arrears of Interest, if any, and any other unpaid interest accrued to (but excluding) the date of redemption in accordance with these Conditions; or

(b) the Issuer may, subject to Condition 5.2 (without any requirement for the consent or approval of the Noteholders) and having given not less than 30 nor more than 60 days' notice to the Trustee, the Principal Paying Agent, the Registrar and, in accordance with Condition 15, the Noteholders (which notice shall be irrevocable), substitute at any time all (and not some only) of the Notes for, or vary the terms of the Notes so that they remain or become, Qualifying Dated Tier 2 Securities, and the Trustee shall (subject to the following provisions of this paragraph (b) and subject to the receipt by it of the certificates of the Directors of the Issuer referred to below and in the definition of Qualifying Dated Tier 2 Securities) agree to such substitution or variation. The Trustee shall not be obliged to agree to the substitution or variation of the Notes for or into Qualifying Dated Tier 2 Securities if the terms of the securities into which the Notes are to be substituted or are to be varied or such substitution or variation impose, in the Trustee's opinion, more onerous obligations or duties upon it or expose it to liabilities or reduce its protections. If the Trustee does not so agree as provided above, the Issuer may, subject as provided above, redeem the Notes as provided above.

Prior to the publication of any notice of redemption, substitution or variation pursuant to this Condition 5.5 the Issuer shall deliver to the Trustee a certificate signed by two Directors stating that a Capital Disqualification Event has occurred and is continuing as at the date of the certificate. Such certificate shall be treated and accepted by the Issuer, the Trustee, the holders of the Notes and all other interested parties as correct, conclusive and sufficient evidence thereof and the Trustee shall be entitled to rely on such certificate without liability to any person. Upon expiry of such notice the Issuer shall (subject to Condition 5.2 and, in the case of a redemption, to Condition 2.2, Condition 5.1(b), Condition 5.1(c) and Condition 5.1(d)) either redeem, vary or substitute the Notes, as the case may be.

In connection with any substitution or variation in accordance with this Condition 5.5, the Issuer shall comply with the rules of any stock exchange or other relevant authority on which the Notes are for the time being listed or admitted to trading.

5.6 Purchases

Subject to Conditions 2.2 and 5.2, the Issuer and any of its Subsidiaries may at any time purchase Notes in the open market or otherwise at any price.

5.7 Cancellation

All Notes purchased by or on behalf of the Issuer or any of its Subsidiaries may (at the option of the Issuer or the relevant Subsidiary) be held, reissued, resold or surrendered for cancellation. Each Note surrendered for cancellation shall be surrendered to the Principal Paying Agent. All Notes surrendered for cancellation, together with all Notes redeemed by the Issuer, shall be cancelled forthwith. Any Notes so redeemed or surrendered for cancellation may not be reissued or resold and the obligations of the Issuer in respect of any such Notes shall be discharged.

5.8 Trustee Not Obliged to Monitor

The Trustee shall not be under any duty to monitor whether any event or circumstance has happened or exists within this Condition 5 and will not be responsible to Noteholders for any loss arising from any failure by the Trustee to do so. Unless and until the Trustee has actual knowledge of the occurrence of any event or circumstance within this Condition 5, it shall be entitled to assume that no such event or circumstance exists.

6. Payments

6.1 Method of Payment

Payment of principal and interest (including, without limitation, Arrears of Interest) will be made by transfer to the registered account of the Noteholder or by pounds sterling cheque drawn on a bank that processes payments in pounds sterling mailed to the registered address of the Noteholder if it does not have a registered account. Payments of principal and interest (including, without limitation, Arrears of Interest) due at the time of redemption of the Notes will only be made against surrender of the relevant Certificate at the specified office of any of the Agents. Payments of principal and interest (including, without limitation, Arrears of Interest) will be paid to the holder shown on the Register at the close of business on the date (the “**record date**”) being the fifteenth day before the relevant due date in respect of such payment.

For the purposes of this Condition, a Noteholder's **registered account** means the pounds sterling account maintained by or on behalf of it with a bank that processes payments in pounds sterling, details of which appear on the Register at the close of business, on the second Business Day before the due date for payment and a Noteholder's registered address means its address appearing on the Register at that time.

6.2 Payments subject to Fiscal Laws

All payments will be subject in all cases to (a) any fiscal or other laws and regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 7 and (b) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the "**Code**") or otherwise imposed pursuant to Sections 1471 through 1474 of the Code, any regulations or agreements thereunder, any official interpretations thereof, or (without prejudice to the provisions of Condition 7) any law implementing an intergovernmental approach thereto.

6.3 No commissions

No commissions or expenses shall be charged to the Noteholders in respect of any payments made in accordance with this Condition.

6.4 Payment on Business Days

Where payment is to be made by transfer to a registered account, payment instructions (for value the due date or, if that is not a Business Day, for value the first following day which is a Business Day) will be initiated and, where payment is to be made by cheque, the cheque will be mailed, on the Business Day preceding the due date for payment or, in the case of a payment of principal or interest (including, without limitation, Arrears of Interest) due at the time of redemption of the Notes, if later, on the Business Day on which the relevant Certificate is surrendered at the specified office of an Agent.

Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day, if the Noteholder is late in surrendering its Certificate (if required to do so) or if a cheque mailed in accordance with this Condition arrives after the due date for payment.

6.5 Partial Payments

If the amount of principal or interest (including, without limitation, Arrears of Interest) which is due on the Notes is not paid in full, the Registrar will annotate the Register with a record of the amount of principal or interest in fact paid.

6.6 Appointment of Agents

The Principal Paying Agent initially appointed by the Issuer and its specified office are listed below. Subject as provided in the Agency Agreement, the Principal Paying Agent and the Paying Agents act solely as agents of the Issuer and do not assume any obligation or relationship of agency or trust for or with any Noteholder. The Issuer reserves the right at any time with the approval of the Trustee to vary or terminate the appointment of the Principal Paying Agent or any other Paying Agent and to appoint additional or other Paying Agents, provided that:

(a) so long as the Notes are listed on any stock exchange, there will at all times be a Paying Agent with a specified office in such place as may be required by the rules and regulations of the relevant stock exchange (or any other relevant authority);

(b) insofar as the Issuer would be obliged (but for the provisions of Condition 7(b)) to pay additional amounts pursuant to Condition 7 upon presentation of the Notes (as the case may be) for payment in the Relevant Jurisdiction, there will at all times be a Paying Agent with a specified office in a European city other than the Relevant Jurisdiction;

(c) there will at all times be a Principal Paying Agent;

(d) there will at all times be a Paying Agent in a European Union Member State (if any) that is not obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive; and

(e) there will at all times be a Registrar.

Notice of any such change or any change of any specified office shall promptly be given to the Noteholders in accordance with Condition 15.

7. Taxation

All payments of principal and interest by or on behalf of the Issuer in respect of the Notes shall be made free and clear of, and without withholding or deduction for or on account of, any taxes, duties, assessments or governmental charges of whatever nature ("**Taxes**") imposed, levied, collected, withheld or assessed by or on behalf of the Relevant Jurisdiction, unless such withholding or deduction is required by law. In that event, the Issuer shall pay such additional amounts as shall result in receipt by the Noteholders of such amounts as would have been received by them had no such withholding or deduction been required by law to be made ("**Additional Amounts**"), except that no such Additional Amounts shall be payable with respect to any Note:

(a) surrendered for payment by or on behalf of a holder who would have been able to avoid such withholding or deduction by complying with any statutory requirement or by making a declaration of non-residence or other similar claim for exemption or filing, but fails to do so;

(b) surrendered for payment in the Relevant Jurisdiction;

(c) the holder of which is liable to the Taxes in respect of the Note by reason of his having some connection with any Relevant Jurisdiction other than the mere holding of the Note; or

(d) where such withholding or deduction is required to be made pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive; or

(e) surrendered for payment by or on behalf of a holder who would have been able to avoid such withholding or deduction by surrendering the relevant Note to another Paying Agent in a Member State of the European Union; or

(f) surrendered for payment more than 30 days after the Relevant Date (as defined below) except to the extent that a holder would have been entitled to such

Additional Amounts on surrendering the same for payment on the last day of the period of 30 days assuming that day to have been a Business Day.

As used in these Conditions:

"**Relevant Date**" in respect of any Note means the date on which payment in respect of it first becomes due or (if any amount of the money payable is improperly withheld or refused) the date on which payment in full of the amount outstanding is made or (if earlier) the date seven days after that on which notice is duly given to the Noteholders that, upon further presentation of the Note being made in accordance with the Conditions, such payment will be made, provided that payment is in fact made upon such presentation. References in these Conditions to principal and/or interest shall be deemed to include any Additional Amounts that may be payable under this Condition or any undertaking given in addition to or in substitution for it under the Trust Deed; and

"**Relevant Jurisdiction**" means the United Kingdom or any political subdivision or any authority thereof or therein having power to tax or any other jurisdiction or any political subdivision or any authority thereof or therein having power to tax to which the Issuer becomes subject in respect of payments made by it of principal and interest on the Notes.

8. Prescription

Claims against the Issuer for payment in respect of the Notes shall be prescribed and become void unless made within 10 years (in the case of principal) or five years (in the case of interest including, without limitation, Arrears of Interest) from the appropriate Relevant Date in respect of them.

9. Events of Default and Enforcement

9.1 Rights to institute and/or prove in a winding-up

Notwithstanding any of the provisions below in this Condition 9, the right to institute winding-up proceedings is limited to circumstances where payment has become due and is not duly paid. Pursuant to Condition 2.2, no principal, interest or any other amount will be due on the relevant payment date if the Solvency Condition is not satisfied, at the time of and immediately after any such payment. In the case of any payment of interest in respect of the Notes, such payment will be deferred and will not be due if Condition 4.1 applies and in the case of payment of principal, such payment will be deferred and will not be due if Condition 5.1(b) applies or the Relevant Regulator does not consent to the redemption (to the extent that consent is then required by the Relevant Regulator or the Relevant Rules), the Relevant Regulator objects to the redemption or such redemption otherwise cannot be effected in compliance with the Relevant Rules on such date.

If default is made for a period of 14 days or more in the payment of any interest (including, without limitation, Arrears of Interest) or principal due in respect of the Notes or any of them, the Trustee in its discretion may, and if so requested by Noteholders of at least one quarter in principal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution shall (subject, in each case, to its having been indemnified and/or secured and/or prefunded to its satisfaction) institute proceedings for the winding-up of the Issuer and/or prove in the winding-up or administration of the Issuer and/or claim in the liquidation of the Issuer for such payment, but may take no further or other action to enforce, prove or claim for any such payment. No payment in respect of the Notes or the Trust Deed may be made by the Issuer pursuant to Condition 9.1, nor will the Trustee accept the same, otherwise than during or after a winding-up of the Issuer or after an administrator of the Issuer has given notice that it intends to declare and distribute a dividend, unless the Issuer has given prior written notice (with a copy to the Trustee) to, and received consent or non-objection from, the Relevant Regulator, which the Issuer shall confirm in writing to the Trustee.

9.2 Amount payable on winding-up or administration

If an order is made by the competent court or resolution passed for the winding-up of the Issuer, (other than an Approved Winding-up) or an administrator of the Issuer gives notice that it intends to declare and distribute a dividend, the Trustee at its discretion may, and if so requested by Noteholders of at least one quarter in principal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution shall (subject, in each case, to its having been indemnified and/or secured and/or prefunded to its satisfaction), give notice to the Issuer (or, as applicable, the administrator or liquidator) that the Notes are, and they shall accordingly forthwith become, immediately due and repayable at the amount equal to their principal amount together with Arrears of Interest, if any, and any other accrued and unpaid interest, and the claim in respect thereof will be subject to the subordination provided for in Condition 2.1.

In addition, any other amounts in respect of the Notes (including any damages awarded for breach of any obligations under these Conditions or the Trust Deed) in respect of which the Solvency Condition was not satisfied on the date upon which the same would otherwise have become due and payable ("**Solvency Claims**") will be payable by the Issuer in a winding-up or administration of the Issuer, and the claim in respect thereof will be subject to the subordination provided for in Condition 2.1. A Solvency Claim shall not bear interest.

9.3 Enforcement

Without prejudice to Condition 9.1 or Condition 9.2 above, the Trustee may at its discretion and without further notice institute such proceedings or take such steps or actions against the Issuer as it may think fit to enforce any obligation, condition or provision binding on the Issuer under the Trust Deed or the Notes (other than any payment obligation of the Issuer under or arising from the Notes or the Trust Deed including, without limitation, payment of any principal or interest (including, without limitation, Arrears of Interest) in respect of the Notes and any damages awarded for breach of any obligations) but in no event shall the Issuer, by virtue of the institution of any such proceedings or the taking of such steps or actions, be obliged to pay any sum or sums (in cash or otherwise) sooner than the same would otherwise have been payable by it. Nothing in this Condition 9.3 shall, subject to Condition 9.1, prevent the Trustee instituting proceedings for the winding-up of the Issuer, proving in any winding-up of the Issuer and/or claiming in any liquidation of the Issuer in respect of any payment obligations of the Issuer arising from the Notes or the Trust Deed (including without limitation, payment of any principal or interest (including, without limitation, Arrears of Interest) in respect of the Notes and any damages awarded for any breach of any obligations under the Notes or the Trust Deed).

9.4 Entitlement of the Trustee

The Trustee shall not be bound to take any of the actions referred to in Condition 9.1, Condition 9.2 or Condition 9.3 above to enforce the obligations of the Issuer under the Trust Deed or the Notes unless (a) it shall have been so directed by an Extraordinary Resolution of the Noteholders or so requested in writing by the holders of at least one-quarter in principal amount of the Notes then outstanding and (b) it shall have been indemnified and/or secured and/or prefunded to its satisfaction.

9.5 Right of Noteholders

No Noteholder shall be entitled to proceed directly against the Issuer or to institute proceedings for the winding-up or claim in the liquidation of the Issuer or to prove in such winding-up unless the Trustee, having become so bound to proceed, institute, claim or prove, fails to do so within a reasonable period and such failure shall be continuing, in which case the Noteholder shall have only such rights against the Issuer as those which the Trustee is entitled to exercise as set out in this Condition 9.

9.6 Extent of Noteholders' remedy

No remedy against the Issuer, other than as referred to in this Condition 9, shall be available to the Trustee or the Noteholders, whether for the recovery of amounts owing in respect of the Notes or under the Trust Deed or in respect of any breach by the Issuer of any of its other obligations under or in respect of the Notes or under the Trust Deed.

Nothing in this Condition 9 shall affect or prejudice the right of the Trustee to take any action or step or institute proceedings to enforce its rights to payment of its costs, fees, charges, expenses, liabilities or remuneration under the Trust Deed or the rights and remedies of the Trustee in respect thereof.

10. Meetings of Noteholders, Modification, Waiver and Substitution

10.1 Meetings of Noteholders

The Trust Deed contains provisions for convening meetings of Noteholders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of any of these Conditions or any provisions of the Trust Deed. Such a meeting may be convened by Noteholders holding not less than 10 per cent. in principal amount of the Notes for the time being outstanding. The quorum for any meeting convened to consider an Extraordinary Resolution shall be one or more persons holding or representing a clear majority in principal amount of the Notes for the time being outstanding, or at any adjourned meeting one or more persons holding Notes or representing Noteholders whatever the principal amount of the Notes held or represented, unless the business of such meeting includes consideration of proposals, *inter alia* (a) to amend the dates of maturity or redemption of the Notes or any date for payment of interest or Arrears of Interest on the Notes, (b) to reduce or cancel the principal amount of the Notes, (c) to reduce the rate or rates of interest or Arrears of Interest in respect of the Notes or to vary the method or basis of calculating the rate or rates or amount of interest or the basis for calculating any interest amount in respect of the Notes, (d) to vary the currency or currencies of payment or denomination of the Notes, (e) to take any steps that as specified hereon may only be taken following approval by an Extraordinary Resolution to which the special quorum provisions apply,

(f) to modify the provisions concerning the quorum required at any meeting of Noteholders or the majority required to pass an Extraordinary Resolution, or (g) to modify Condition 2, in which case the necessary quorum shall be one or more persons holding or representing not less than two-thirds, or at any adjourned meeting not less than one-third, in principal amount of the Notes for the time being outstanding.

The Trust Deed provides that (a) a resolution passed at a meeting duly convened and held by a majority consisting of not less than three-quarters of the persons voting at such meeting, (b) a resolution in writing signed by or on behalf of the holders of not less than three-quarters in principal amount of the Notes for the time being outstanding, or (c) consents given by way of electronic consents though the relevant clearing system(s) (in a form satisfactory to the Trustee) by or on behalf of the holder(s) of not less than three-quarters in principal amount of the Notes for the time being outstanding, shall, in each case, be effective as an Extraordinary Resolution of the Noteholders. Any resolution in writing referred to in (b) may be contained in one document or several documents in the same form, each signed by or on behalf of the one or more Noteholders.

The agreement or approval of the Noteholders shall not be required in the case of any variation of these Conditions and/or the Trust Deed made in the circumstances described in Condition 5.4 or Condition 5.5 in connection with the substitution or variation of the Notes so that they remain or become Qualifying Dated Tier 2 Securities, and to which the Trustee has agreed pursuant to the relevant provisions of Condition 5.4 or Condition 5.5, as the case may be. Any Extraordinary Resolution duly passed shall be binding on Noteholders (whether or not they were present at the meeting at which such resolution was passed or otherwise voted in respect of the Extraordinary Resolution).

10.2 Modification of the Trust Deed or the Agency Agreement

The Trustee may agree, without the consent of the Noteholders, to (a) any modification of any of these Conditions and the provisions of the Trust Deed or the Agency Agreement that is in the opinion of the Trustee of a formal, minor or technical nature or is made to correct a manifest error, and (b) any other modification (except as mentioned in the Trust Deed), and any waiver or authorisation of any breach or proposed breach, of any of these Conditions and the provisions of the Trust Deed or the Agency Agreement that is in the opinion of the Trustee not materially prejudicial to the interests of the Noteholders.

Any such modification, authorisation or waiver shall be binding on the Noteholders and such modification shall be notified to the Noteholders as soon as practicable thereafter.

10.3 Notice to the Relevant Regulator

No modification to these Conditions or any other provisions of the Trust Deed shall become effective unless (to the extent then required by the Relevant Regulator or the Relevant Rules) the Issuer shall have given at least one month's prior written notice to, and received consent or no objection from, the Relevant Regulator (or such other period of notice as the Relevant Regulator may from time to time require or accept).

10.4 Substitution

The Trustee may agree with the Issuer, without the consent of the Noteholders, to the substitution on a subordinated basis equivalent to that referred to in Condition 2 of any person or persons incorporated in any country in the world (the "**Substitute Obligor**") in place of the Issuer (or any previous Substitute Obligor under this Condition) as a new principal debtor under the Trust Deed and the Notes provided that:

(a) a trust deed is executed or some other form of undertaking is given by the Substitute Obligor in form and manner satisfactory to the Trustee, agreeing to be bound by the terms of the Trust Deed and the Notes, with any consequential amendments which the Trustee may deem appropriate, as fully as if the Substitute Obligor had been named in the Trust Deed and on the Notes, as the principal debtor in place of the Issuer (or of any previous Substitute Obligor, as the case may be);

(b) (unless the successor in business of the Issuer is the Substitute Obligor) the obligations of the Substitute Obligor under the Trust Deed and the Notes are guaranteed by the Issuer (or the successor in business of the Issuer) on a subordinated basis equivalent to that referred to in Condition 2 and in the Trust Deed and in a form and manner satisfactory to the Trustee, and provided further that the obligations of such guarantor shall be subject to a solvency condition equivalent to that set out in Condition 2.2, such guarantor shall not exercise rights of subrogation or contribution against the Substitute Obligor without the consent of the Trustee and the only event of default applying to such guarantor shall be an event of default equivalent to that set out in Condition 9.1;

(c) the directors of the Substitute Obligor or other officers acceptable to the Trustee certify that the Substitute Obligor is solvent at the time at which the said substitution is proposed to be effected (and the Trustee may rely absolutely on such certification without liability to any person and shall not be bound to have regard to the financial condition, profits or prospects of the Substitute Obligor or to compare the same with those of the Issuer);

(d) (without prejudice to the rights of reliance of the Trustee under Condition 10.4(c) above) the Trustee is satisfied that the said substitution is not materially prejudicial to the interests of the Noteholders;

(e) (without prejudice to the generality of Condition 10.4(a) above) the Trustee may in the event of such substitution agree, without the consent of the Noteholders, to a change in the law governing the Trust Deed and/or the Notes, provided that such change would not in the opinion of the Trustee be materially prejudicial to the interests of the Noteholders;

(f) if the Substitute Obligor is, or becomes, subject generally to the taxing jurisdiction of a territory or any authority of or in that territory with power to tax (the "**Substituted Territory**") other than the territory or any such authority to the taxing jurisdiction of which the Issuer is subject generally (the "**Issuer's Territory**"), the Substitute Obligor will (unless the Trustee otherwise agrees) give to the Trustee an undertaking satisfactory to the Trustee in terms corresponding to Condition 7 with the substitution for the references in that Condition and in Condition 5.4 to the Issuer's Territory of references to the Substituted Territory whereupon the Trust Deed and the Notes will be read accordingly; and

(g) the Issuer and the Substitute Obligor comply with such other requirements as are reasonable in the interests of the Noteholders, as the Trustee may direct.

Any substitution pursuant to this Condition 10 shall be subject (to the extent then required by the Relevant Regulator or the Relevant Rules) to any notifications to, or consent or non-objection from, the Relevant Regulator.

11. Entitlement of the Trustee

In connection with any exercise of its functions (including but not limited to those referred to in Condition 10), the Trustee shall have regard to the interests of the Noteholders as a class and the Trustee shall not have regard to the consequences of such exercise for individual Noteholders resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory. In connection with any such exercise as aforesaid, no Noteholder shall be entitled to claim, whether from the Issuer, the Substitute Obligor or the Trustee or any other person, any indemnification or payment in respect of any tax consequence of any such substitution or any such exercise upon any individual Noteholders except to the extent already provided in Condition 7 and/or any undertaking given in addition thereto or in substitution therefor pursuant to the Trust Deed.

12. Indemnification of the Trustee and its Contracting with the Issuer

12.1 Indemnification of the Trustee

The Trust Deed contains provisions for the indemnification of, and/or provision of security and/or prefunding for, the Trustee and for its relief from responsibility, including provisions relieving it from taking any action or steps or instituting any proceedings unless indemnified and/or secured and/or prefunded to its satisfaction.

12.2 Trustee Contracting with the Issuer

The Trust Deed also contains provisions pursuant to which the Trustee is entitled, *inter alia*, (a) to enter into business transactions with the Issuer and/or any of its Subsidiaries and to act as trustee for the holders of any other securities issued or guaranteed by, or relating to, the Issuer and/or any of its Subsidiaries, (b) to exercise and enforce its rights, comply with its obligations and perform its duties under or in relation to any such transactions or, as the case may be, any such trusteeship without regard to the interests of, or consequences for, the Noteholders, and (c) to retain and not be liable to account for any profit made or any other amount or benefit received thereby or in connection therewith.

The Trustee may rely without liability to Noteholders on a report, confirmation or certificate or any advice of any accountants, financial advisers, financial institution or any other expert, whether or not addressed to it and whether their liability in relation thereto is limited (by its terms or by any engagement letter relating thereto entered into by the Trustee or in any other manner) by reference to a monetary cap, methodology or otherwise. The Trustee may accept and shall be entitled to rely on any such report, confirmation or certificate or advice and such report, confirmation or certificate or advice shall be binding on the Issuer, the Trustee and the Noteholders.

The Trustee is not responsible for monitoring or supervising the performance by the Principal Paying Agent and/or any other person of its obligations to the Issuer and may assume these are being performed unless and until it has actual knowledge to the contrary.

13. Replacement of Certificates

If any Certificate is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Registrar upon payment by the claimant of the expenses incurred in connection with the replacement and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

14. Further Issues

The Issuer may from time to time without the consent of the Noteholders create and issue further securities either having the same terms and conditions as the Notes in all respects (or in all respects except for the first payment of interest on them) and so that such further issue shall be consolidated and form a single series with the outstanding securities of any series (including the Notes) or upon such terms as the Issuer may determine at the time of their issue. References in these Conditions to the Notes include (unless the context requires otherwise) any other securities issued pursuant to this Condition and forming a single series with the Notes. Any further securities forming a single series with the outstanding securities of any series (including the Notes) constituted by the Trust Deed or any deed supplemental to it shall, and any other securities may (with the consent of the Trustee), be constituted by the Trust Deed. The Trust Deed contains provisions for convening a single meeting of the Noteholders and the holders of securities of other series where the Trustee so decides.

15. Notices

All notices to the Noteholders will be valid if mailed to them by first class mail or (if posted to an address overseas) by airmail to the holders (or the first of any joint named holders) at their respective addresses in the Register maintained by the Registrar. The Issuer shall also ensure that notices are duly given or published in a manner which complies with the rules and regulations of any stock exchange or other relevant authority on which the Notes are for the time being listed. Any such notice will be deemed to have been given on the fourth day after being so mailed or on the date of publication or, if published more than once or on different dates, on the first date on which publication is made.

16. Contracts (Rights of Third Parties) Act 1999

No person shall have any right to enforce any term or condition of the Notes under the Contracts (Rights of Third Parties) Act 1999.

17. Definitions

As used herein:

"**Additional Amounts**" has the meaning given to it in Condition 7;

"**Agency Agreement**" has the meaning given in the preamble to these Conditions;

“**Agent**” has the meaning given in the preamble to these Conditions;

“**Approved Winding-up**” means a solvent winding-up of the Issuer solely for the purposes of a reconstruction or amalgamation or the substitution in place of the Issuer of a successor in business of the Issuer, the terms of which reconstruction, amalgamation or substitution (i) have previously been approved in writing by the Trustee or by an Extraordinary Resolution and (ii) do not provide that the Notes shall thereby become payable;

“**Arrears of Interest**” has the meaning given to it in Condition 4.2;

“**Assets**” means the unconsolidated gross assets of the Issuer, as shown in the latest published audited balance sheet of the Issuer, but adjusted for subsequent events, all in such manner as the Directors may determine;

“**Business Day**” means (i) except for the purposes of Conditions 1.4, 6 and 7(f), a day (other than a Saturday, Sunday or public holiday) on which commercial banks and foreign exchange markets are open for general business in London, (ii) for the purposes of Condition 1.4, a day (other than a Saturday, Sunday or public holiday) on which commercial banks are open for business in the city in which the specified office of the Agent with whom a Certificate is deposited in connection with a transfer is located and (iii) for the purpose of Conditions 6 and 7(f), a day (other than a Saturday, Sunday or public holiday) on which commercial banks are open for business in London and, in the case of surrender of a Certificate, in the place in which the Certificate is surrendered;

“**Calculation Agent**” means The Bank of New York Mellon, London Branch (or its successor);

“**Call Date**” means 8 May 2020;

“**Capital Disqualification Event**” is deemed to have occurred if as a result of any change to (or change to the interpretation by any court or authority entitled to do so of) the Relevant Rules, the Directive or Solvency II, the entire principal amount of the Notes is fully excluded from counting as Tier 2 Capital for the purposes of the Issuer or all or any part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group), whether on a solo or group basis, except (in either case) where such non-qualification is only as a result of any applicable limitation on the amount of such capital;

“**Certificate**” has the meaning given in Condition 1.1;

“**CISGIL Group**” means, at any time, the Issuer and its Subsidiaries (if any) at such time;

“**CISGIL Group Supervisor**” means the regulatory authority exercising group supervision over the CISGIL Group in accordance with the Solvency II Directive;

“**Directive**” means Directive 98/78/EC of the European Union as amended (from time to time);

“**Directors**” means the directors of the Issuer;

“**EEA Regulated Market**” means a market as defined by Article 4.1 (14) of Directive 2004/39/EC of the European Parliament and of the Council on markets in financial instruments, as amended;

“**European Economic Area**” or “**EEA**” means the countries comprising the European Union together with Norway, Liechtenstein and Iceland;

“**Extraordinary Resolution**” has the meaning given in the Trust Deed;

“**FSMA**” means the UK Financial Services and Markets Act 2000, as amended from time to time;

“**Initial Fixed Interest Rate**” has the meaning given to it in Condition 3.4;

“**Initial Fixed Rate Interest Period**” means the period from (and including) the Issue Date to (but excluding) the Reset Date;

“**Insolvent Insurer Winding-up**” means:

(i) the winding-up of any Insurance Undertaking within the CISGIL Group;

(ii) the appointment of an administrator of any Insurance Undertaking within the CISGIL Group,

where the claims of the policyholders of the Insurance Undertaking which is in winding-up or administration may or will not be met in full (and for these purposes, the claims of policyholders shall include all amounts to which policyholders are entitled under applicable legislation or rules relating to the winding-up of insurance companies to reflect any right to receive or expectation of receiving benefits which policyholders may have);

“**Insurance Undertaking**” has the meaning given to it in the Solvency II Directive;

“**Interest Payment Date**” has the meaning given to it in Condition 3.1;

“**Interest Rate**” means the Initial Fixed Interest Rate and/or the Reset Rate of Interest, as the case may be;

“**Issue Date**” means 8 May 2015, being the date of the initial issue of the Notes;

“**Junior Securities**” has the meaning given to it in Condition 2.1;

“**Liabilities**” means the unconsolidated gross liabilities of the Issuer, as shown in the latest published audited balance sheet of the Issuer, but adjusted for contingent liabilities and for subsequent events, all in such manner as the Directors may determine;

“**Lower Tier 2 Capital**” has the meaning given to it for the purposes of the Relevant Rules and shall following Solvency II Implementation or any other change in law or any Relevant Rules such that Lower Tier 2 Capital ceases to be a separately recognised tier of capital resources, be deemed to be a reference to Tier 2 Capital;

“**Mandatory Interest Deferral Date**” means each Interest Payment Date in respect of which a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or would occur if payment of interest was made on such Interest Payment Date;

“**Margin**” means 10.671 per cent.;

“**Maturity Date**” means 8 May 2025;

“**Pari Passu Creditors**” means creditors of the Issuer whose claims rank, or are expressed to rank, *pari passu* with the claims of the Noteholders, including (without limitation) holders of Pari Passu Securities;

“**Pari Passu Securities**” has the meaning given to it in Condition 2.1;

“**pounds sterling**” or “**£**” means the lawful currency of the UK;

“**Paying Agent**” has the meaning given in the preamble to these Conditions;

“**Principal Paying Agent**” has the meaning given in the preamble to these Conditions;

“**Qualifying Dated Tier 2 Securities**” means securities issued directly by the Issuer or indirectly and guaranteed by the Issuer (such guarantee to rank on a subordinated basis equivalent to that referred to in Condition 2 and in the Trust Deed) that:

(i) have terms not materially less favourable to a holder than the terms of the Notes, as reasonably determined by the Issuer in consultation with an independent investment bank of international standing; and

(ii) (subject to (i) above) contain terms which comply with the then current requirements of the Relevant Regulator in relation to Lower Tier 2 Capital (prior to Solvency II Implementation) or Tier 2 Capital (on or after Solvency II Implementation); and

(iii) are listed or admitted to trading on the EEA Regulated Market of the London Stock Exchange or such other stock exchange as is a Recognised Stock Exchange at that time as selected by the Issuer and approved by the Trustee,

and provided that a certification to the effect of (i) and (ii) above, signed by two Directors, shall have been delivered to the Trustee (upon which the Trustee shall be entitled to rely without liability to any person) prior to the issue of the relevant securities;

“**Recognised Stock Exchange**” means a recognised stock exchange as defined in section 1005 of the Income Tax Act 2007 as the same may be amended from time to time and any provision, statute or statutory instrument replacing the same from time to time;

“**Register**” has the meaning given in Condition 1.1;

“**Registrar**” has the meaning given in the preamble to these Conditions;

"**Regulatory Capital Requirements**" means any applicable capital resources requirement or applicable overall financial adequacy rule (or equivalent) required by the Relevant Regulator, as any such requirement or rule is in force from time to time;

"**Regulatory Deficiency Interest Deferral Event**" means any event (including, without limitation, where an Insolvent Insurer Winding-up has occurred and is continuing and any event which causes any Solvency Capital Requirement applicable to the Issuer, all or part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group) or any Insurance Undertaking within the CISGIL Group to be breached and such breach is an event) which under Solvency II and/or under the Relevant Rules means that the Issuer must defer payment of interest (or, if applicable, Arrears of Interest) in respect of the Notes;

"**Regulatory Deficiency Redemption Deferral Event**" means any event (including, without limitation, where an Insolvent Insurer Winding-up has occurred and is continuing and any event which causes any Solvency Capital Requirement applicable to the Issuer, all or part of the CISGIL Group (which part includes the Issuer and at least one other member of the CISGIL Group) or any Insurance Undertaking within the CISGIL Group to be breached and such breach is an event) which under Solvency II and/or under the Relevant Rules means that the Issuer must defer or suspend repayment or redemption of the Notes;

"**Relevant Date**" has the meaning given to it in Condition 7;

"**Relevant Jurisdiction**" has the meaning given to it in Condition 7;

"**Relevant Regulator**" means the UK Regulator or, if the UK Regulator at any time ceases to be the CISGIL Group Supervisor or the Supplementary Supervisor, such other regulator as becomes the CISGIL Group Supervisor for the purposes of Solvency II or the Supplementary Supervisor for the purposes of the Directive (as applicable);

"**Relevant Rules**" means any legislation (including European legislation with direct effect in the jurisdiction of the Relevant Regulator, rules or regulations (whether having the force of law or otherwise) in the jurisdiction of the Relevant Regulator, implementing the Directive or, as applicable, Solvency II and includes any relevant prudential rules for insurers applied by the Relevant Regulator and any amendment, supplement or replacement of either thereof from time to time relating to the characteristics, features or criteria of own funds or capital resources;

"**Reset Date**" means 8 May 2020;

"**Reset Determination Date**" means the day falling two London business days prior to the first day of the Reset Period;

"**Reset Period**" means the period from (and including) the Reset Date to (but excluding) the date on which the Notes are redeemed pursuant to Condition 5;

"**Reset Rate of Interest**" has the meaning given to it in Condition 3.5;

"**Reset Reference Banks**" means four major banks in the interbank market in London as selected by the Issuer;

"**Reset Reference Rate**" means in respect of the Reset Period, (i) the applicable semi-annual mid-swap rate for swap transactions in pounds sterling (with a maturity equal to 5 years) as displayed on the Screen Page at 11.00 a.m. (London time) on the Reset Determination Date or (ii) if such rate is not displayed on the Screen Page at such time and date, the Reset Reference Bank Rate, where:

> "**Mid-Swap Quotations**" means the arithmetic mean of the bid and offered rates for the semi-annual fixed leg (calculated on a Actual/365 day count basis) of a fixed for floating interest rate swap transaction in pounds sterling which (i) has a term commencing on the Reset Date which is equal to 5 years; (ii) is in an amount that is representative of a single transaction in the relevant market at the relevant time with an acknowledged dealer of good credit in the relevant swap market; and (iii) has a floating leg based on the 6-month LIBOR rate (calculated on an Actual/365 day count basis);
>
> "**Reset Reference Bank Rate**" means the percentage rate determined on the basis of the Mid-Swap Quotations provided by the Reset Reference Banks to the Issuer and notified to the Calculation Agent at or around 11:00 a.m. (London time) on the Reset Determination Date and, rounded, if necessary, to the nearest 0.001 per cent. (0.0005 per cent. being rounded upwards). If at least four quotations are provided, the Reset Reference Bank Rate will be the rounded arithmetic mean of the quotations provided, eliminating the highest quotation (or, in the event of equality, one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest). If only two or three quotations are provided, the Reset Reference Bank Rate will be the rounded arithmetic mean of the quotations provided. If only one quotation is provided, the Reset Reference Bank Rate will be the rounded quotation provided. If no quotations are provided, the Reset Reference Bank Rate will be determined by an investment bank of international standing appointed by the Issuer in its sole discretion; and
>
> "**Screen Page**" means Reuters screen page "ICAP2", or such other screen page as may replace it on Reuters or, as the case may be, on such other information service that may replace Reuters, in each case, as may be nominated by the person providing or sponsoring the information appearing there for the purpose of displaying comparable rates;

"**Senior Creditors**" means (a) creditors of the Issuer who are unsubordinated creditors of the Issuer including all policyholders of the Issuer (for the avoidance of doubt, the claims of policyholders shall include all amounts to which policyholders are entitled under applicable legislation or rules relating to the winding-up of insurance companies to reflect any right to receive or expectation of receiving benefits which policyholders may have) and (b) creditors of the Issuer whose claims are, or are expressed to be, subordinated to the claims of other creditors of the Issuer (other than those whose claims are in respect of instruments or obligations which constitute, or would but for any applicable limitation on the amount of any such capital, constitute (i) Tier 1 Capital, (ii) Upper Tier 2 Capital issued prior to Solvency II Implementation or Lower Tier 2 Capital issued prior to Solvency II Implementation or (iii) Tier 2 Capital issued on or after Solvency II Implementation, or whose claims otherwise rank, or are expressed to rank, *pari passu* with, or junior to, the claims of the Noteholders);

"**Solvency Capital Requirement**" means the Solvency Capital Requirement or the group Solvency Capital Requirement (as applicable) referred to in, or any other capital requirement howsoever described in, Solvency II or the Relevant Rules (including, for the avoidance of doubt, any minimum capital requirement);

"**Solvency II**" means the Solvency II Directive and any additional measures adopted to give effect to the Solvency II Directive (for the avoidance of doubt, whether implemented by way of a regulation, a directive or otherwise);

"**Solvency Condition**" has the meaning given to it in Condition 2.2;

"**Solvency II Directive**" means Directive 2009/138/EC of the European Union of 25 November 2009 on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II) and which must be transposed by Member States of the European Economic Area pursuant to Article 309 of Directive 2009/138/EC;

"**Solvency II Implementation**" means the date from which legislation, rules or other measures implementing Solvency II in the UK (or, if the UK Regulator ceases to be the Supplementary Supervisor or ceases to be the CISGIL Group Supervisor, in the jurisdiction of such replacement Supplementary Supervisor or of the replacement CISGIL Group Supervisor, as applicable) are applied to the Issuer;

"**Subsidiary**" has the meaning given to it in section 102 of the Co-operative and Community Benefit Societies Act 2014 (as amended from time to time);

"**successor in business**" means any body corporate which, as the result of any amalgamation, merger, reconstruction, acquisition or transfer:

> owns beneficially the whole or substantially the whole of the undertaking, property and assets owned by the Issuer or a successor in business of the Issuer prior thereto; and
>
> carries on, as successor to the Issuer or a successor in business of the Issuer, the whole or substantially the whole of the business carried on by the Issuer or a successor in business of the Issuer prior thereto;

"**Supplementary Supervisor**" means the regulatory authority exercising supplementary supervision over the CISGIL Group in accordance with the Directive;

"**Taxes**" has the meaning given to it in Condition 7;

"**Tax Event**" means an event of the type described in Condition 5.4(a) or 5.4(b);

"**Tax Law Change**" has the meaning given to it in Condition 5.4(a);

"**Tier 1 Capital**" has the meaning given to it for the purposes of the Relevant Rules;

"**Tier 2 Capital**" has the meaning given to it for the purposes of the Relevant Rules;

"**UK Regulator**" means the UK Prudential Regulation Authority or any successor UK regulatory authority having prudential supervisory responsibilities with respect to the Issuer and/or the CISGIL Group;

"**United Kingdom**" or "**UK**" means the United Kingdom of Great Britain and Northern Ireland; and

"**Upper Tier 2 Capital**" has the meaning given to it for the purposes of the Relevant Rules.

18. Governing Law

The Trust Deed and the Notes and any non-contractual obligations arising out of or in connection with the Trust Deed and the Notes are governed by, and shall be construed in accordance with, English law.

SUMMARY OF PROVISIONS RELATING TO THE NOTES WHILST IN GLOBAL FORM

The Global Certificate contains provisions which apply to the Notes while they are in global form, some of which modify the effect of the terms and conditions of the Notes set out in this Prospectus. The following is a summary of certain of those provisions.

1. Accountholders

For so long as any of the Notes are evidenced by the Global Certificate, each person (other than another clearing system) who is for the time being shown in the records of Euroclear or Clearstream, Luxembourg as the holder of a particular aggregate principal amount of the Notes (each an **Accountholder**) (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg as to the aggregate principal amount of such Notes standing to the account of any person shall be conclusive and binding for all purposes save in the case of manifest error) shall be treated as the holder of such aggregate principal amount of such Notes (and the expression "Noteholders" and references to "holding of Notes" and to "holder of Notes" shall be construed accordingly) for all purposes other than with respect to payments on such Notes, the right to which shall be vested, as against the Issuer and the Trustee, solely in the nominee for the relevant clearing system (the **Relevant Nominee**) in accordance with and subject to the terms of the Global Certificate. Each Accountholder must look solely to Euroclear or Clearstream, Luxembourg, as the case may be, for its share of each payment made to the Relevant Nominee.

2. Cancellation

Cancellation of any Note following its redemption or purchase by the Issuer or any of Subsidiaries will be effected by reduction in the aggregate principal amount of the Notes in the register of Noteholders and by the annotation of the appropriate schedule to the relevant Global Certificate.

3. Payments

Payments of principal and interest in respect of Notes represented by the Global Certificate will be made to the registered holder of the Global Certificate. Upon payment of any principal or interest, the amount so paid shall be endorsed by or on behalf of the Registrar on behalf of the Issuer on the schedule to the Global Certificate.

Distributions of amounts with respect to book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be credited, to the extent received by the Registrar, to the cash accounts of participants in Euroclear, Clearstream, Luxembourg or any Alternative Clearing System in accordance with the relevant clearing system's rules and procedures.

All payments in respect of the Notes whilst they are represented by the Global Certificate will be made to, or to the order of, the person whose name is entered in the Register at the close of business on the Clearing System Business Day immediately prior to the date for payment, where "**Clearing System Business Day**" means Monday to Friday (inclusive) except 25 December and 1 January.

4. Calculation of interest

Notwithstanding the provisions of the final paragraph of Condition 3.3, for so long as all of the Notes are represented by a Global Certificate, interest shall be calculated on the aggregate principal amount of the Notes represented by such Global Certificate (and not per £1,000 in principal amount), but otherwise shall be calculated in accordance with Condition 3.

5. Notices

For so long as all of the Notes are represented by the Global Certificate and such Global Certificate is held on behalf of Euroclear and/or Clearstream, Luxembourg, notices to Noteholders may be given by delivery of the relevant notice to Euroclear and/or Clearstream, Luxembourg (as the case may be) for communication to the relevant Accountholders (or otherwise in such manner as the Trustee, the Principal Paying Agent and Euroclear and/or Clearstream, Luxembourg (as the case may be) may approve for this purpose) rather than by delivery or publication as required by Condition 15 provided that, so long as the Notes are admitted to listing or trading on any stock exchange, the requirements of such stock exchange have been complied with. Any such notice shall be deemed to have been given to the Noteholders on the day which is one business day, being a day on which banks are generally open, in Brussels and Luxembourg, after the date on which such notice is delivered to Euroclear and/or Clearstream, Luxembourg as aforesaid.

6. Registration of Title

Registration of title to Notes in a name other than that of the Relevant Nominee will not be permitted unless Euroclear or Clearstream, Luxembourg notifies the Issuer that it is unwilling or unable to continue as a clearing system in connection with a Global Certificate and a successor clearing system approved by the Trustee is not appointed by the Issuer within 90 days after receiving such notice from Euroclear, Clearstream, Luxembourg. In these circumstances title to a Note may be transferred into the names of holders notified by the Relevant Nominee in accordance with the Conditions, except that Certificates in respect of Notes so transferred may not be available until 21 days after the request for transfer is duly made.

The Registrar will not register title to the Notes in a name other than that of the Relevant Nominee for a period of 15 calendar days preceding the due date for any payment of principal, or interest (including, without limitation, Arrears of Interest) in respect of the Notes.

7. Transfers

Transfers of book-entry interests in the Notes will be effected through the records of Euroclear, and Clearstream, Luxembourg and their respective participants in accordance with the rules and procedures of Euroclear, and Clearstream, Luxembourg and their respective direct and indirect participants.

USE OF PROCEEDS

The net proceeds of the issue of the Notes, amounting to approximately £68,750,000, will be applied by the Issuer to enable it to implement its strategic plan as outlined in "*Business Description* - *Strategy*" whilst maintaining its regulatory capital buffer at an appropriate level.

BUSINESS DESCRIPTION

Description of the Issuer

Overview

The Issuer, CIS General Insurance Limited (**CISGIL**), is a wholly owned Subsidiary of Co-operative Banking Group Limited. The ultimate holding company of the Issuer is Co-operative Group Limited (**CGL**). CGL and its Subsidiaries are herein referred to as the **Co-operative Group**. The Issuer offers general insurance products including home and motor insurance products. The Issuer is authorised by the PRA and regulated by the FCA and the PRA.

The Issuer is a registered society under the Co-operative and Community Benefit Societies Act 2014. The Issuer is of indefinite duration and domiciled in England and Wales. It was incorporated and registered in England and Wales on 29 September 2005 under the Industrial and Provident Societies Act 1965-2003 with registered number 29999R and began trading on 15 January 2006.

The Issuer's registered office and principal place of business is Miller Street, Manchester M60 0AL. The telephone number of the Issuer's registered office is 0161 832 8686.

History of the Issuer

- Prior to its incorporation in 2005, the Issuer's business enjoyed a long and distinguished history as part of the Co-operative Insurance Society, which was initially registered as the Co-operative Insurance Company Limited on 29 August 1867.

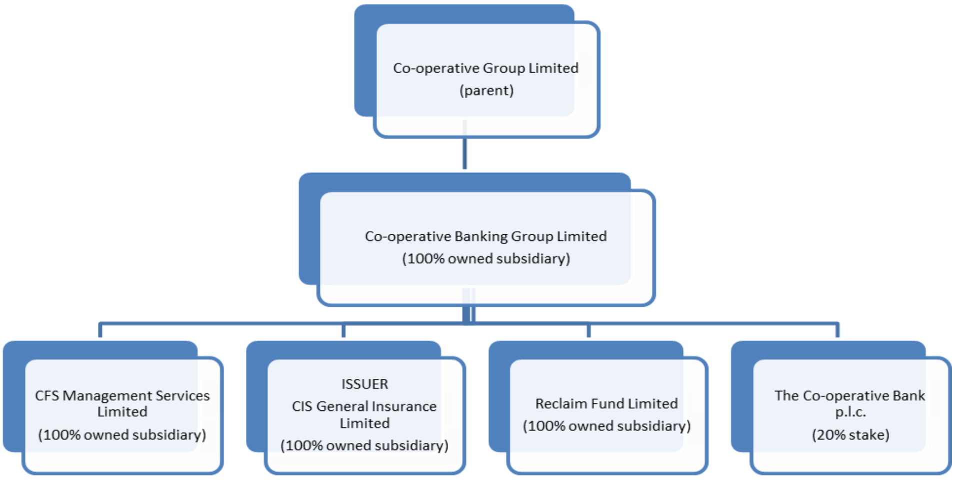
- 2005: Co-operative Insurance Society Limited split its life and general insurance businesses and CIS General Insurance Limited was incorporated.

- 2006: First insurer to launch an Eco-Motor Insurance policy.

- 2011: First major insurer to introduce a telematics product to help lower the cost of insurance for young drivers.

Organisational Structure of the Co-operative Group

The following chart shows a simplified summary of the organisational structure of the Co-operative Group and highlights the Issuer's position within the Co-operative Group.



Principal Activities

The Issuer is a manufacturer and distributor of general insurance products, under the Co-operative Insurance brand. The Issuer's principal products are Motor Insurance and Home Insurance as more particularly described below. Insurance policies are originated and distributed through a range of retail channels which currently include direct website and telephone sales, sales via other Co-operative Group businesses, brokers and price comparison websites. For FY 2014, approximately 62 per cent. of new policies were originated directly by the Issuer or via other Co-operative Group businesses, 14 per cent. via brokers and 24 per cent. via price comparison websites.

The Issuer's operating model is based on the provision of most operating functions in-house (i.e. sales and service, claims contact centres and claims handling and back office functions). Certain products, such as the Young Driver Insurance product (as described below), and sales via the aggregator channel are provided with operating model components by specialist third parties that have been used to provide the technological solution for these products.

The Issuer also markets and distributes commercial lines products for small and medium size enterprises, underwritten by specialist third party providers and acts as an introducer to specialist broker partners for larger corporate risks, where relevant. As at the date of the Prospectus, the Issuer also currently underwrites a small amount of commercial insurance, which is fully reinsured, although the Issuer is looking to cease such underwriting in the near future.

Products

Motor Insurance – comprehensive insurance covers against liability for both bodily injury and property damage; for physical damage to an insured's vehicle from collision, including 24 hour accident recovery service; and for loss resulting from fire or theft including replacement of keys.

The following optional covers are also available:

- Motor Breakdown Cover and Accident Recovery Services - provided in association with AXA Assistance (UK) Ltd;
- Enhanced Courtesy - provided by Albany Assistance Ltd;

- Extended foreign use cover for longer travel periods in Europe; and
- Motor Legal Expenses cover - underwritten by CISGIL acting through The Co-operative Legal Services Ltd.

The following related products available include:

- *Young Driver Insurance* – insurance cover designed specifically for drivers aged between 17 and 24 and their parents and underwritten by CISGIL. Smartbox technology is used with the aim of reducing insurance premiums through safe and responsible driving. Through Smartbox technology a box is installed inside the insured's vehicle to record driving behaviour data.

Additional covers also available with this product:

- Breakdown cover provided by RAC Motoring Services (RAC Insurance Ltd);
- Gadget cover is administrated by Supercover Insurance Ltd and underwritten by Ageas Insurance Ltd;
- Key cover is administered by Boomerang-Tag Ltd and underwritten by Ageas Insurance Ltd; and
- Motor Legal Expenses cover is underwritten by CISGIL acting through Co-operative Legal Services Ltd.

- *Motor Breakdown Cover* from the Co-operative Insurance is provided by Axa Assistance (UK) Ltd. Annual and Short trip covers are separately available.

Home Insurance – insurance covers against loss of or damage to the buildings and contents of private residences including cover for underground pipes, drains and cables, cover for domestic outbuildings at the insured address, including sheds, garages and greenhouses; and legal expenses cover. Home Legal Expenses cover is underwritten by CISGIL acting through Co-operative Legal Services Ltd.

The following optional covers are available:

- Home Emergency cover branded HomeRescue Plus **-** provided by AXA Assistance (UK) Ltd;
- Building Accidental Damage – offers further protection against accidents arising from, for example, DIY drilling through a pipe or cable;
- Personal Possessions– allows customers to insure their possessions outside of the home; and
- Contents Accidental Damage – provides further protection against damage such as paint spills on carpet or furniture.

Other **General Insurance** products are distributed under the Co-operative Insurance brand, and underwritten mainly by specialist third party providers as follows:

- *Pet Insurance* - insurance covers veterinary treatment fees, death or loss of pet, third party liability and boarding fees. Cover is provided, underwritten and administered by Allianz Insurance plc. Dog and Cat Insurance are separately available.

- *Business Insurance* **–** insurance cover tailored to the needs of a wide range of business needs underwritten by CISGIL but reinsured 100 per cent. to Aviva Insurance Ltd including Self-employed Insurance; Office and Surgery Insurance; Shop and Salon Insurance; Landlord Insurance; and Pub, Restaurant and Hotel Insurance. Business insurance is also directed to and underwritten by Aviva Insurance Ltd for Motor Fleet Insurance and Motor Trade Insurance.

- *Van Insurance* - arranged and administered by Vehicle Direct Insurance Services (a trading style of Brightside Insurance Services Ltd) and underwritten by a panel of insurers.

- *Historic Insurance* – in the past the Issuer provided commercial insurance cover primarily but not exclusively for Co-operative businesses. Cover is no longer provided, however this is long tail business for which incurred but not reported claims could still arise.

Principal markets

The Issuer operates in the UK general insurance market and does not operate or offer any insurance products or services outside the UK, Channel Islands and the Isle of Man.

Summary Financial Information

	Financial Year	
	FY 2013	FY 2014
Combined Operating Ratio	100.5%	106.9%
Gross Written Premiums	£443.6m	£365.2m
Investment Return	£40.9m	£23.6m
Profit/loss before taxation	£33.6m	£-6.8m
Profit/loss after taxation	£27.7m	-£6.9m
Capital Resources Requirement	£181.9m	£83.8m
Excess of available capital	£153.2m	£260.3m

The Issuer recognised a loss after tax of £6.9m in FY 2014 (FY 2013 profit of £27.7m). This reflects a challenging market for general insurers with an average decrease in motor premiums over the year of approximately 10 per cent. combined with storms and floods in the first quarter that cost the industry approximately £450m and which led to a significant increase in claims incurred. The negative impact of the challenging market conditions and occurrence of natural events was further compounded by adverse media coverage surrounding the Co-operative Group in the first half of 2014 which affected sales.

The Issuer's gross written premium decreased from £443.6m (FY 2013) to £365.2m (FY 2014). During this period the proportion of premium earned between Motor, Home and Other remained constant. For FY 2014, 62.6 per cent. of premium earned was from Motor Insurance and related products, 36.9 per cent. from Home Insurance and related products and 0.5 per cent. from other general insurance products.

The Issuer's investment result decreased from £40.9m (FY 2013) to £23.6m (FY 2014). The investment portfolio in FY 2014 consisted on average of 83 per cent. Fixed Interest securities (Corporate bonds/Gilts) and 17 per cent. cash. The bonds are classed as 'Available for Sale' and the cash as 'fair value through the income statement'. The FY 2014 decrease in the investment result noted above reflects a £10m reduction in gains realised through the sales of investments and also a reduction in the value of the portfolio. This, along with a move to a more risk averse mix of holdings, has resulted in a reduction to the bond income earned. The result does not include an increase of £20.4m in the Available for Sale reserve. For further information on the fair value of financial assets on the Issuer please see page 52 of the 2014 financial statements set out at page F-042 of Appendix 1 to this Prospectus.

The Issuer's combined operating ratio (**COR**) increased from 100.5 per cent. (FY 2013) to 106.9 per cent. (FY 2014). This reflects very challenging market conditions, particularly in the

Motor insurance sector where the average COR across companies in the sector has risen to 109 per cent.

As at 31 December 2014, the Issuer had total assets of £1,174m as compared to £1,272m in FY 2013, net assets (total assets less liabilities) of £381m as compared to £283m in FY 2013 and financial assets and cash and cash equivalents of £913m as compared to £962m in FY 2013.

Capital Position

The Issuer's capital requirements are prescribed by the PRA rules which implement certain EU insurance directives and provide additional standards applicable to the UK. These rules are described in detail in "*Regulatory Overview – UK Regulatory Environment – Regulatory Capital*" below. See also "*Risk Reduction and Capital Management*" below.

Strategy

The Issuer completed its 2014 Strategic Review in 2014. This was conducted with and validated by external consultants. The Issuer aims to be "the go to insurance provider for Co-operative members" with a continued focus on Motor and Home Insurance products. The key elements of the strategy to achieve this strategic goal are:

- Focus on existing customers of the Co-operative Group;
- Build strong data and analytical capabilities to utilise and leverage data captured by the Co-operative Group;
- Develop key distribution partnerships; and
- Reduce risk to diversify income (and volatility) and reduce regulatory capital requirements.

To support the strategy the Issuer intends to leverage three sustainable competitive advantages:

- Brand – utilising the Co-operative brand to support a proposition based around "insurance done better" in a market which is mistrusted, yet where trust remains an important driver of purchase choice. Research has shown that the Co-Operative brand still resonates strongly with consumers in this area.

- Privileged access to data – the Issuer has the benefit of access to the data of members of Co-operative Group companies. The available data provides a valuable insight into behaviour and potential insurance requirements of Co-operative members which yields advantages in insurance risk assessment (which can support better pricing), and recruitment (through increased marketing effectiveness).

- Distribution reach– active marketing direct to consumers and through other Co-operative Group businesses with a focus on members will provide additional opportunities. This will be supported by widening the competitive position and underwriting footprint through the creation and operation of a panel of other underwriters supporting the Issuer proposition.

To ensure the correct focus is placed on developing and implementing the strategy, a specific governance structure has been introduced around the business transformation programme. A specific Board Committee, the Board Transformation Committee has been formed with overall responsibility for delivering the programme, which reports directly to the Issuer's Board. In addition to the Board Transformation Committee, there is a pyramid of further committees with responsibilities for specific aspects of the transformation programme. Reporting to the Board Transformation Committee are the Transformation Executive Steering Committee and the Business Design Authority which are the primary forums for the delivery of the transformation programme and which are accountable for managing the transformation, in particular overseeing cost, quality, timing and scope. There are a number of further sub-committees with reporting lines to the Transformation Executive Steering Committee and the Business Design Authority. These reporting lines ensure that there is a properly understood and functional methodology to provide oversight and direction to the plan and an established escalation process for decision making and risk assessment. By separating the transformation programme reporting structure from the day-to-day management of the business, the objective is to ensure that appropriate actions necessary for the business to continue functioning are taken while the strategy implementation teams retain the correct focus.

Operating Model

The operating model was reviewed as part of the 2014 Strategic Review and a number of issues identified, both in its current operations and as a model for moving forward. The lack of flexibility inherent in the Issuer's IT processes and legacy systems has meant that while business levels have been falling the fixed nature of a number of costs within the business has resulted in a commission and expense ratio in FY 2014 of 40.2 per cent. compared to 31.1 per cent. in FY 2013 which is significantly higher than the Issuer's competitors and is not sustainable. The Issuer concluded during the period of the 2014 Strategic Review that, while it would be possible to improve performance by taking actions in the identified areas under the existing operating model, to fully deliver its strategic goals it would be necessary to establish a programme to transform its technology capabilities as follows:

- A new operating model will be supported by a new technology solution which will be delivered by an experienced system integrator using a platform already proven in the UK insurance market and delivered through third parties.

- Capabilities will be improved in key areas such as pricing, data, proposition and distribution by strengthening the leadership team and leveraging the capabilities offered by the new platform.

- Operational improvements will be made in the current operating model to minimise the drag on short-term profitability whilst the transformation is executed.

The Issuer plans to design, configure and implement the new technology solution in 2015. It plans to write new business on this platform from early 2016 and to transfer existing business from mid-2016.

The new operating model thus implemented is expected to bring expense ratios in line with market levels, to give the flexibility to properly utilise the data available from within the Co-operative Group, to increase premium and new business volume and to enable the planned expansion of distribution partnerships.

The Issuer's profitability and capital base will be significantly impacted by the build costs of the new platform, both internal and external, and the need to dual run the existing and new operating models until all policies are transferred onto the new platform by mid-2017. Ways to accelerate this timeline will be considered, but these will be assessed against any potential increase in execution risk as the success of the transformation programme is fundamental to the ongoing success of the organisation.

Risk Reduction and Capital Management

The Issuer has already improved the overall quality of its capital base through the issuing of £85m of equity (tier one capital) in December 2014, the proceeds of which have been used to repay existing tier two subordinated loans. However, at present, the Issuer's buffer capital is below the minimum level of capital (the 1-in-6 year event buffer capital threshold) which the Issuer aims to hold in accordance with its risk appetite (described in "Risk Factors - *Failure to* *maintain adequate capital could have a variety of negative regulatory and operational implications for the Issuer*").

Regulatory capital requirements are determined by reference to the risks faced by the business. Consequently, it is possible to reduce capital requirements by executing actions that reduce risk, albeit often resulting in reduced returns. Management have identified potential actions related to the risks faced by the business which fall into three main categories:

- Actions to reduce insurance risk through reinsurance for future large claims or catastrophe and adverse development cover (**ADC**) for existing reserves. These actions will reduce the potential volatility of the Issuer's results, thus having a positive impact on capital requirements;

- Actions to reduce other types of risk – for example, de-risking the investment portfolio; and

- Actions that would require an increased risk appetite.

There are credible and material actions available in the first two categories for implementation later within 2015. No actions are being taken that would require an increased risk appetite as this is not felt to be appropriate at this time.

As part of the Issuer's management of these risks, on 1 April 2015 the Issuer signed up to an ADC arrangement which the Issuer expects to generate capital benefits under the current regulatory capital framework. The ADC arrangement impacts the Issuer's capital position by reducing the volatility of the reserves thus reducing the ICA. The Issuer estimates that the impact of the ADC cover will be equivalent to an increase in the ICG coverage ratio as at 31 December 2014 from 118 per cent. to approximately 124 per cent. The capital benefit of this cover can be expected to continue during 2015 while the current regulatory capital framework is in force. Although the ADC arrangement reduces overall risk within the business, once the Solvency II framework comes into effect from 1 January 2016, using the standard formula (as described in "*Recent and future developments – Solvency II*") the ADC arrangement will have no direct impact on the calculation of the SCR, and hence capital coverage going forward.

The New Capital will provide the capital required (i) to bring the Issuer back within its risk appetite and increase the Issuer's buffer capital to above 31 per cent. of the ICA (its 1-in-6 year event buffer capital threshold) and (ii) to support the transformation programme, which will impact on the capital base of the Issuer as discussed in "*Strategy – Operating Model*" above. The Issuer expects to meet the costs of the Notes, including interest payments thereon, through the cash flows generated by the Issuer's business but this is largely dependent upon the Issuer realising the cost savings and other benefits from effectively implementing the new IT platform and operating model (see "*Strategy – Operating Model*").

Directors of the Issuer

The following is a list of directors of the Issuer and their principal directorships (if any) performed outside of the Issuer which are, or may be, significant with respect to the Issuer, as at the date of this Prospectus. The business address of each of the directors referred to below is at Miller Street, Manchester, M60 0AL.

Name	Position at the Issuer	Principal Directorships performed outside of the Issuer (if any)
Alistair Hugh Asher	Non-Executive Director	Co-operative Legal Services Limited, NOMA (GP) Limited, The Co-operative Trust Corporation Limited,

		and Federal Retail and Trading Services Limited.
Caroline Elizabeth Fawcett	Non-Executive Director	Engage Mutual Assurance, Customer Experience First Ltd, Homeowners Friendly Society.
David William Lister	Non-Executive Director	Nuffield Health, Department of Work and Pensions and The Tech Partnership.
Neil McKenzie	Non-Executive Director	Judge Business School Executive Education Limited.
Robert Newton	Chairman	Silentair Group Limited, Silentair Limited, Silentair Systems Limited, Reclaim Fund Limited, Co-operative Banking Group Limited.
Graham Lloyd Singleton	Non-Executive Director	Tayam Consulting Limited.
Mark Andrew Summerfield	Executive Director	None.

Potential conflicts of interest between a director's duties to the Issuer and his or her private interests and/or other duties arise from:

- Alistair Asher's role as General Counsel of Co-operative Group Limited, the ultimate holding company of the Issuer; and

- Robert Newton's directorship of Co-operative Banking Group Limited (CBGL) and CBGL's relationship as the Issuer's parent company which also owns the Issuer's main internal service company CFSMS.

Except for the potential conflicts of interest listed above and as policyholders, no director of the Issuer has any actual or potential conflicts of interest between any of his or her duties to the Issuer and his or her private interests and/or other duties.

Litigation

The Issuer has a contract with Parabis Ltd for the provision of claims handling services for third party motor claims. Such services are currently treated as VAT exempt. HMRC are challenging this view. If this challenge is upheld, the Issuer will be liable for approximately £3.0m in VAT payments. The Issuer's legal counsel has indicated that the challenge is unlikely to be upheld and no provision has been made in the financial statements.

REGULATORY OVERVIEW

The Issuer is a general insurance company authorised in the United Kingdom by the PRA and is subject to the FSMA. Following the reform of the UK regulatory system (as described further below), from 1 April 2013, the Issuer is dual-regulated, i.e. it is subject to regulation and supervision by both the PRA (as regards prudential and organisational requirements) and the FCA (as regards conduct of business requirements).

UK domiciled insurers must comply with the rules and guidance of the PRA and the FCA made under the FSMA. Important sources of these rules and guidance are set out in the PRA Handbook (the **PRA Handbook**) (which contains the PRA's rules and other provisions), the PRA Rulebook (the **PRA Rulebook**) (which contains rules and directions made by the PRA that apply only to PRA authorised firms) and the FCA Handbook of Rules and Guidance (the **FCA Handbook** and together with the PRA Handbook and PRA Rulebook, the **FS Handbook**). It is the intention of the PRA to gradually phase out the PRA Handbook, but at present, the PRA Handbook must be read in conjunction with the PRA Rulebook provisions to understand the full set of applicable requirements. In June 2014, the PRA introduced the "Fundamental Rules" (a high level expression of the PRA's objectives and expectations of regulated firms) which apply to PRA authorised firms, and can be found in both the PRA Handbook and PRA Rulebook. These are similar to the "Principles for Businesses" (a general statement of the fundamental obligations of firms under the regulatory system) which can be found in the FCA Handbook. As dual regulated firms, insurers will be required to comply with both the Fundamental Rules and the Principles of Business.

The following discussion considers the main features of the UK regulatory regime for insurance businesses as it applies to the Issuer.

UK REGULATORY ENVIRONMENT

Financial Services Act 2012

On 1 April 2014, the PRA and the FCA replaced the Financial Services Authority and became the regulators for persons authorised under the FSMA to undertake regulated activities in the financial services sector in the UK. The reforms were implemented under the Financial Services Act 2012 (the **Financial Services Act**). The PRA (a subsidiary of the Bank of England) oversees and is responsible for the prudential regulation of banks, building societies, insurers, credit unions and some large investment firms. The FCA (a separate legal entity) is responsible for conduct of business regulation for all authorised firms, market regulation and the prudential regulation of firms not authorised by the PRA. The Financial Policy Committee (which also sits within the Bank of England) is responsible for the macro-prudential regulation of the entire financial services sector.

The role of the PRA is defined in terms of two statutory objectives: to promote the safety and soundness of the firms it regulates; and (specifically for insurers) to contribute to the securing of an appropriate degree of protection for policyholders. The FCA has an overarching strategic objective to ensure that relevant markets function well and this is underpinned by three operational objectives. These are securing an appropriate degree of protection for consumers, protecting and enhancing the integrity of the UK financial system and a new objective relating to the promotion of effective competition in the interests of consumers.

The PRA and the FCA have extensive powers to supervise and intervene in the affairs of the firms they are responsible for regulating, for example, if they consider it appropriate in order to protect policyholders against the risk that the firm may be unable to meet its liabilities as they fall due, that the threshold conditions (see further below) may not be met, that the firm or its parent has failed to comply with obligations under the relevant legislation or rules, that the firm has furnished them with misleading or inaccurate information or that there has been substantial departure from any proposal or forecast submitted to the relevant regulator.

The FCA also has the power to take a range of informal and formal disciplinary or enforcement actions in relation to a breach by a firm of the FSMA or the rules in the PRA or FCA Handbooks, including private censure, public censure, restitution, fines or sanctions and the award of compensation. The PRA (or FCA where relevant) may also cancel or vary (including by imposing limitations on) the firm's authorisation, including in the case of an insurer cancelling permission to write new policies, thereby putting the firm into run-off.

The Financial Services Act also conferred new powers on the PRA and FCA. For example, the PRA has the following three new powers that can, in certain circumstances, be applied directly to qualifying parent undertakings where those parent undertakings are not themselves regulated:

(a) power of direction;

(b) a rule-making power for information gathering; and

(c) a supporting disciplinary power to fine or censure a qualifying parent undertaking for breaches of a direction or an information rule.

The FCA was granted new early intervention powers which enable it to intervene directly in the market and make product intervention rules and withdraw misleading financial promotions with the aim of preventing harm to consumers. In April 2014, the FCA took over from the Office of Fair Trading to become the regulator for the consumer credit industry.

Permission to Transact Business

Subject to the exemptions provided in the FSMA, no person may effect or carry out contracts of insurance (referred to below as carrying on **insurance business**) in the United Kingdom unless authorised to do so under the FSMA by the PRA. The PRA has authority to grant regulatory permission to provide insurance for one or more of the classes of business recognised by the EU insurance directives. In deciding whether to grant authorisation, both the PRA and the FCA are required to determine whether the applicant satisfies the requirements of the FSMA, including the applicant's ability to meet a set of "threshold conditions" (the **Threshold Conditions**). These are the minimum conditions that must be satisfied (both at authorisation and on an on-going basis) in order for a firm to gain and to continue to have permission to undertake regulated activities in the United Kingdom.

The PRA and FCA are each responsible for assessing a set of Threshold Conditions. At a high level, the PRA Threshold Conditions require an insurer's head office to be in the UK, for the business to be conducted in a prudent manner (and in particular that it maintains appropriate financial and non-financial resources), that the insurer is fit and proper and appropriately staffed and that it is capable of being effectively supervised. Although there is a degree of cross-over with the FCA's Threshold Conditions, the FCA considers them from a customer perspective and, in addition, includes a condition relating to the insurer's business model and the need for the strategy for doing business to be suitable for its regulated activities. As dual-regulated firms, insurance companies are required to satisfy both the PRA's as well as the FCA's Threshold Conditions.

FS Handbook

Authorised firms, where they are dual-regulated, are also required to comply with the Principles for Businesses, the Fundamental Rules and the requirements of the FS Handbook. The FS Handbook comprises a number of sourcebooks which set out the rules which apply to regulated firms.

The Principles for Businesses and the Fundamental Rules

PRA-authorised insurance companies are subject to certain overarching principles issued by the PRA and the FCA. These principles are intended to ensure fairness and integrity in the provision of financial services in the UK and contain the fundamental obligations of insurers. In particular, the Principles for Businesses promulgated by the FCA require a firm to:

a) conduct its business with integrity;

b) conduct its business with due skill, care and diligence;

c) take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems;

d) maintain adequate financial resources;

e) observe proper standards of market conduct;

f) pay due regard to the interests of its customers and treat them fairly;

g) pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading;

h) manage conflicts of interest fairly, both between itself and its customers and between a customer and another client;

i) take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgement;

j) arrange adequate protection for clients' assets when it is responsible for them; and

k) deal with its regulators in an open and cooperative way, and to disclose to the appropriate regulator anything relating to the firm of which that regulator would reasonably expect notice.

The Fundamental Rules require a PRA authorised firm to:

a) conduct its business with integrity;

b) conduct its business with due skill, care and diligence;

c) act in a prudent manner;

d) maintain adequate financial resources;

e) have effective risk strategies and risk management systems;

f) organise and control its affairs responsibly and effectively;

g) deal with its regulators in an open and cooperative way and disclose to the PRA anything relating to the firm which the PRA would reasonably expect to have notice of; and

h) prepare for resolution so that, if the need arises, a matter can be resolved in an orderly manner with minimum disruption of critical services.

Conduct of business rules

Conduct of business rules (**ICOBS Rules**) forming part of the FS Handbook, regulate the day-to-day conduct of business standards to be observed by authorised firms in carrying out regulated activities. The scope and range of obligations imposed on an authorised firm under the ICOBS Rules vary according to the scope of the firm's business and the nature of its clients. Generally, the obligations imposed on an authorised firm by the ICOBS Rules will include the need to provide clients with information about the firm, meet certain standards of product disclosure, ensure that promotional materials which it produces are clear, fair and not misleading, assess suitability when advising on certain products, manage conflicts of interest, report appropriately to its clients and provide certain protections in relation to client assets.

TCF

The FCA is responsible for ensuring that authorised firms treat customers fairly (**TCF**) in line with Principle 6 of the Principles for Businesses, and communicate with customers in a manner that is clear, fair and not misleading. The FCA has established six key outcomes it expects firms to focus on as part of their TCF strategy, including that consumers can be confident they are dealing with firms where the fair treatment of customers is central to the firm's corporate culture, and that products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

The Approved Persons regime

The regulatory approach of the PRA and the FCA is to place personal responsibility on individuals who are able to exercise significant influence over an authorised firm, including an insurer. In particular, an authorised insurer is required to obtain PRA (or, depending on the controlled function, FCA) approval for any individual who carries on any specific "controlled function", such as, for example, executive or non-executive directors and persons responsible for risk management, internal audit or compliance. These individuals are known as "Approved Persons" (**Approved Persons**) and must comply with a set of principles which largely mirror the Principles for Businesses referred to above.

The PRA (or the FCA, as the case may be) will only approve an individual to undertake a controlled function if that individual is assessed to be a fit and proper person. In particular, the PRA (or, where relevant, the FCA) must be satisfied as to the person's honesty, integrity and reputation, competence and capability for the role that the person is to assume in the firm and financial soundness.

Regulatory Capital

Rules in force in the UK (in large part implementing EU insurance directives) require insurance firms (and, on a consolidated basis, groups of which insurance firms are members) to maintain capital resources equal to, or in excess of, their applicable capital resources requirement. Detailed rules define how to calculate the capital resources requirement and what constitutes capital for these purposes. Under the General Prudential Sourcebook (**GENPRU**), individual companies permitted to carry on insurance business in the UK are required to maintain a minimum level of capital (the "minimum capital requirement" or **MCR**) consistent with the EU insurance directives. Detailed rules in GENPRU and the Prudential Sourcebook for Insurers (**INSPRU**) define how to calculate the capital resources requirement and what constitutes capital for these purposes.

The MCR for a general insurance firm is calculated as the higher of (i) the base requirement (EU directive minimum) and (ii) the general insurance capital requirement (which is itself calculated as the highest of the "premiums amount", the "claims amount" and the "brought-forward amount" which are each calculated according to rules and guidance in INSPRU).

In addition, general insurers are required to calculate an enhanced capital requirement (**ECR**) which serves as an indicative measure of the capital resources, in particular the individual capital assessment that the firm may need to hold, based on risk-sensitive calculations applied to insurance, credit, market and other risks arising in relation to its business profile. Again, this is calculated according to rules and guidance in INSPRU.

Rules in the PRA Handbook and INSPRU require an insurer to calculate its capital requirements through its own risk assessment (known as an **individual capital assessment** or **ICA**). If the PRA disagrees with an insurer's ICA, it may draw up its own "individual capital guidance" (**ICG**) for the insurer, which it will provide on a confidential basis. An ICG can be imposed as a requirement on the scope of the insurer's permissions, resulting in that ICG becoming mandatory for the insurer.

Supervision and enforcement

The PRA and FCA have extensive powers to investigate and intervene in the affairs of insurers. In relation to dual-regulated firms, under the terms of a Memorandum of Understanding entered into in April 2013, the PRA and FCA will consult each other before taking enforcement action. The PRA has the right to veto certain FCA regulatory actions in relation to dual regulated firms, but the FCA is not required to comply if in its opinion it would be incompatible with any EU or other international obligation of the UK.

The regulator's enforcement powers, which may be exercised against insurers as well as and Approved Persons, include public censure, imposition of unlimited fines and, in serious cases, the variation or revocation of permission to carry on regulated activities or of an Approved Person's status. The FCA may also vary or revoke an insurer's permissions to protect the interests of consumers or potential consumers if the insurer has not engaged in regulated activity for 12 months, or if it is failing to meet the Threshold Conditions for authorisation. The FCA has further powers to obtain injunctions against Approved Persons and to impose or seek restitution orders where consumers have suffered loss.

In addition to applying sanctions for market abuse, the FCA has the power to prosecute criminal offences arising under the FSMA and insider dealing under Part V of the Criminal Justice Act 1993, and breaches of money laundering regulations. The FCA's stated policy is to pursue criminal prosecution in all appropriate cases.

Consumer complaints and compensation

Insurance companies, along with all other regulated firms and certain other unregulated businesses, are under the compulsory jurisdiction of the Financial Ombudsman Service (**FOS**) which has been set up under the FSMA. The FOS operates independently of the PRA and the FCA and deals with disputes for certain categories of customer complaints, including complaints about mis-selling, misleading advertisements, unsuitable advice, unfair treatment, maladministration and delay and poor service provided by firms. It is funded by levies and case fees which businesses it covers are required to pay by law. The FOS provides an alternative to customers bringing complaints in the courts and is empowered to order a firm to pay fair compensation for any loss or damage it causes to a customer as a result of the firm breaching any applicable rule.

The Financial Services Compensation Scheme (**FSCS**) has been established under the FSMA and provides compensation to certain categories of customers who suffer losses as a consequence of the inability of a regulated firm to meet its liabilities arising from claims made in connection with regulated activities. The FSCS is funded by means of levies on all its participating financial services firms, including insurers. The levy is calculated separately for each class of financial services, although there are circumstances in which one class of financial services firms can be required to pay levies to fund payments to customers of a financial services firm of another class that is in default.

The Motor Insurers' Bureau (**MIB**) was set up in 1946 to provide a way of compensating the victims of uninsured or untraced motorists. Every insurer underwriting compulsory motor insurance is obliged, by virtue of the Road Traffic Act 1988, to be a member of the MIB and to contribute to its funding. The amount that each member contributes is calculated by means of a formula and is relative to the level of gross premium income generated by the member.

Financial crime

It is one of the FCA's statutory objectives to protect and enhance the integrity of the UK financial system and the FCA is under a duty to consider the importance of minimising the risk of the firms it regulates being used for financial crime. It therefore looks at the measures a firm takes to monitor, detect, and prevent financial crime. This includes measures in respect of money laundering, terrorist financing, data security, bribery and corruption, fraud and sanctions breaches.

All the FSMA authorised firms are required to undertake certain administrative procedures and checks, which are designed to prevent money laundering. The FCA's Senior Management Arrangements, Systems and Controls sourcebook (**SYSC**) contains rules which require firms to take reasonable care to establish and maintain effective systems and controls for countering the risk that the firm might be used to further financial crime. For these purposes, financial crime includes any offence involving fraud or dishonesty, misconduct in, or misuse of information relating to, a financial market or handling the proceeds of crime, as well as bribery and corruption offences.

Gender discrimination in contracts of insurance

As a result of a decision of the European Court of Justice on gender equality, there is a risk that the exemption from the age discrimination provisions under the Equality Act 2010 (which allows insurers to take age into account in the assessment of risk) may be open to challenge. The Issuer's ability to price risk effectively and accurately may be affected if the use of age as a factor in risk assessment is prohibited. The impact of this may be heightened by the fact that, following the 2011 decision of the European Court of Justice, ruling that gender-related factors could not be used in determining premiums and benefits under insurance policies, the Issuer is no longer able to use gender as a factor in pricing risk. This prohibition came into effect in the United Kingdom on 21 December 2012 by means of an amendment to the Equality Act 2010.

Data Protection

The Data Protection Act 1998 (the **DPA**), which came into force in March 2000 and gives effect to an EU Directive, regulates in the UK the obtaining and use of personal data relating to living individuals. Personal data includes any data about an individual by which he or she can be identified (including, for example, a name, address, age, bank or credit card details). The data need not be private or confidential. The DPA applies to both computerised data and to certain sets of manual data such as address books and filing systems. It lays down certain principles which, in general, must be followed by those who hold personal data. The Issuer and everyone working at the Issuer's businesses must comply with local jurisdiction data protection and privacy requirements. Breach of the DPA may give rise to criminal or civil liability and other enforcement action can be taken.

EU AND EEA REGULATORY ENVIRONMENT

The European Union Life and Non-Life Insurance Directives (the **EU Insurance Directives**) establish a framework for regulation of insurers in the European Union which is extended to the European Economic Area (**EEA**). The EU Insurance Directives provide that an authorisation to carry on insurance business granted by the insurance regulator in an EEA member state where the insurer is incorporated or has its head office (a **home state regulator**) is valid for the entire EEA (the **passporting right**). The home state regulator determines the procedures for exercising the passporting right depending on whether an insurer proposes to establish a branch or provide insurance services on a cross-border basis in another EEA member state (a **host state**).

Generally, in accordance with the principles set out in the EU Insurance Directives, prudential regulation of an insurer is a matter for its home state regulator whereas the conduct of business and marketing requirements applicable in a host state are determined by the host state regulator.

Distance Marketing Directive

Under the Distance Marketing Directive, EU member states are required to implement a framework of rules and guidance in order to protect consumers by:

(i) setting minimum standards for information that must be provided to consumers before entering into a financial services contract by means of distance communication, which includes sales taking place on-line, by email, post or telephone; and

(ii) for certain products and services, giving a cooling-off period in which a consumer may cancel a contract without penalty.

Insurance Mediation Directive

The Insurance Mediation Directive (**IMD**) requires EU member states to establish a framework to:

(i) ensure that insurance and reinsurance intermediaries have been registered on the basis of a minimum set of professional and financial requirements;

(ii) ensure that registered intermediaries will be able to operate in other member states by availing themselves of the freedom to provide services or by establishing a branch; and

(iii) impose requirements on insurance intermediaries to provide specified minimum information to potential customers.

A proposal for a revision of the IMD was adopted by the European Commission in 2012 (**IMD 2**), and its objective is to upgrade consumer protection in the insurance sector by creating common standards across insurance sales and ensuring proper advice.

Recent and future developments

Solvency II

Solvency II (comprising the Solvency II Directive, delegated acts, binding technical standards and guidance) sets out the new solvency regime which will, with effect from 1 January 2016, replace the current EU regulatory framework for the prudential supervision of insurers and reinsurers (currently set out in the EU Insurance Directives, and implemented in the UK under the FSMA and the FS Handbook).

Solvency II adopts a three pillar approach to prudential regulation:

(a) Pillar 1 relates to quantitative requirements, covering technical provisions, capital requirements and the rules on valuation;

(b) Pillar 2 covers risk management, governance requirements, the "own risk and solvency assessment" and supervisory review; and

(c) Pillar 3 covers public and supervisory reporting and disclosure.

Although the Solvency II Directive has some similarities to the current UK regime set out in the FS Handbook, the implementation of the Solvency II regime will result in important changes to the regulation of insurers in the EU, including the introduction of a risk sensitive capital requirement (the **Solvency Capital Requirement** or **SCR**) which can be calculated using a prescribed methodology known as the "standard formula", an approved internal model or a combination of the two. The Issuer intends to calculate its SCR using the standard formula.

Solvency II provides less flexibility for the regulators to exercise discretion with respect to supervisory decisions and, under Solvency II, the European Insurance and Occupational Pensions Authority (**EIOPA**) will have an increased role being able to exercise certain powers potentially affecting UK insurers, such as powers to resolve disagreements between national supervisors and to act as a coordinator in "emergency situations". EIOPA may also issue binding technical standards and monitor compliance by European Member States.

Fourth Anti Money Laundering Directive

In February 2013 the European Commission adopted a legislative proposal for a fourth money laundering directive (**MLD4**). MLD4 is likely to be published in the Official Journal during 2015, and to take effect two years after its publication. Key changes introduced by MLD4 will include changes to the scope of the anti-money laundering regime, measures designed to provide enhanced clarity and accessibility with regard to beneficial owner information, a tightening of the rules on when simplified due diligence can be used and a strengthening of the sanctioning powers of national supervisors through the introduction of a set of minimum principles-based rules. It remains unclear how MLD4 will be implemented both at a European and Member State level.

EU Data Protection Legislation

Draft amendments to EU data protection legislation have been proposed. If enacted, these amendments would lead to substantial changes to UK data protection laws. On 12 March 2014, the European Parliament approved an amended draft of the European Commission's proposed General Data Protection Regulation (**Draft GDPR**). The Draft GDPR differs from the Data Protection Directive (95/46/EC) (which it will replace) in respect of, among other things, territorial reach, sanctions, right to erasure and changes in the role of data processors. Political agreement on the Draft GDPR is not expected to be reached before the summer of 2015, and the regime is not expected to apply before Spring 2018 (two years after the expected adoption of the Draft GDPR).

TAXATION

United Kingdom Taxation

The comments below, which are of a general nature and are based on the Issuer's understanding of current United Kingdom law and HM Revenue & Customs published practice, describe only the United Kingdom withholding tax treatment of payments in respect of the Notes. They are not exhaustive. They do not deal with any other United Kingdom taxation implications of acquiring, holding or disposing of Notes. Prospective holders of Notes who are in any doubt as to their tax position or who may be subject to tax in a jurisdiction other than the United Kingdom are strongly advised to consult their own professional advisers.

The Notes issued will constitute "quoted Eurobonds" provided they are and continue to be listed on a recognised stock exchange, within the meaning of Section 1005 Income Tax Act 2007. The London Stock Exchange is a recognised stock exchange for these purposes. Securities will be treated as listed on the London Stock Exchange if they are included in the Official List by the United Kingdom Listing Authority and are admitted to trading on the regulated market of the London Stock Exchange. Whilst the Notes are and continue to be quoted Eurobonds, payments of interest by the Issuer on the Notes may be made without withholding or deduction for or on account of United Kingdom income tax.

Interest on the Notes may also be paid without withholding or deduction for or on account of tax either (i) if the interest is payable to a person whose usual place or abode is in the United Kingdom or (ii) where, at the time the payment is made, the Issuer reasonably believes (and any person by or through whom interest on the Notes is paid reasonably believes) that the beneficial owner of the interest is within the charge to United Kingdom corporation tax as regards the payment of interest, provided HM Revenue & Customs has not given a direction that the interest should be paid under deduction of tax.

In other cases, absent any other relief or exemption (such as a direction by HM Revenue & Customs that interest may be paid without withholding or deduction for or on account of tax to a specified Noteholder following an application by that Noteholder under an applicable double tax treaty), an amount must generally be withheld on account of income tax at the basic rate (currently 20 per cent.) from payments of interest on the Notes.

Where Notes are issued at an issue price of less than 100 per cent. of their principal amount, any payments in respect of the accrued discount element on any such Notes should not be subject to any withholding or deduction for or on account of income tax.

Noteholders may wish to note that certain information (including the name and address of the recipient or the beneficial owner of the payments under the Notes) may be obtained by, or be required to be reported to, HM Revenue & Customs. Information may be required to be provided by the registered holder of the Notes, persons who effect or are a party to a transaction in the Notes on behalf of others, registrars and administrators of such transactions, persons who make or receive or are entitled to receive payments derived from the Notes and persons by or through whom interest and payments treated as interest are paid or credited. Any information so reported or obtained may, in certain circumstances, be exchanged by HM Revenue & Customs with the tax authorities of other jurisdictions.

EU Savings Directive

Under the Savings Directive, each Member State of the European Union is required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State or to certain limited types of entities established in that other Member State.

Amendments to the Savings Directive adopted by the Council of the European Union on 24 March 2014 will expand the circumstances in which payments which indirectly benefit an individual resident in another Member State must be reported, including where the payment is made to, or secured for, certain trusts or certain other legal arrangements. The amendments will also expand the range of payments covered by the Savings Directive, in particular to include additional types of income payable on securities.

Member States are required to apply these new requirements from 1 January 2017.

For a transitional period, Austria is instead required, unless during such period it elects otherwise, to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). Once the amendments referred to above are implemented, investors should be aware that withholding in Austria may occur in a wider range of circumstances than at present.

A number of other non-EU countries and territories including Switzerland have adopted similar measures (a withholding system in the case of Switzerland).

The proposed financial transactions tax (FTT)

On 14 February 2013, the European Commission published a proposal (the Commission's Proposal) for a Directive for a common FTT in Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the participating Member States).

The Commission's Proposal has very broad scope and could, if introduced, apply to certain dealings in the Notes (including secondary market transactions) in certain circumstances.

Under the Commission's Proposal the FTT could apply in certain circumstances to persons both within and outside of the participating Member States. Generally, it would apply to certain dealings in the Notes where at least one party is a financial institution, and at least one party is established in a participating Member State. A financial institution may be, or be deemed to be, "established" in a participating Member State in a broad range of circumstances, including (a) by transacting with a person established in a participating Member State or (b) where the financial instrument which is subject to the dealings is issued in a participating Member State.

Joint statements issued by participating Member States indicate an intention to implement the FTT by 1 January 2016.

However, the FTT proposal remains subject to negotiation between the participating Member States and the scope of any such tax is uncertain. Additional EU Member States may decide to participate.

Prospective holders of the Notes are advised to seek their own professional advice in relation to the FTT.

FATCA

Certain provisions of U.S. law, commonly known as "FATCA", impose a new reporting and withholding regime with respect to (i) certain U.S. source payments, (ii) gross proceeds from the disposition of property that can produce U.S. source interest and dividends and (iii) certain payments made by, and financial accounts held with, entities that are classified as foreign financial institutions for purposes of FATCA. In order to avoid becoming subject to a 30 per cent. withholding tax under FATCA, non-U.S. financial institutions must enter into agreements with the U.S. Internal Revenue Service (**IRS Agreements**) (as described below) or otherwise be exempt from the requirements of FATCA. Non-U.S. financial institutions that enter into IRS Agreements or become subject to provisions of local law (**IGA legislation**) intended to implement an intergovernmental agreement entered into pursuant to FATCA (**IGAs**), may be required to identify "financial accounts" held by U.S. persons or entities with substantial U.S. ownership, as well as accounts of other financial institutions that are not themselves participating in (or otherwise exempt from) the FATCA reporting regime. In addition, in order (a) to obtain an exemption from FATCA withholding on payments it receives and/or (b) to comply with any applicable IGA legislation, a financial institution that enters into an IRS Agreement or is subject to IGA legislation may be required to (i) report certain information on its U.S. account holders to the government of the United States or another relevant jurisdiction and (ii) withhold 30 per cent. from all, or a portion of, certain payments made to persons that fail to provide the financial institution with information, consents and forms or other documentation that may be necessary for such financial institution to determine whether such person is compliant with FATCA or otherwise exempt from FATCA withholding.

Under FATCA, withholding is required with respect to payments to persons that are not compliant with FATCA or that do not provide the necessary information, consents or documentation made on or after (i) 1 July 2014 in respect of certain U.S. source payments, (ii) 1 January 2017, in respect of payments of gross proceeds (including principal repayments) on certain assets that produce U.S. source interest or dividends and (iii) 1 January 2017 (at the earliest) in respect of "foreign passthru payments" and then, for "obligations" that are not treated as equity for U.S. federal income tax purposes, only on such obligations that are issued or materially modified on or after the date that is six months after the date on which the final regulations applicable to "foreign passthru payments" are filed in the Federal Register.

On 12 September 2012, the United Kingdom and the United States entered into the Intergovernmental Agreement to Improve International Tax Compliance and to Implement FATCA (the **UK IGA**) and the United States agreed to amendments proposed by the United Kingdom on 7 June 2013. Section 222 of the Finance Act 2013 empowers Her Majesty's Treasury to make regulations giving effect to the UK IGA, which were issued, initially coming into force 1 September 2013, and have been the subject of periodic revisions. The UK IGA provides, *inter alia*, that the governments of the United States and the United Kingdom are committed to work together to develop a practical and effective alternative approach to achieve the policy objectives of foreign passthru payment and gross proceeds withholding. It is not yet certain how the United States and the United Kingdom will address withholding on foreign passthru payments, whether such withholding will be required at all or whether payments on instruments such as the Notes will constitute foreign passthru payments.

Whilst the Notes are in global form and held within the ICSDs, it is expected that FATCA will not affect the amount of any payments made under, or in respect of, the Notes by the Issuer, any paying agent and the Common Depositary, given that each of the entities in the payment chain between the Issuer and the participants in the ICSDs is a major financial institution whose business is dependent on compliance with FATCA and that any alternative approach introduced under an IGA will be unlikely to affect the Notes. The documentation expressly contemplates the possibility that the Notes may go into definitive form and therefore that they may be taken out of the ICSDs. If this were to happen, then a non-FATCA compliant holder could be subject to withholding. However, definitive Notes will only be printed in remote circumstances.

FATCA IS PARTICULARLY COMPLEX AND ITS APPLICATION TO THE ISSUER, THE NOTES AND THE NOTEHOLDERS IS UNCERTAIN AT THIS TIME. EACH NOTEHOLDER SHOULD CONSULT ITS OWN TAX ADVISER TO OBTAIN A MORE DETAILED EXPLANATION OF FATCA AND TO LEARN HOW THIS LEGISLATION MIGHT AFFECT EACH HOLDER IN ITS PARTICULAR CIRCUMSTANCE.

SUBSCRIPTION AND SALE

Pursuant to a Subscription Agreement dated 6 May 2015 (the **Subscription Agreement**), UBS Limited (the **Manager**) has agreed with the Issuer, subject to the satisfaction of certain conditions, to subscribe for the Notes at the issue price of 100 per cent. of their principal amount less commissions. The Manager is entitled to terminate and to be released and discharged from its obligations under the Subscription Agreement in certain circumstances prior to payment to the Issuer.

United States

The Notes have not been and will not be registered under the U.S. Securities Act of 1933 (the "**Securities Act**"). In addition, the Notes are being offered and sold only outside the United States in offshore transactions pursuant to Regulation S, and may not be offered, sold, issued, delivered, or otherwise placed into the United States or to, or for the account or benefit of, U.S. persons except in accordance with Regulation S under the Securities Act ("**Regulation S**") or pursuant to an exemption from the registration requirements of the Securities Act. The Manager represents that it has offered and sold the Notes, and agrees that it will offer and sell the Notes (i) as part of its distribution at any time and (ii) otherwise until 40 days after the later of the commencement of the offering and the Closing Date, only in accordance with Rule 903 of Regulation S. Accordingly, neither it, its affiliates nor any persons acting on its or their behalf have engaged or will engage in any directed selling efforts with respect to the Notes, and it and they have complied and will comply with the offering restrictions requirement of Regulation S. The Manager agrees that, at or prior to confirmation of sale of Notes, it will have sent to each distributor, dealer or person receiving a selling concession, fee or other remuneration that purchases Notes from it during the distribution compliance period a confirmation or notice to substantially the following effect:

"The securities covered hereby have not been registered under the U.S. Securities Act of 1933 (the "**Securities Act**"). In addition, the Notes are being offered and sold only outside the United States in offshore transactions pursuant to Regulation S, and may not be offered, sold, issued, delivered, or otherwise placed in or into the United States or to, or for the account or benefit of, U.S. persons (i) as part of their distribution at any time or (ii) otherwise until 40 days after the later of the commencement of the offering and the closing date of the offering, except in either case in accordance with Regulation S under the Securities Act. Terms used above have the meanings given to them by Regulation S under the Securities Act."

Terms used in this paragraph have the meanings given to them by Regulation S.

The Manager represents that it has not entered and agrees that it will not enter into any contractual arrangement with any distributor (as that term is defined in Regulation S) with respect to the distribution or delivery of the Notes, except with its affiliates or with the prior written consent of the Issuer.

United Kingdom

The Manager has represented warranted and agreed that: (i) it has only communicated or caused to be communicated and will only communicate or cause to be communicated any invitation or inducement to engage in investment activity (within the meaning of section 21 of the FSMA) received by it in connection with the issue or sale of any Notes in circumstances in which section 21(1) of the FSMA would not, if the Issuer was not an authorised person, apply to the Issuer; and (ii) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to such Notes in, from or otherwise involving the United Kingdom.

General

No action has been or will be taken by the Issuer or the Manager that would permit a public offering of the Notes or possession or distribution of this document or other offering material relating to the Notes in any jurisdiction where, or in any circumstances in which, action for these purposes is required. This document does not constitute an offer and may not be used for the purposes of any offer or solicitation in or from any jurisdiction where such an offer or solicitation is not authorised.

Neither the Issuer nor the Manager represents that the Notes may at any time lawfully be sold in or from any jurisdiction in compliance with any applicable registration requirements or pursuant to an exemption available thereunder or assumes any responsibility for facilitating such sales.

GENERAL INFORMATION

Authorisation

1. The issue of the Notes was duly authorised by a resolution of the Board of Directors of the Issuer dated 10 March 2015.

Listing

2. It is expected that the applications for the Notes to be admitted to the Official List of the UK Listing Authority and to trading on the London Stock Exchange's regulated market will be granted on or about 8 May 2015 (subject only to the issue of the Global Certificate) and that such admission will become effective, and that dealings in the Notes on the London Stock Exchange will commence, on or about 11 May 2015. The total expenses related to the admission to trading of the Notes are estimated to be £4,000.

Clearing Systems

3. The Notes have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The ISIN for the Notes is XS1229301731 and the Common Code is 122930173.

   The address of Euroclear is Euroclear Bank SA/NV, 1 Boulevard du Roi Albert II, B-1210 Brussels, Belgium and the address of Clearstream, Luxembourg is Clearstream Banking, 42 Avenue JF Kennedy, L-1855 Luxembourg.

No significant change and No Material Adverse Change

4. There has been no significant change in the financial or trading position of the Issuer since 31 December 2014, nor has there has been any material adverse change in the financial position or prospects of the Issuer since 31 December 2014.

Legal and Arbitration Proceedings

5. Save as disclosed in the section "*Business Description – Litigation*", there are no governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which the Issuer is aware) in the 12 months preceding the date of this document which may have or have in such period had a significant effect on the financial position or profitability of the Issuer.

Auditors

6. The auditors of the Issuer are KPMG LLP, One St. Peter's Square, Manchester, M2 3AE, who have audited the Issuer's accounts, without qualification, in accordance with IFRS for each of the two financial years ended on 31 December 2013 and 31 December 2014.

Documents Available

7. Copies of the following documents will be available for inspection from the specified office of the Paying Agents, so long as any of the Notes remains outstanding:

   (a) the constitutional documents of the Issuer;

(b) the audited financial statements of the Issuer in respect of the financial years ended 31 December 2013 and 31 December 2014, in each case with the audit reports in connection therewith. The Issuer currently prepares audited accounts on an annual basis;

(c) the Trust Deed;

(d) the Agency Agreement; and

(e) this Prospectus.

In addition, copies of this Prospectus are available on the website of the Regulatory News Service operated by the London Stock Exchange at http://www.londonstockexchange.com/exchange/news/market-news/market-news-home.html.

Yield

8. The yield of the Notes is 12.551 per cent., on an annual basis. The yield is calculated as at the Issue Date on the basis of the issue price for the period from the Issue Date until the Reset Date and assuming no deferral of interest. It is not an indication of future yield.

Manager transacting with the Issuer

9. The Manager and its affiliates have engaged, and may in the future engage, in investment banking and/or commercial banking transactions with, and may perform services to the Issuer and its affiliates in the ordinary course of business.

Material Contracts

10. There are no material contracts entered into other than in the ordinary course of the Issuer's business which could result in the Issuer being under an obligation or entitlement that is material to the Issuer's ability to meet its obligations to Noteholders in respect of the Notes.

APPENDIX 1

FINANCIAL INFORMATION

Index to Financial Statements

Independent auditor’s report to the members of CIS General Insurance Limited

We have audited the accounts of CIS General Insurance Limited (CISGIL) for the year ended 31 December 2014 set out on pages 12 to 23, in notes E, F, H and I, on pages 27 to 33, and on pages 34 to 54. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU.

This report is made solely to CISGIL’s members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 as applied to CISGIL and as modified by the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008 and to facilitate compliance with section 496 of the Companies Act 2006. Our audit work has been undertaken so that we might state to CISGIL’s members those matters we are required to state to them in an auditor’s report and to facilitate compliance by CISGIL’s directors with the requirement relating to section 496 of the Companies Act 2006, as applied to CISGIL by Regulation 3 of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than CISGIL and CISGIL’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 10, the directors are responsible for the preparation of the accounts and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on the accounts 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 accounts

A description of the scope of an audit of accounts is provided on the Financial Reporting Council’s website at www.frc.org.uk/auditscopeukprivate.

Opinion on the accounts

In our opinion the accounts:

- give a true and fair view of the state of CISGIL’s affairs as at 31 December 2014 and of its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the EU, as applied in accordance with the provisions of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, which apply the provisions of chapters 4 and 5 of part 15 of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, which modify and apply the Co-operative and Community Benefit Societies Act 2014.

Opinion in order to facilitate compliance by CISGIL’s directors with the requirement relating to section 496 of the Companies Act 2006, as applied to CISGIL by Regulation 3 of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008

In our opinion the information given in the Strategic Report and the Directors’ Report for the financial year for which the accounts are prepared is consistent with the accounts.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Co-operative and Community Benefit Societies Act 2014 and the Companies Act 2006 as modified and applied by the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008 require 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
- a satisfactory system of control over transactions has not been maintained; or
- the accounts 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.

Karen Orr (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
1 St Peter’s Square
Manchester
M2 3AE

10 March 2015

Income statement

For the year ended 31 December 2014
All amounts are stated in £m unless otherwise indicated

	Notes	**2014**	2013
Income			
Gross earned premiums		**400.0**	509.0
Less premiums ceded to reinsurers		**(27.4)**	(32.5)
Net earned premiums	2	**372.6**	476.5
Fee and commission income	3	**9.5**	13.3
Investment income	4	**20.6**	27.9
Gains less losses arising from financial instruments	5	**3.0**	13.0
Other operating income	6	**-**	0.3
Net income		**405.7**	531.0
Claims paid		**(364.4)**	(410.0)
Less amounts receivable from reinsurers		**7.8**	6.8
Net policyholder claims and benefits paid	7	**(356.6)**	(403.2)
Change in insurance contract liabilities	21	**91.1**	60.2
Change in reinsurance assets	21	**16.9**	12.2
Net policyholder claims and benefits incurred		**(248.6)**	(330.8)
Fee and commission expenses	8	**(16.7)**	(19.8)
Operating expenses	9	**(143.8)**	(143.3)
Finance costs		**(3.4)**	(3.5)
(Loss)/profit before taxation		**(6.8)**	33.6
Income tax	10	**(0.1)**	(5.9)
(Loss)/profit for the financial year		**(6.9)**	27.7

Profit for the financial year is attributable to the equity shareholder and relates to continuing activities.

Statement of comprehensive income

For the year ended 31 December 2014
All amounts are stated in £m unless otherwise indicated

	Notes	2014	2013
(Loss)/profit for the financial year		**(6.9)**	27.7
Changes in available for sale assets:			
Net changes in fair value recognised directly in equity		**28.9**	(14.2)
Net gains transferred from equity to the income statement		**(3.0)**	(13.0)
Income tax	22	**(5.5)**	6.3
Other comprehensive income/(expense) for the financial year, net of income tax		**20.4**	(20.9)
Total comprehensive income for the financial year		**13.5**	6.8

Total comprehensive income for the financial year is attributable to CISGIL's equity holders and relates to continuing activities. All items will be reclassified subsequently to the income statement when assets are sold.

Balance sheet

At 31 December 2014

All amounts are stated in £m unless otherwise

	Notes	2014	2013
Assets			
Property, plant and equipment	11	**0.2**	-
Intangible assets	12	**1.6**	-
Deferred acquisition costs	13	**20.2**	35.3
Reinsurance assets	21	**71.9**	56.8
Financial investments at fair value through income or expense	14	**156.3**	207.6
Available for sale assets	15	**764.6**	763.4
Insurance receivables and other assets	16	**159.2**	208.5
Total assets		**1,174.0**	1,271.6
Capital and reserves attributable to equity holders			
Share capital	18	**268.0**	183.0
Retained earnings	19	**43.0**	49.9
Other reserves	19	**70.4**	50.0
Total equity		**381.4**	282.9
Liabilities			
Insurance contract liabilities	21	**737.6**	866.3
Other borrowed funds	20	**-**	85.0
Deferred tax liabilities	22	**5.6**	5.7
Current tax liabilities	22	**10.6**	4.9
Other reinsurance liabilities	23	**0.5**	-
Insurance and other payables	24	**30.4**	17.9
Bank overdraft	17	**7.9**	8.9
Total liabilities		**792.6**	988.7
Total equity and liabilities		**1,174.0**	1,271.6

Approved by the Board of Directors on 10 March 2015 and signed on its behalf by:

Robert Newton, Chairman
Mark Summerfield, Director
Pat Wade, Secretary

Statement of cash flows

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

	Notes	2014	2013
Cash flows from operating activities			
(Loss)/profit before taxation		**(6.8)**	33.6
Adjustment for:			
Interest payable		**3.4**	3.5
Amortisation of investments		**(11.9)**	10.4
Decrease/(increase) in deferred acquisition costs		**15.1**	(5.4)
Increase in reinsurance assets		**(15.1)**	(12.0)
Decrease/(increase) in available for sale assets		**36.6**	(27.5)
Decrease in financial investments at fair value through income and expense		**51.3**	106.4
Decrease in insurance receivables and other assets		**49.3**	16.2
Decrease in insurance contract liabilities		**(128.7)**	(162.4)
Increase/(decrease) in other reinsurance liabilities		**0.5**	(2.3)
Increase/(decrease) in insurance and other payables		**12.5**	(4.0)
Income tax received	22	**-**	0.6
Net cash flows from operating activities		**6.2**	(42.9)
Cash flows from investing activities			
Purchase of tangible fixed assets		**(0.2)**	-
Purchase of intangible fixed assets		**(1.6)**	-
Repayment of loans and receivables		**-**	50.0
Net cash flows from investing activities		**(1.8)**	50.0
Cash flows from financing activities			
Interest paid		**(3.4)**	(3.5)
Net cash flows from financing activities		**(3.4)**	(3.5)
Net increase in cash and cash equivalents		**1.0**	3.6
Cash and cash equivalents at the beginning of the financial year		**(8.9)**	(12.5)
Cash and cash equivalents at the end of the financial year	17	**(7.9)**	(8.9)

Cash flows from operating activities

CIS General Insurance Limited (CISGIL) classifies the cash flows for the acquisition and disposal of financial assets as operating cash flows. This is because purchases are funded from the cash flows associated with the origination of insurance contracts, net of the cash flows for payments of benefits and claims incurred for insurance contracts, which are classified under operating activities. Additionally, operating cash flows include interest received of £22.3m (2013: £31.4m).

Bank overdrafts are included within cash and cash equivalents in the statement of cash flows.

In December 2014, the CISGIL Board approved the issuance of new equity to its immediate parent, the Co-operative Banking Group Limited. Proceeds of the issuance were used to repay subordinated debt of £85.0m owed by CISGIL to the Co-operative Banking Group Limited. There was no cash movement.

Statement of changes in equity

For the year ended 31 December 2014

All amounts are stated in £m unless otherwise indicated

	Share capital	Available for sale reserve	Capital reserve	Retained earnings	Total
2014					
Balance at the beginning of the financial year	**183.0**	**(7.1)**	**57.1**	**49.9**	**282.9**
Total comprehensive income/(expense) for the financial year:					
Loss for the year	**-**	**-**	**-**	**(6.9)**	**(6.9)**
Other comprehensive income	**-**	**20.4**	**-**	**-**	**20.4**
Transactions with owners:					
Issuance of new share capital	**85.0**	**-**	**-**	**-**	**85.0**
Balance at the end of the financial year	**268.0**	**13.3**	**57.1**	**43.0**	**381.4**
2013					
Balance at the beginning of the financial year	183.0	13.8	57.1	22.2	276.1
Total comprehensive (expense)/income for the financial year:					
Profit for the year	-	-	-	27.7	27.7
Other comprehensive income	-	(20.9)	-	-	(20.9)
Balance at the end of the financial year	183.0	(7.1)	57.1	49.9	282.9

CIS General Insurance Limited (CISGIL) is a co-operative society registered in England under the Co-operative and Community Benefit Societies Act 2014 and not a company registered under the Companies Act. The annual report and accounts were authorised for issue by the directors on 10 March 2015.

Statement of compliance

The annual report and accounts have been prepared in accordance with the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, which modify and apply the Co-operative and Community Benefit Societies Act 2014. The Regulations require CISGIL to prepare its annual report and accounts substantially as though it were a company registered under the Companies Act 2006 (the Act), and apply, with certain exemptions, the provisions of Parts 15 and 16 of the Act.

Basis of preparation

The annual report and accounts have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) and IFRS Interpretations Committee (IFRIC) guidance, as issued by the International Accounting Standards Board (IASB) and endorsed by the European Union (EU). The annual report and accounts also follow the provisions of the Revised Statement of Recommended Practice on Accounting for Insurance Business (SORP) issued by the Association of British Insurers in December 2005 (as amended in December 2006) in so far as these are compatible with the requirements of IFRS.

The financial information has been prepared under the historic cost convention as modified by the revaluation of available for sale financial assets, derivative contracts and certain other financial assets and financial liabilities held at fair value. CISGIL applies the recognition, measurement and disclosure requirements of IFRS in issue that are endorsed by the EU and are effective for accounting periods beginning on or after 1 January 2014.

Standards and interpretations issued and effective

In preparing these annual report and accounts, CISGIL has adopted the following new pronouncement during the year:

- IFRIC 21 (Levies)

  This interpretation provides guidance on when to recognise a liability for a levy imposed by a government. IFRIC 21 identifies the obligating event for the recognition of a liability as the activity that triggers the payment of the levy in accordance with the relevant legislation. The interpretation clarifies that 'economic compulsion' and the going concern principle do not create or imply that an obligating event has occurred, and allows for the liability to be recognised progressively if the obligating event occurs over a period of time.

  IFRIC 21 is now effective for accounting periods on or after 21 June 2014 with early adoption permitted. The accounting policy in respect of the Financial Services Compensation Scheme (FSCS) levy has changed to reflect the new guidance; this has not resulted in a material financial impact.

Standards and interpretations issued but not yet effective

- IFRS 9 (Financial Instruments)

  This new standard is the IASB's replacement of IAS 39 (Financial Instruments: Recognition and Measurement). The Standard includes requirements for recognition and measurement, impairment, derecognition and general hedge accounting.

  It becomes effective for accounting periods beginning on or after 1 January 2018, with early adoption permitted once endorsed by the EU. CISGIL are still evaluating the impact of this standard but expectation is that, with the exception of additional disclosures, this is likely to be immaterial.

- IFRS 15 (Revenue from Contracts with Customers)

  The core principle of IFRS 15 is that an entity will recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This core principle is delivered in a five-step model framework.

  It becomes effective for accounting periods beginning on or after 1 January 2017, with early adoption permitted once endorsed by the EU. The impact of IFRS 15 is likely to be immaterial to CISGIL.

Other standards and interpretations have been issued but these are not considered to be relevant to CISGIL’s operations.

Basis of preparation (continued)
Going concern
CISGIL's business activities, together with its financial position and the factors likely to affect its future development and performance are set out in the strategic report and the directors' report. In addition, the risk management section on pages 24 to 33 of the annual report and accounts includes CISGIL's objectives, policies and processes for managing its risk, including its exposure to risk. The capital management section on page 34 provides information on CISGIL's capital policies and capital resources. Details of financial instruments are disclosed in note 29.

The assessment of the going concern basis of preparation has been subject to a thorough process involving analysis and discussion by management, the Board Audit Committee and the Board, in line with the governance processes discussed in the risk management sections of these accounts. The analysis covered forecast information for the strategic planning period, stress tests and reverse stress tests, as well as management actions and focused on the profitability, liquidity and capital requirements of CISGIL.

CISGIL reported a statutory loss for the year of £6.9m. Moving forward the business forecasts a period of underperformance as costs in relation to CISGIL's planned strategic transformation programme are incurred. CISGIL plan to raise additional capital in 2015 in order to finance this transformation.

As can be seen in note 14, CISGIL has significant deposits with credit institutions of £156.3m, considerably in excess of the Board's target minimum liquidity requirement.

As explained on pages 34 and 35, there are a number of regulatory capital requirements with which CISGIL must comply. Total regulatory capital was £344.1m at 31 December 2014, which is in excess of all externally imposed regulatory capital requirements. Current forecasts show that CISGIL's available capital will remain above all these regulatory capital requirements for the foreseeable future, including when Solvency II comes into force with effect from 1 January 2016.

While CISGIL has maintained capital above all its regulatory requirements throughout the period, since September 2014 CISGIL has fallen below its 1-in-6 year risk appetite buffer capital requirement. In assessing capital resilience for the period under review, CISGIL has considered a number of stress and reverse stress tests on capital both in the context of restoring capital above risk appetite and maintaining capital above all regulatory requirements. In considering these scenarios, management has identified potential actions that could be taken to improve the capital position if overall solvency is threatened.

CISGIL has identified risks in respect of its transformation programme, the implementation of the Solvency II regulatory regime from 1 January 2016, and Group related risks, as key risks to its going concern status.

The key risk to CISGIL's transformation programme is CISGIL's ability to raise the finance required to fund transformation. Based on the information available to the Board at the current time, including taking external advice, CISGIL is highly confident in its ability to raise additional finance. Until completion however, there remains a risk that events not wholly within the Board's control could impact on the capital being secured. In this eventuality, and CISGIL remains on its existing operating model in the immediate future, CISGIL is forecast to continue to meet all of its capital requirements over the going concern assessment period.

A designated Solvency II programme and plans are in place, targeting compliance with the new regime from 1 January 2016. Forecast solvency projections show that CISGIL maintains its capital buffer when the new regulation comes into force although this makes no allowance for any capital add-ons that the regulator may apply under the new regime. Whilst the size of a potential add-on cannot be predicted, an add-on of similar magnitude to that currently applied under Solvency I would not affect CISGIL's going concern status.

Group risks that could affect the future performance and capital position of CISGIL are primarily a result of the bank separation exercise, notably in respect of the separation activities themselves and the impact on the pension scheme arrangements. For these risks the Directors do not have direct control of all possible mitigating actions.

- Whilst none of the separation costs will be borne by CISGIL, there are operational risks associated with the shared services arrangements in the short term. The separation presents CISGIL with risks around IT, shared assets and service providers. These risks are being actively managed by management and the Board. CISGIL management has established a committee at Board level and a programme team to lead business transformation. Work is focussing on the design of a new operating model that will facilitate separation from existing shared assets and contracts; and

- As disclosed on page 50, CISGIL has an agreement with CFSMS to pay an appropriate share of the pension contributions relating to staff employed by CFSMS that are assigned to work for CISGIL. As a consequence, CISGIL is exposed to potential future increases in contributions, deficit funding and section 75 debts. Management is working closely with the parent companies, who manage this pension risk. At present CISGIL is not aware of any actions being undertaken by the parent that would have a material adverse impact on CISGIL.

After consideration of the above, and making relevant enquiries of the Co-operative Group Limited (the Group), the directors are satisfied that CISGIL has the resources to continue to meet its liabilities as they fall due and has therefore continued to adopt the going concern basis in preparing the annual report and accounts.

Use of estimates and judgments
The preparation of the annual report and accounts requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the annual report and accounts, are described within the significant accounting policies below.

Basis of preparation (continued)

Use of estimates and judgments (continued)

Information about estimation uncertainty, that has the most significant effect on the amounts recognised in the annual report and accounts, relates to the determination of the ultimate liability arising from claims made under insurance contracts. Details of the methodology, key assumptions and sensitivities are provided in note 21 (b). Additionally further reference is made within the risk management section in relation to insurance risk on pages 27 and 28.

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these annual report and accounts. The accounting policies are split between non-insurance specific accounting policies and insurance accounting policies. The insurance accounting policies are detailed in accounting policy 16 on pages 22 and 23.

(1) Property, plant and equipment

Property, plant and equipment are stated at cost or deemed cost less accumulated depreciation and impairment losses.

Depreciation is charged to the income statement on a straight line basis to allocate the difference between cost and residual value over the estimated useful lives when assets are commissioned for use. Estimated useful lives are as follows:

- computer equipment 3 – 10 years
- furniture and equipment 5 – 10 years

Assets in the course of construction are only depreciated when they are commissioned for use.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and are recognised net within operating expenses in the income statement.

(2) Intangible assets

Intangible assets comprise computer software together with the costs of development of the software.

Acquired computer software licences are capitalised on the basis of cost incurred to acquire and bring the software to use.

Costs that are directly associated with the internal production of software products that will generate future economic benefit are capitalised and recognised as intangible assets in the course of construction. Only costs which meet the definition of development costs under IAS 38 (Intangible Assets) are capitalised, with costs being capitalised only if the costs of the asset can be reliably measured, will generate future economic benefits and there is an ability to use the asset. Expenditure that is not directly attributable to the development of such assets is recognised in the income statement in the period to which it relates.

The expenditure capitalised includes direct employee costs and an appropriate portion of relevant direct overheads. Assets in the course of construction are transferred to computer software and amortised only when they are commissioned for use. Amortisation is charged to the income statement on a straight line basis to allocate the cost over the estimated useful life when commissioned for use, which is between three and ten years.

(3) Financial instruments (excluding derivatives)

CISGIL classifies its financial assets (excluding derivatives) as either:

- available for sale; or
- financial assets at fair value through income or expense; or
- loans and receivables.

i) Recognition of financial assets and financial liabilities

Financial assets are recognised by CISGIL on the trade date which is the date it commits to purchase the instruments. Loans are recognised when the funds are advanced.

All other financial instruments are recognised on the date that they are originated.

ii) Derecognition of financial assets and financial liabilities

Financial assets are derecognised when they are qualifying transfers and:

- the rights to receive cash flows from the assets have ceased; or
- CISGIL has transferred substantially all the risks and rewards of ownership of the assets.

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires. When an existing liability is replaced by the same counterparty on substantially different terms or the terms of an existing liability are substantially modified, the original liability is derecognised and a new liability is recognised, with any difference in carrying amounts recognised in the income statement.

iii) Financial assets designated as available for sale

CISGIL classifies its holdings in debt securities as available for sale. Initial measurement is at fair value, being purchase price upon the date on which CISGIL commits to purchase plus directly attributable transaction costs.

Subsequent valuation is at fair value with movements recognised in other comprehensive income as they arise. Where there is evidence of impairment, the extent of any impairment loss is recognised in the income statement. For further information refer to (3(vii)).

On disposal, gains or losses previously recognised in other comprehensive income are transferred to the income statement.

Significant accounting policies (continued)
(3) Financial instruments (excluding derivatives) (continued)

iv) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and CISGIL does not intend to sell immediately or in the near term. For CISGIL this includes insurance premium debt receivables but excludes salvage and subrogation. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently these are measured at amortised cost. The amortised cost is the initial amount at recognition less principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, less impairment provisions for incurred losses.

v) Financial investments at fair value through income or expense

Investments, other than those in debt securities, are designated as financial assets at fair value through income or expense, where they are managed and their performance is evaluated on a fair value basis in accordance with a documented risk management or investment strategy, and information is provided internally to key management personnel on that basis. Initial measurement is at fair value, being purchase price upon the date on which CISGIL commits to purchase. Directly attributable transaction costs are expensed immediately on recognition.

Subsequent valuation is at fair value with changes in fair value being recognised in gains less losses within the income statement in the period in which they arise. Where there is no active market or the investments are unlisted, the fair values are based on commonly used valuation techniques.

vi) Financial liabilities

Financial liabilities are contractual obligations to deliver cash or other financial assets. Financial liabilities are recognised initially at fair value, net of directly attributable transaction costs. Financial liabilities, other than derivatives, are subsequently measured at amortised cost.

Financial liabilities primarily represent borrowed funds. Borrowings are recognised initially at fair value, which equates to issue proceeds net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

vii) Impairment of financial assets

Assessment

At the balance sheet date, CISGIL assesses its financial assets not carried at fair value through income or expense for objective evidence that an impairment loss has occurred.

Objective evidence that financial assets are impaired can include default by a borrower or issuer, indications that a borrower or issuer will enter bankruptcy or the disappearance of an active market for that financial asset because of financial difficulties.

Measurement

Any impairment losses on assets classified as available for sale, and those carried at amortised cost, are recognised immediately through the income statement

The amount of the loss is the difference between:

- the asset's carrying amount (calculated on an amortised cost basis); and
- the present value of estimated future cash flows (discounted at the asset's original or variable effective interest rate for amortised cost assets or at the current market rate for available for sale assets).

Impairment of financial assets classified as available for sale

Impairment losses are recognised by transferring the cumulative loss that has been recognised directly in equity to the income statement.

When a subsequent event causes the amount of impaired loss on available for sale investment securities to decrease, and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the income statement. However any further recovery in fair value of an impaired available for sale equity security is recognised directly in equity.

Impairment of financial assets carried at amortised cost

The amount of the impairment loss on assets carried at amortised cost is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

A write off is made when all or part of an asset is deemed uncollectable or forgiven after all the possible collection procedures have been completed and the amount of loss has been determined. Write offs are charged against previously established provisions for impairment or directly to the income statement.

Any additional recoveries from borrowers, counterparties or other third parties made in future periods are offset against the write off charge in the income statement once they are received.

Provisions are released at the point when it is deemed that following a subsequent event the risk of loss has reduced to the extent that a provision is no longer required.

Significant accounting policies (continued)
(3) Financial instruments (excluding derivatives) (continued)

viii) Gains less losses arising from financial assets
Gains less losses arising from financial assets represents unrealised fair value movements of assets held at fair value through income or expense as well as realised gains/losses on available for sale assets.

(4) Sale and repurchase arrangements
CISGIL participates in reverse sale and repurchase transactions whereby CISGIL buys gilts but is contractually obliged to sell them at a fixed price on a fixed future date. Cash pledged under reverse repo arrangements are classified as deposits with credit institutions within financial investments at fair value through income or expense on the balance sheet as a result of CISGIL's documented risk management policy.

(5) Cash and cash equivalents
Cash and cash equivalents comprises cash balances and balances with a maturity of three months or less from the acquisition date, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Bank overdrafts that are repayable on demand and form an integral part of CISGIL's cash management are included as a component of cash and cash equivalents for the purpose of the cash flow statement.

(6) Offsetting
Financial assets and financial liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(7) Impairment of non-financial assets
The carrying value of CISGIL's non-financial assets, excluding deferred tax assets, are reviewed at the balance sheet date to determine whether there is any indication of impairment. If impairment is indicated, the asset's recoverable amount (being the greater of fair value less cost to sell and value in use is assessed by reference to discounted future cash flows) is estimated.

An impairment loss is recognised in the income statement to the extent that the carrying value of an asset exceeds its recoverable amount. An impairment loss is reversed if there has been an increase in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent of the asset's carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(8) Provisions
A provision is recognised in the balance sheet if CISGIL has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(9) Revenue recognition
Revenue principally comprises:

Premium income from insurance contracts
CISGIL's accounting policy in respect of revenue arising from insurance contracts is set out within the insurance specific accounting policy (16i) on page 22.

Investment income
Interest income on financial assets designated as available for sale and loans and receivables are recognised within investment income on an effective interest rate (EIR) basis, inclusive of directly attributable incremental transaction costs and fees, and discounts and premiums where appropriate.

The EIR basis spreads the interest income over the expected life of the instrument. The EIR is the rate that, at inception of the instrument, exactly discounts expected future cash payments and receipts through the expected life of the instrument back to the initial carrying amount. When calculating EIR, CISGIL estimates cash flows considering all contractual terms of the instrument (for example prepayment options) but does not consider future credit losses.

Interest income on assets designated as fair value through income or expense is recognised within investment income in the income statement as it accrues on an effective interest basis.

Fee and commission income
Fees and commission receivable mainly relates to fee income, recognised as the related service is provided, and brokerage commission earned over the lifetime of the related policy.

(10) Fee and commission expenses
Fees and commission payable mainly relates to commission payable to broker intermediaries that is incurred over the lifetime of the related policy. All other fee and commission payable is recognised on an accruals basis as the service is provided.

Significant accounting policies (continued)

(11) Income tax

Tax on the income statement for the year comprises current and deferred tax, which is recognised in the income statement except to the extent that it relates to items in other comprehensive income, in which case it is recognised in the statement of comprehensive income.

Current tax

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax

Deferred tax is provided using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided for is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(12) Foreign currencies

The functional and presentational currency for CISGIL is sterling. Substantially all transactions conducted by CISGIL are in sterling. All amounts presented are stated in pound sterling and millions, unless stated otherwise.

(13) Significant items

Items which are material by both size and nature (i.e. outside the normal operating activities of CISGIL) are treated as significant items and disclosed separately on the face of the income statement.

The separate reporting of significant items helps provide an indication of CISGIL's underlying business performance. Events which may give rise to the classification of items as significant include individually significant costs.

(14) Profit based payments to members of The Co-operative Group

Members of the Group may receive a dividend based on their transactions with the Group and its subsidiaries, including CISGIL. Once these profit based payments are approved by The Co-operative Group Limited, CISGIL is recharged an amount which reflects its eligible products' contribution to the overall Co-operative Group member dividend. There were no such payments in the year (2013: £nil).

(15) Dividends

Dividends are only recognised in the annual report and accounts by CISGIL once they have been approved by the shareholders in a general meeting.

(16) Insurance accounting policies

Contracts under which CISGIL accepts significant insurance risk from another party (the policyholder), by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary are classified as insurance contracts. A contract that qualifies as insurance remains an insurance contract until all the risks and obligations are extinguished or expire.

All contracts of general insurance business written by CISGIL are classified as insurance contracts. General insurance business is accounted for on an annual basis.

i) Premiums

Gross written premiums comprise premiums receivable on those contracts which incepted during the financial year, irrespective of whether they relate in whole or in part to a later accounting period, together with any necessary adjustments to amounts reported in prior periods.

Gross written premiums:

- are stated gross of commission and exclude any taxes or levies based on premiums; and
- include an estimate of the premiums receivable on those contracts which incepted prior to the year end but which have not been notified by the balance sheet date ('pipeline premium'). When calculating pipeline premiums it is assumed, where appropriate, that options to renew contracts automatically will be exercised.

Gross written premium (whether paid in advance or by instalments) is earned evenly over the period of the contract (usually twelve months). The treatment of outward reinsurance premiums is similar to gross premiums written.

Significant accounting policies (continued)

(16) Insurance accounting policies (continued)

ii) Unearned premium provision

For general insurance business, the proportion of written premiums relating to periods of risk beyond the year end is carried forward to future accounting periods. The relevant proportion is calculated using the daily pro rata basis.

Outward reinsurance premiums are treated as earned in accordance with the profile of the reinsured contracts.

iii) Claims incurred

Insurance claims incurred comprise claims paid during the year, together with related handling costs and the change in the gross liability for claims in the period net of related recoveries including salvage and subrogation.

iv) Claims outstanding

Claims outstanding comprises provisions representing the estimated ultimate cost of settling:

- estimates on claims reported by the balance sheet date ('claims reported'); and
- expected additional cost in excess of claims reported for all claims occurring by the balance sheet date ('claims incurred but not reported').

Aggregate claims provisions, which include attributable claims handling expenses, are set at a level such that no adverse run off deviations are envisaged. Adverse run off deviations, which are material in the context of the business as a whole, would be separately disclosed in the notes to the annual report and accounts including the claims development tables.

Anticipated reinsurance recoveries and estimates of salvage and subrogation recoveries are disclosed separately within assets under the headings of 'reinsurance assets' and 'insurance receivables and other assets' respectively.

In accordance with accounting regulations, discounting of outstanding claims is permitted in certain circumstances. For statutory accounts the outstanding reserves are discounted in respect of periodical payments and a portion of liability type claims from the electric industry ('EIROS') for which separate assets are held of appropriate term and nature.

v) Unexpired risk provision

Additional provision is made for unexpired risks where the claims and expenses, likely to arise after the end of the financial year in respect of contracts concluded before that date, are expected to exceed the unearned premiums less deferred acquisition costs carried forward for those contracts.

Unexpired risk provision is calculated for each category of business. Where categories of business are managed together a combined calculation is performed. Surpluses and deficits within each category are offset within the calculation. The provision is determined after taking account of future investment return arising on investments supporting the unearned premium provision and unexpired risk provision.

Such provisions ensure that the carrying amount of unearned premiums provision less related deferred acquisition costs is sufficient to cover the current estimated future cash flows, including claims handling expenses and therefore meets the requirements of the liability adequacy test as set out in IFRS 4 (Insurance Contracts).

vi) Acquisition costs

Costs directly associated with the acquisition of new business, including commission, are capitalised and amortised in accordance with the rate at which the gross written premiums associated with the underlying contract are earned.

vii) Reinsurance

Contracts with reinsurers that give rise to a significant transfer of insurance risk are accounted for as reinsurance contracts. Amounts recoverable under such contracts are recognised in the same period as the related claim. Premiums, claims and receivables are presented on a gross basis in the income statement and balance sheet.

Amounts recoverable under reinsurance contracts are assessed for impairment at each balance sheet date. If objective evidence of impairment exists, reinsurance assets are reduced to the level at which they are considered to be recoverable and an impairment loss is recognised in the income statement.

CIS General Insurance Limited (CISGIL) issues contracts that transfer insurance risk and is exposed to financial risk through its holdings of financial assets and liabilities. This section summarises these risks and the way CISGIL manages them.

Developments during 2014

CISGIL has a stand-alone risk management framework which was based on the Co-operative Banking Group Limited (the Banking Group) framework but adapted for CISGIL's risks, governance and processes. During 2014, a number of enhancements to the framework have taken place:

- Enhanced conduct risk management framework – (RMF);
- Added group risk as a principal risk;
- Further embedded suite of risk policies and control standards;
- Refined risk reporting to the Board and Executive Risk Committee;
- Strengthened stand-alone 2nd line risk function; and
- Formalised and improved the risk event reporting and risk acceptance process.

The following section summarises the risk management structures that are in place.

Our approach to risk management

CISGIL operates a three lines of defence governance model to ensure appropriate responsibility and accountability is allocated to the identification, measurement, management, monitoring and reporting of risks.

Business management is the first line of defence. It is responsible for implementing and operating processes to identify, measure, manage, monitor and report risks. This includes those risks deriving from the development of new products, processes or other business change. It manages the risks that reside within the business areas on a day-to-day basis and implements effective monitoring and control processes to ensure that the business risk profile is understood and maintained within the Board's defined risk appetite.

The Chief Risk Officer and Risk function are the second line of defence. They own the risk management framework, oversee and challenge its implementation and operation by the first line of defence, and consider current and emerging risks across CISGIL. They also provide review and challenge of the delegated authority framework and oversee appropriate escalation of breaches, mitigating actions and reporting to the Executive Risk Committee and the Board.

The Head of Internal audit leads the third line of defence. They independently challenge the overall management of the framework and provide assurance to the Board Audit Committee and senior management on the adequacy of both the first and second lines. The Chair of the Board Audit Committee oversees the internal audit function and risk-based audit plan. CISGIL has contracts in place with external consultants to provide internal audit capability.

Risk assessment of CISGIL

CISGIL has undertaken a robust assessment of the principal risks facing the company. It has developed its own Risk and Solvency Assessment (ORSA) process, which is an integral part in developing its Strategic Plan. One of the outputs of the ORSA process is the ORSA Report. This report provides a comprehensive picture of the risks that CISGIL is exposed to or could face in the future. These risks are described in detail within the report and summarised on page 26.

The prospects of CISGIL as at 31 December 2014 have primarily been assessed using the latest information (the 2014 year end position) and the 2015 - 2019 Strategic Plan, which was approved by the CISGIL Board in December 2014. Based on this information, CISGIL has adequate capital and liquidity to continue its operation, under old and new regulatory regimes. Indicators which could impact upon its operations have been considered and appropriate management action has been taken where necessary to mitigate issues as identified.

As part of CISGIL's Risk Management Framework, its Executive Team are required to attest that they understand the risks and controls in their area of accountability and support an open risk management culture. In support of the attestation, each Executive and/or Risk Framework Owner is required to undertake a Risk and Control Self-Assessment – which identifies the risks to the achievement of their objectives, the controls against these risks together with an assessment of the effectiveness of the controls (Design and Performance) with appropriate testing of control performance. The Risk and Control Self-Assessments are designed to cover all material controls including financial, operational and compliance controls and also cover the minimum requirements outlined in CISGIL's risk policies and control standards.

Risk management structure

The Board is responsible for approving the general insurance strategy, its principal markets and the level of acceptable risks articulated through its statement of risk appetite. It is also responsible for overall corporate governance which includes ensuring that there is an adequate system of risk management in place.

CISGIL has developed and implemented a governance and organisation structure, which supports the Board. The Board has established risk and audit sub-committees, and senior management committees, to:

- oversee the risk management process;
- identify the key risks facing the business; and
- assess the effectiveness of planned management actions.

Specific Board authority has been delegated to the Board sub-committees and the Chief Executive Officer (CEO) who has, in turn, delegated elements of these discretions to appropriate members of the senior management team.

CISGIL has developed a Delegated Authority Framework setting out the accountabilities delegated by the CEO to the Executive Team members which are reflected within the individual job descriptions of the Executive Team members. Those with delegated authority consider these in conjunction with their responsibilities as Approved Persons and their associated functional accountabilities. The practical application of this framework is documented in the Delegated Authorities Operating Manual.

Risk management committees

The CIS General Insurance Board (Board)

The responsibilities of the Board include:

- Setting the overall Risk Strategy;
- Approving the design and implementation of risk management approaches, including the Risk Management Framework Policy and the Risk Appetite Statements and metrics that underpin them;
- Delegating authority for oversight of the risk management framework, systems and high-level limits to the Board Risk Committee;
- Delegating authority for cascading the setting and approval of the more granular risk limits and tolerances to the CEO;
- Using the output of the semi-annual certification process, to approve the effectiveness of the Risk Management Framework with support from internal audit through their risk-based review programme; and
- Reviewing and challenging Board Risk Committee reports on the effectiveness of the risk management framework and systems.

CISGIL Board Risk Committee (BRC)

BRC responsibilities include:

- Providing oversight and advice to the Board on current and potential risks and the overall risk framework including risk appetite, risk tolerance and risk management strategies;
- Reviewing and challenging the design of the Risk Management Framework, Risk Appetite limits and tolerances and recommending to the Board for approval;
- Reviewing and challenging the implementation of the Risk Management Framework through the semi-annual certification process and reviewing the quality and effectiveness of the Risk Management Framework, systems and function;
- Reviewing and challenging internal controls and process of risk management including the coverage of the risk taxonomy;
- Monitoring the organisation's performance and compliance against high-level risk appetite limits and tolerances;
- In co-operation with the Board Audit Committee, monitoring identified risk control failings and weaknesses and management actions taken to resolve them; and
- Reporting on the effectiveness of the Risk Management Framework and systems to the Board.

CISGIL Board Transformation Committee (BTC) (established 2015)

BTC responsibilities include:

- Review and challenge Transformation Portfolio activities to ensure performance is in the best interests of key CISGIL stakeholders and aligned to the CISGIL Strategic Plan;
- Oversee the overall strategic investment budget and ensure appropriate prioritisation of funding;
- Review and oversee the customer journey and customer outcomes throughout transformation;
- Monitor, review and challenge performance and forecasts against overall Portfolio benefits and the Strategic Plan; and
- Periodically review and approve the mandate of the Transformation Portfolio, in particular ensuring that it has adequate resources to enable it to perform its function effectively.

CISGIL Board Audit Committee (BAC)

BAC responsibilities include:

- Review and oversight of financial statements and annual reports before submission to the Board;
- Assisting the Board in carrying out its responsibilities relating to internal control, including control breaches and remediation;
- Exercising oversight of identified risk control framework failings and weaknesses as well as management actions taken to resolve them; and
- Oversight of internal and external assurance and audit.

CISGIL Executive Committee (ExCo)

The ExCo responsibilities include:

- Overseeing the establishment and maintenance of appropriate risk management systems and controls in line with the Board agreed Risk Management Framework;
- Supporting the CEO in developing, reviewing and approving detailed risk appetite limits and tolerances as delegated by the Board; and
- Ensuring the implementation of the risk strategy set by the Board so as to deliver an effective risk management environment for CISGIL.

CISGIL Transformation Steering Executive Committee (TSEC)

The TSEC responsibilities include:

- Overseeing the delivery of the CISGIL Transformation and Business Critical Programmes, reviewing and approving new initiatives;
- Recommending approval for changes to timescales, costs, quality, costs, scope, risks and benefits; including material drawdown requests;
- Proactively managing risks and issues, highlighting thematic hotspots and initiating mitigating action plans;
- Overseeing the overall strategic investment budget:
- Overseeing the efficient and effective use of GI resources, by monitoring demand to ensure successful delivery of the Roadmap;
- Oversight of the CISGIL Benefits Realisation tracking plans; and
- Ensuring design decisions consider the implications on both the New Solution and current CISGIL operating model.

All amounts are stated in £m unless otherwise indicated

Risk management committees (continued)

CISGIL Executive Risk Committee (ERC)

The ERC responsibilities include:

- Driving the detailed implementation of the CISGIL Risk Management Framework approved by the Board;
- Providing a mechanism for ensuring that the CISGIL-wide risk and capital management requirements, developments, and processes are in place;
- Supporting the CEO in developing the Risk Strategy, Risk Management Framework, and Risk Appetite Statement and recommending to the Board Risk Committee for review, challenge and recommendation to the Board for approval;
- Supporting the CEO in approving Risk Policies, proposing Risk Appetite limits and tolerances to Board Risk Committee for review, challenge and recommendation to the Board for approval;
- Reviewing approaches to stress testing, risk management reporting and governance, and referring them to the Board Risk Committee for review, challenge and recommendation for approval by the Board;
- Supporting the CEO in semi-annually reviewing the effectiveness of the Risk Management Framework, systems and function and providing a report to the Board Risk Committee;
- On a periodic basis, assessing the performance of the Risk Management Framework; and
- Monitoring the business's risk profile against the agreed limits and tolerances and reporting on these to the Board Risk Committee.

Senior Management Committees

CISGIL has other committees that advise and support the CEO and members of the senior management team in carrying out their responsibilities, and provide detailed oversight and monitoring in the following areas:

- Customer and Operations;
- Conduct Risk Steering;
- Commercial;
- Capital, Liquidity, Investment and Pension;
- Reserving;
- Operational Risk;
- Data Governance; and
- Model Governance.

Principal risks

The following are considered to be the principal risks facing CISGIL:

	Risk Type	Definition	Page
A	Strategic and business risk*	The risk to earnings and capital that may arise as a result of strategic/management decisions or business choices or lack of responsiveness to changes in the business environment	27
B	Reputation risk*	The risk associated with an issue which could in some way be damaging to the brand of the organisation among all or any stakeholders	27
C	Conduct risk*	The risk that CISGIL's behaviours, offerings or interactions will result in unfair outcomes for customers	27
D	Regulatory risk*	The risk of fines, public censure, limitation on business, or restitution costs arising from failing to understand, interpret, implement and comply with UK and EU regulatory requirements	27
E	Insurance risk	The inherent uncertainties as to the occurrence, amount and timing of insurance liabilities	27
F	Market risk	The risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers e.g. interest rates, market prices of assets and liabilities	28
G	Operational risk*	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events	30
H	Liquidity risk	The current and prospective risk to earnings or capital arising from CISGIL's inability to meet its obligations when they come due without incurring unacceptable losses	30
I	Credit risk	The risk to earnings and capital arising from a debtor's failure to meet their legal and contractual obligations	31
J	Pension risk*	The risk to capital and company funds from exposure to scheme liabilities (to the extent liabilities are not met by scheme assets) and risks inherent in the valuation of scheme liabilities and assets	33
K	Group risk*	The risks that arise through being part of the Co-operative Group	33

For each of the principal risks, CISGIL appoints a Risk Framework Owner (RFO) and a risk framework must be defined and documented. The framework includes Board approved risk policies and risk appetite statements with underpinning metrics. The metrics have approved limits within which business operations are to be conducted, along with thresholds to give early warning of emerging issues.

Risks marked with an asterisk (*) above are termed unaudited as they are outside the scope of the external audit.

Principal risks (continued)

A. Strategic and business risks (unaudited)

Strategic and business risks to earnings and capital arise as a result of strategic/management decisions or business choices or lack of responsiveness to changes in the business environment. Specific strategic and business risks, and management actions, are regularly reported and reviewed by the ERC and Board. CISGIL's objective in managing these risks is to maintain a sufficient capital buffer in excess of minimum regulatory capital requirements to cover projected risks and maintain market confidence, and obtain a sufficient, stable and sustainable return on equity. The Board have defined detailed metrics and limits underpinning these objectives, which are measured, monitored and reported regularly to the ERC and Board. The Board have approved a strategic transformation programme to ensure the business model can respond to the technology driven changing insurance market.

B. Reputation risk (unaudited)

Reputational risk is defined as the risk associated with an issue which could in some way be damaging to the brand of CISGIL either through its strategic decisions, business performance, an operational failure or external perception. CISGIL's objective is to maintain a strong reputation in line with our values and principles through robust operational standards, continual monitoring of our corporate reputation and brand, commitment to our Social Goals Strategy and proactive PR.

As part of the assessment and control of this risk, our business performance and risk profile across all of our risk types are closely monitored and reviewed. CISGIL proactively monitors and manages media, public and customer opinion and works closely with external rating agencies to ensure fair and balanced representation. This approach helps maintain member, customer and market confidence. This risk is regularly monitored and reported to the Operational Risk Committee, ERC and Board.

During the first half of 2014, media coverage associated with reputational issues faced by the Co-operative Group Limited (the Group) led to brand impairment for CISGIL. Since the Group AGM in May 2014, the media profile has improved. The Co-operative Group has now established its recovery strategy which has resulted in an improved brand position, and levels of risk to the brand through group contagion have continued to reduce.

C. Conduct risk (unaudited)

Conduct risk is the risk that CISGIL's behaviours, offerings or interactions will result in unfair outcomes for customers. Accordingly, conduct risk may arise from any aspect of the way a business is conducted, the sole test being whether the outcome is an unfair one for customers. Conduct risk is a key area of focus across the financial services industry, with increasing scrutiny from the Financial Conduct Authority.

CISGIL's objective is to maintain the highest standards in our conduct and treatment of customers and the quality of our customer experience through the operation of a robust Conduct Risk Strategy and framework and the application of systems and controls in conjunction with ongoing oversight and monitoring from risk functions. These established systems and controls mitigate and prevent emerging conduct risk.

During 2014, improvements were made in the control of Conduct Risk including; implementation of Conduct Risk & MI Reporting, Risks and Issues Register, Roll out of conduct risk training. A new Product Governance Forum was established to oversee and govern the product throughout its lifecycle. The establishment of a monthly executive Conduct Risk Steering Committee in 2014 ensures the timely identification, measurement, management, monitoring and reporting of conduct risks through management structures and to the ERC and Board.

D. Regulatory risk (unaudited)

Regulatory risk is the risk of fines, public censure, limitation on business, or restitution costs arising from failing to understand, interpret, implement and comply with UK and EU regulatory requirements. CISGIL's objective is to maintain a robust process to ensure that all regulatory expectations and requirements are met within agreed or mandated timeframes, by promoting and embedding a compliance culture and developing positive regulatory relationships.

Regulatory risks are reported through management structures and regularly monitored and reported to the ERC and Board.

E. Insurance risk

Insurance risk comprises risks that arise in respect of claims that have already occurred and for which reserves are already held (reserving risk) and of claims that are yet to occur (underwriting risk). Underwriting risk includes risks from attritional claims and from natural or man-made catastrophe events.

The main classes of business written are private motor and home business, written directly or through brokers. In addition CISGIL writes some commercial insurance business, which is fully reinsured, and continues to manage some business that is now in run off, including a commercial account, commercial motor business and pet insurance. Almost all risks under general insurance policies cover a 12 month duration.

Principal risks under motor policies are bodily injury to third parties, accidental damage to property including policyholders' and third parties' vehicles, and theft of or from policyholders' vehicles. The most significant factors affecting the frequency and severity of motor claims are judicial, legislative and inflationary changes and the frequency and severity of large bodily injury claims.

Principal risks under home policies are damage from storm and flood, fire, escape of water, subsidence, theft of or accidental damage to contents and liability risks.

Principal risks (continued)

E. Insurance risk (continued)

CISGIL's aims to manage insurance risk:

- to achieve acceptable profits and return on equity by ensuring that insurance risks are carefully selected in accordance with risk appetite, underwritten in accordance with risk strategy and priced to reflect the underlying risk;
- to minimise reserve risk volatility through robust reserving and modelling approaches; and
- to mitigate catastrophe risk through the use of appropriate reinsurance arrangements.

Insurance risk is managed through the underwriting strategy, reinsurance arrangements, proactive claims handling and the claims provisioning process. The objective of the underwriting strategy is to ensure that the underwritten risks are diversified in terms of type and amount of risk, industry/demographic profile and geography, and only those risks which conform with underwriting criteria are accepted. Exposure mix and the frequency and average costs of claims are monitored throughout the year and where significant deviations from expectation are identified remedial action is taken.

The overriding objective in claims handling is to ensure all claims are properly scrutinised and paid where they fall within the terms and conditions of the policy. The proper scrutiny of claims is facilitated by the use of various technical aids such as weather validation and fraud databases, and the use of claims specialists. The basis for assessing claims provisions is set out in note 21.

The nature of insurance contracts is that the obligations of the insurer are uncertain as to the timing or quantum of liabilities arising from contracts. CISGIL takes all reasonable steps to ensure that it has information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established. CISGIL manage this risk through the Reserving Committee which supports the Finance Director in their responsibility to formally reviews claims reserves on a quarterly basis.

CISGIL uses reinsurance to manage insurance risk, and in particular to mitigate the cost of catastrophe events such as storms and floods and the cost of large claims arising within its motor account. The appropriate level of reinsurance is determined by management, using CISGIL's capital model to inform decision making. In 2014 CISGIL had two main reinsurance programmes in place: catastrophe excess of loss cover and motor excess of loss cover. Other reinsurances include the 100% reinsurance of the commercial insurance business being written by CISGIL, mentioned above.

In March 2014, a Part VII transfer was completed to transfer the general insurance business that had been written by Co-operative Insurance Society Limited (CISL) to CISGIL. CISGIL commenced underwriting business in January 2006. Prior to this the general insurance business was underwritten by CIS, a composite insurer writing both life and general insurance business. An indemnification arrangement was implemented at that time whereby CISGIL assumed financial responsibility for the run off of this business and received a premium, settled by transfer of assets, equivalent to the net technical liabilities of this business included in CIS's financial statements at 2005 year end. CIS was subsequently sold to Royal London Group, as part of the sale of the life and savings business, and became a subsidiary of Royal London. The Part VII transfer transferred the general insurance business within that subsidiary to CISGIL, hence CISGIL now has direct financial responsibility for this run off business, rather than via an indemnification agreement.

Insurance risk sensitivity analysis can be found in Note 21 b iii on page 45.

F. Market risk

Market risk is the risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers such as interest rates and market prices of assets and liabilities.

CISGIL invests in high-quality fixed and variable interest bonds issued by corporations ("corporate bonds") and the UK government ("gilts"), and in short-term sterling deposits with financial institutions ("cash"). The value of, or income from, assets held is subject to volatility from changes in both market interest-rates and additional spreads related to the specific credit-worthiness of the issuer ("credit-spreads"). Proceeds from maturing investments are also subject to risk over the future return on reinvestment.

CISGIL is also exposed to market interest-rates through the discounted present value placed upon future claims. All future claims are discounted for economic assessment purposes for economic capital. However, IFRS short term insurance reserves (normally less than five years) are not directly affected by market interest-rates as they are undiscounted.

In December 2014, capital quality was improved through the issuance of new equity to its immediate parent, the Co-operative Banking Group Limited. Proceeds of the issuance were used to repay the existing £85.0m subordinated debt to its immediate parent. This removed the interest rate risk upon £65.0m of this debt, which previously paid interest based on three month LIBOR. There was no interest rate risk on the remaining £20.0m as it paid a fixed interest rate.

CISGIL writes contracts of insurance in the United Kingdom and insurance liabilities and borrowings are denominated in sterling. Funds are invested solely in assets denominated in sterling and consequently there is no direct exposure to currency risk.

While CISGIL is not a participating employer, it has an agreement to pay pension contributions relating to staff employed by CFSMS that are assigned to work for CISGIL. This means that CISGIL is indirectly exposed to market risks (including interest rate, credit spread, equity and property), through the Co-operative Group pension scheme (PACE), to which CISGIL contributes.

In summary, the principal market risks that CISGIL is exposed to are:

- changes in interest-rates, which impact both asset and liability values, and investment income; and
- movements in credit-spreads which impact the market value of corporate bonds.

Principal risks (continued)
F. Market risk (continued)

Objective and strategy

CISGIL's objective is to achieve acceptable returns through the use of highly rated UK government and corporate bonds while minimising exposure to equities and other volatile instruments. To enhance certainty over the investment return generated from these assets, management practice is generally to maintain holdings to maturity.

CISGIL determines its strategic asset allocation through considering the risk/reward trade off and the impact upon capital adequacy and solvency of the overall company, which relies on outputs from CISGIL's capital model. CISGIL's investments are managed by Royal London Investment Management (RLAM) with whom CISGIL have an agreed investment mandate with limits for exposure by credit-rating, maximum terms and maximum exposure to individual counterparties. The Capital, Liquidity, Investment and Pension Committee supports the Finance Director to oversee RLAM, monitor and manage asset exposures against the strategic asset allocation and approved investment limits.

CISGIL manages credit-spread and default risks from corporate bonds through the limits for exposure to credit-ratings and individual counterparties. Other risk mitigation techniques employed to manage exposure to counterparty default include transacting only through a diversified range of authorised counterparties and the requirement for certain transactions (including cash, investment and trading in futures, stock lending and gilt repo transactions) to be collateralised on a daily basis. The Capital, Liquidity, Investment and Pension Committee supports the Finance Director in overseeing the monitoring and management of these risks and exposures against limits.

Interest-rate risk is managed through investing in fixed interest securities with a similar duration profile to the liabilities under the general insurance contracts. CISGIL matches the average duration of assets and liabilities in this portfolio by estimating their mean duration. The mean duration of liabilities is calculated using historical claims data to determine the expected settlement pattern for claims arising from insurance contracts in force at the balance sheet date (both incurred claims and future claims arising from the unexpired risks at the balance sheet date). Index-linked investments and other specific debt securities are used to match periodical payment liabilities and provisions relating to exposure within the electric industry ('EIROS' claims) by amount and duration. In order to do this, an expert opinion on life expectancy is used along with an expectation of long term average earnings. Mean durations are:

	2014	2013
Adopted insurance liabilities	**2.84 years**	3.20 years
Financial assets	**2.35 years**	2.53 years

Periodical payments	**Amount (£m)**	**Duration**
Insurance liabilities	**20.5**	**17.9**
Financial assets	**49.2**	**16.5**

EIROS claims	**Amount (£m)**	**Duration**
Insurance liabilities	**2.3**	**10.9**
Financial assets	**3.2**	**14.1**

Sensitivity analysis

Currently, the most significant aspect of market risk to which CISGIL is exposed is changes in credit-spreads upon corporate bonds. The resulting movements in the market values of corporate bonds directly affect CISGIL's internal economic assessment of solvency, including the ICA. As CISGIL has adopted a policy of recognising most investment assets on an 'available for sale' basis, movements in market values of these assets are recognised in other comprehensive income and so have limited impact upon reported IFRS profits.

An increase of 100 basis points in credit-spreads would reduce the carrying value of CISGIL's assets at the end of the financial year by £22.9m (2013: £17.9m). This would reduce the value placed upon these assets in CISGIL's internal economic assessment of solvency, including the ICA, by the same amount. On an IFRS basis it would result in a reduction in other comprehensive income of £18.0m net of tax (2013: £13.7m) The impact of a decrease of 100 basis points in credit-spreads would have similar but opposite effects.

The method used for this calculation increases the implied redemption yield by 100 basis points and uses this modified yield to calculate the revised market value of each bond in the portfolio. The calculation assumes that a change in credit-spreads would have an immediate and equal impact at all points on the yield curve and upon all corporate bonds regardless of their credit-rating. The probability of this credit-spread change over one year is assessed as 24% (2013: 24%) using CISGIL capital model.

All amounts are stated in £m unless otherwise indicated

Principal risks (continued)

G. Operational risk (unaudited)

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or external events and includes; internal and external fraud, loss or theft of confidential customer information, loss of key personnel, system capacity issues or programme failure and external events over which CISGIL has limited controls, such as terrorist attack. CISGIL's objective is to minimise operational risk through the implementation of a robust control environment which minimises the potential for loss as a result of the failure of processes, people, technology and due to external events.

CISGIL has defined the following sub-categories within operational risk, which represent the major areas of operational risk exposure. Each sub-category has its own policy, approved by the ERC and is supported by underlying control standards:

- Financial Reporting Risk
- Model Risk
- Technology Risk
- Physical Assets and Security
- Third Party Supplier Risk
- Change Risk
- Product Approval Risk
- Information Risk
- Financial Crime Risk
- People Risk
- Legal Risk
- Business Continuity Planning (BCP)
- Anti-Money Laundering (AML) and Counter Terrorist Financing (CTF)

Operational risks are identified, managed and mitigated through ongoing risk management practices including risk assessments, formal control procedures and contingency planning. Operational risks and key controls are regularly reviewed by the Operational Risk Committee. Significant operational risks are reported to the ERC and Board.

During 2014, the separation of the Co-operative Bank Limited (the Bank) from the Group presented a number of risks to CISGIL including; continuity of service, technology service provision, data access, governance structures of CFS Management Services Limited/the Banking Group. A programme is underway to separate CISGIL's IT from an infrastructure that is currently shared with the Banking Group and Royal London Group. Business continuity arrangements are in place in order to minimise the risk of disruption in the event of a sudden, unplanned occurrence that could seriously disrupt business operations. This includes developing and exercising crisis and incident management teams to maintain appropriate preparedness in the event of a major operational disruption.

CISGIL has a corporate insurance programme to transfer specific risks to insurers as part of its risk management approach.

H. Liquidity risk

Liquidity risk is the current and prospective risk to earnings or capital arising from an inability to meet obligations when they come due without incurring unacceptable losses. CISGIL's objective is to meet all policyholder and other funding obligations as they fall due primarily through the use of cash and highly liquid UK government and corporate bonds.

The Board's risk appetite is that liquid assets should be at least equal to 20% of the ultimate cost of a 1-in-100 year UK windstorm loss before reinsurance recoveries. The ultimate cost is calculated based upon the catastrophe component of CISGIL's capital model. The latest model assesses the ultimate cost of a 1-in-100 year UK windstorm as £136.0 m (2013: £147.0m), giving a minimum requirement for £27.2m (2013: £29.4m) of liquid assets against actual liquid assets of £673.9m (2013: £763.6m).

Liquid assets are considered to be:

Asset type		**Value included as liquid assets**
Gilts		100%
Cash		100%
Corporate bonds:	AAA	85%
	AA	85%
	A	50%
	BBB	50%
All other investments		0%

The level of cash and other assets held are monitored regularly and managed through the Capital, Liquidity, Investment and Pension Committee, with oversight by the ERC and Board. This includes monthly reporting of liquid assets against risk appetite limits.

All amounts are stated in £m unless otherwise indicated

Principal risks (continued)
H. Liquidity risk (continued)

The following table indicates the time profile of undiscounted cash flows arising from financial liabilities (based upon contractual maturity), and insurance liabilities (based upon estimated timing of amounts recognised in the balance sheet). Included in the analysis on insurance contract liabilities below is £47.3 m (2013: £40.0m) of discounted reserves relating to PPO and EIROS. Further details are included in note 21.

	Carrying value	**Gross nominal out flow**	**Up to 1 year**	**1 to 2 years**	**2 to 3 years**	**3 to 4 years**	**4 to 5 years**	**More than 5 years**
As at 31 December 2014								
Insurance contract liabilities	**737.6**	**737.6**	**403.9**	**115.0**	**69.0**	**44.6**	**28.5**	**76.6**
Financial liabilities at amortised cost:								
Other reinsurance liabilities	**0.5**	**0.5**	**0.5**	**-**	**-**	**-**	**-**	**-**
Insurance and other payables	**30.4**	**30.4**	**30.4**	**-**	**-**	**-**	**-**	**-**
Cash and cash equivalents	**7.9**	**7.9**	**7.9**	**-**	**-**	**-**	**-**	**-**
	776.4	**776.4**	**442.7**	**115.0**	**69.0**	**44.6**	**28.5**	**76.6**
Other liabilities	**16.2**							
Total recognised liabilities	**792.6**							

	Carrying value	Gross nominal out flow	Up to 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	More than 5 years
As at 31 December 2013								
Insurance contract liabilities	866.3	866.3	470.2	132.2	66.3	42.0	26.5	129.1
Financial liabilities at amortised cost:								
Subordinated debt	85.0	92.3	33.0	2.5	2.5	54.3	-	-
Insurance and other payables	17.9	17.9	17.9	-	-	-	-	-
Cash and cash equivalents	8.9	8.9	8.9	-	-	-	-	-
	978.1	985.4	530.0	134.7	68.8	96.3	26.5	129.1
Other liabilities	10.6							
Total recognised liabilities	988.7							

I. Credit risk

Credit Risk is the risk to earnings and capital arising from a debtor's failure to meet their legal and contractual obligations. CISGIL does not aim to earn a return from credit risk hence its appetite for credit risk is very low. Potential losses arising from credit risk are minimised by the use of high quality reinsurers and highly rated investments.

CISGIL's principal credit risk exposures are as follows:

- default or delay in payments due upon corporate bonds or cash;
- reinsurance counterparties failing to meet financial obligations or entering into restructuring arrangements that may adversely affect reinsurance recoveries; and
- default or delay of repayment of loans and receivables.

CISGIL manages credit risks associated with cash and corporate bonds as part of market risk. See Market Risk section above for details.

Where reinsurance is used to manage insurance risk, there is a risk that the reinsurer fails to meet its obligations in the event of a claim. CISGIL places limits over exposure to a single reinsurance counterparty, or counterparty group, based upon their credit-worthiness. These limits apply when reinsurance is initially placed, usually annually, and then regularly monitored by the Capital, Liquidity, Investment and Pension Committee. Where concern exists over reinsurer credit quality, watch lists are maintained and actively managed.

Insurance receivable and other assets are primarily premium debtors, with an element of salvage and subrogation recoveries and some accrued interest.

All amounts are stated in £m unless otherwise indicated

Principal risks (continued)
I. Credit risk (continued)
At the balance sheet date there were no significant concentrations of credit risk. The table below provides an analysis at the balance sheet date of the credit rating of those assets subject to credit risk. CISGIL's policy for making provisions for possible impairment is described within the accounting policy section on pages 20 and 21. Credit ratings are determined by taking an average of ratings provided by Moody's Investors Service, Standard & Poor's and Fitch.

	AAA	**AA**	**A**	**BBB and below**	**Not rated**	**Total**
As at 31 December 2014						
Financial assets at fair value through income or expense:						
Deposits with approved credit institutions (fixed rate)	**-**	**156.3**	**-**	**-**	**-**	**156.3**
Available for sale assets:						
Listed debt (fixed rate)	**100.2**	**245.7**	**287.1**	**82.6**	**-**	**715.6**
Listed debt (variable rate)	**-**	**-**	**36.8**	**12.2**	**-**	**49.0**
Reinsurance assets	**-**	**31.9**	**37.0**	**-**	**3.0**	**71.9**
Insurance receivables and other assets	**1.6**	**2.0**	**5.1**	**1.5**	**149.0**	**159.2**
	101.8	**435.9**	**366.0**	**96.3**	**152.0**	**1,152.0**
Assets not subject to credit risk						**22.0**
						1,174.0

	AAA	AA	A	BBB and below	Not rated	Total
As at 31 December 2013						
Financial assets at fair value through income or expense:						
Deposits with approved credit institutions (fixed rate)	-	-	207.6	-	-	207.6
Available for sale assets:						
Listed debt (fixed rate)	73.3	179.4	429.6	37.7	-	720.0
Listed debt (variable rate)	-	-	31.9	11.5	-	43.4
Loans and receivables at amortised cost	-	-	-	-	-	-
Reinsurance assets	-	25.0	28.9	-	2.9	56.8
Insurance receivables and other assets	1.1	1.6	7.8	0.4	197.6	208.5
	74.4	206.0	705.8	49.6	200.5	1,236.3
Assets not subject to credit risk						35.3
						1,271.6

The maximum exposure to credit risk, before making allowance for collateral held, is represented by the carrying value of each financial asset in the table. Collateral, in the form of gilts, of £143.5m (2013: £178.8m) is held as part of a reverse repo transaction with a cash balance of £147.0m as at 31 December 2014 (2013: £180.0m). Cash collateral pledged sits within deposits with approved credit institutions within financial investments at fair value through income or expense on the balance sheet.

All amounts are stated in £m unless otherwise indicated

Principal risks (continued)
I. Credit risk (continued)

Eurozone risk

CISGIL has no direct exposure to the sovereign debt of European countries. There is currently limited detailed knowledge of indirect exposure to European sovereign debt. Indirect exposure is managed as knowledge of an institution's direct exposure is made public. At this point, if the exposure is considered to be in excess of the risk appetite, action will be taken to reduce the risk through the sale of the relevant holdings. Indirect exposure to European countries is also considered as part of the reinsurance placement. The asset profile of the prospective companies is analysed and those which are over exposed are not included in placement of the programme.

The table below shows exposure to European countries arising from corporate bonds. CISGIL has no exposures to European countries as a result of repo arrangements.

	Up to 1 year	**1 to 5 years**	**5 to 10 years**	**Total**
As at 31 December 2014				
France	**-**	**7.1**	**-**	**7.1**
Germany	**-**	**30.1**	**-**	**30.1**
Netherlands	**9.1**	**38.6**	**-**	**47.7**
Spain	**-**	**21.8**	**-**	**21.8**
Sweden	**-**	**70.1**	**-**	**70.1**
	9.1	**167.7**	**-**	**176.8**

	Up to 1 year	1 to 5 years	5 to 10 years	Total
As at 31 December 2013				
France	-	7.2	-	7.2
Germany	-	43.0	28.3	71.3
Netherlands	-	9.4	-	9.4
Spain	-	29.3	-	29.3
Sweden	-	29.9	34.4	64.3
	-	118.8	62.7	181.5

J. Pension risk (unaudited)

Pension risk is defined as the risk to capital and company funds from exposure to scheme liabilities and risks inherent in the valuation of scheme liabilities and assets.

While CISGIL is not a participating employer, it has an agreement to pay pension contributions relating to staff employed by CFSMS that are assigned to work for CISGIL. This means that CISGIL is exposed to pension risk through the Co-operative Group pension scheme (PACE), a defined benefit scheme. The PACE trustee, in consultation with the Group, is responsible for the risk management arrangements for PACE, agreeing suitable contribution rates, investment strategy and for taking professional advice as appropriate. The scheme is managed at The Co-operative Group level.

In CISGIL’s accounts, the scheme is treated as a defined contribution scheme due to the multi-employer exemption. However, CISGIL is exposed to potential future increases in required contributions and capital is set aside for this. The impact of which is assessed under CISGIL's risk management framework and internal economic assessment of solvency, including the ICA. Costs arise through future accruals contribution, deficit repair contributions, expenses and potential employer debt under Section 75 of the Pensions Act. CISGIL engages with the Group to actively manage the volatility in the pension funding position by continuous monitoring, adjustments to scheme contributions, engagement of external advisors and review of investment and pension strategies.

During 2014, risks in the pension scheme were reduced through improving interest rate matching and reducing exposure to equity values.

K. Group risk (unaudited)

Group risk is defined as the risks that arise through being part of the Co-operative Group. Group risk includes elements of Reputation, Operational and Pension risks as per the sections above. CISGIL currently receives operational resources and certain services from Group through CFSMS. CISGIL is therefore subject to third party supplier risk of managing CFSMS and Group as intergroup suppliers. CISGIL ensures clear identification of Group risks and actively engages with the Group to ensure that Group risks are appropriately managed in a robust control environment.

Objectives when managing capital

For regulatory solvency capital purposes, CISGIL defines capital as share capital and reserves (after regulatory capital deductions and equalisation provisions) plus subordinated debt. The strategy in respect of capital management is to ensure that the following objectives are met:

- it has sufficient capital to meet all regulatory requirements;
- it has sufficient capital to support all the risks in the business, over the internally agreed time horizon and to the internally agreed level of confidence, thus ensuring that policyholders are protected and also that the Board's risk appetite is met; and
- subject to the above objectives being met, it makes the required return on equity.

Required capital

CISGIL is required to hold regulatory capital for its general insurance business in compliance with the rules issued by the Prudential Regulation Authority (PRA).

(a) Regulatory required capital

CISGIL is required to hold capital at the greatest of three measures, namely the Individual Capital Assessment (ICA), the Individual Capital Guidance (ICG) and the Minimum Capital Requirement (MCR). Each of these measures is further described below:

i) ICA: The ICA is an economic risk-based assessment of CISGIL's capital requirements using CISGIL's internal capital model. 2nd Line Risk has responsibility for the overall design and governance of the capital model, which is developed and operated within the actuarial team. Capital model methodology and results are reviewed and approved by the Model Governance Committee, ERC and Board. Outputs from the capital model are used in areas such as investment and reinsurance decisions, determining the risk in the business plans with regard to risk appetite and return on capital in pricing.

ii) ICG: The Prudential Regulation Authority (PRA) reviews the ICA calculation periodically to assess whether it believes the models and controls surrounding the models are adequate and, if it deems it necessary, an 'add-on' is applied to reflect risks that were inadequately captured. The total ICA plus 'add-on' is known as the ICG. In September 2014, the PRA provided CISGIL with an updated ICG, as a result of CISGIL's ICA submission in May 2014.

iii) MCR: In accordance with the General Prudential Sourcebook (GENPRU) 2.1, CISGIL must hold capital resources equal to or in excess of its capital resources requirement. For a company writing general insurance this is termed the MCR and is defined as being the higher of a base capital resource requirement and the general insurance capital requirement (a formulaic hurdle where the calculation is based upon premiums, claims or the brought forward requirement).

Capital requirements under the ICA and ICG are significantly in excess of the published MCR as they are set at a higher confidence level, and also reflect the specific risk-profile of the Issuer.

CISGIL Board sets capital risk appetite, which defines how much additional capital ("buffer capital") CISGIL should hold over and above its most onerous regulatory capital requirement. The risk appetite is currently to aim to hold a buffer at least sufficient to meet a 1-in-6 year event and to target a buffer sufficient to meet a 1-in-10 year event. Based on this risk appetite CISGIL currently aims to hold buffer capital equivalent to at least 31% of ICA, with a target equivalent to 38%. The risk appetite is reviewed periodically and while it is anticipated that the key tests referred to above will remain constant, the actual required buffer capital may change in the future as CISGIL's Internal Model is updated, including to reflect changes in CISGIL's risk exposure, and as CISGIL moves from an ICA basis to Solvency II.

The ICA capital requirement is determined by reference to the risks faced by the business. Consequently, it is possible to reduce capital requirements by executing actions that reduce risk, albeit often resulting in reduced returns. Management have identified potential actions which fall into three main categories:

- Actions to reduce insurance risk through reinsurance for future large claims or catastrophe and adverse development cover for existing reserves. These actions will reduce the potential volatility of CISGILs results, thus having a positive impact on capital requirements;
- Actions to reduce other types of risk – for example, de-risking the investment portfolio; and
- Actions that would require an increased risk appetite – for example, holding a smaller margin over best estimate in claims reserves.

Actions are available in the first two categories for implementation later within 2015. No actions are being taken that would require an increased risk appetite as this is not felt to be appropriate at this time.

CISGIL has improved the overall quality of its capital base through the issuing of £85m of equity (tier one capital), the proceeds of which have been used to repay existing tier two capital subordinated loans.

All amounts are stated in £m unless otherwise indicated

(a) Regulatory required capital (continued)

While CISGIL has maintained capital above all its regulatory requirements throughout the period, since September 2014 CISGIL has fallen below its 1-in-6 year risk appetite buffer capital requirement. Additional capital is required to ensure CISGIL remains within risk appetite over the 2015-2019 Financial Plan period, and to ensure the success of the transformation programme which will also impact on the capital base of the company. CISGIL is seeking a capital injection in the first half of 2015 to address this.

CISGIL reviews solvency continuously through weekly, or when appropriate daily, monitoring. Monthly reports are provided to the Executive Risk Committee and Board.

(b) Capital composition

CISGIL regulatory MCR capital resources comprise total shareholders' equity, excluding inadmissible assets and equalisation provisions recognised in equity.

	2014	2013
Capital and reserves per the financial statements	**381.4**	282.9
Subordinated debt	**-**	85.0
Inadmissible assets	**(6.2)**	(1.8)
Statutory claims equalisation reserve	**(29.6)**	(30.1)
Discounting on technical provisions	**(1.5)**	(0.9)
Regulatory capital	**344.1**	335.1

The new solvency framework for insurers being developed by the EU, referred to as 'Solvency II', is intended to achieve greater harmonisation of approach across EU member states to assessing capital resources and requirements. Solvency II is due to come into force on 1 January 2016. Under Solvency II, the Solvency Capital Requirement (SCR) will replace the ICA and ICG, and the MCR will be re-defined. CISGIL is actively progressing with activities to meet the required standards and with preparations to apply to the PRA for approval to use CISGIL's capital model to calculate the SCR.

All amounts are stated in £m unless otherwise indicated

1. Segmental analysis

The business segments of CISGIL are presented in line with the management information as reported to the Chief Executive Officer, the Chief Operating Decision Maker (CODM).

CISGIL evaluates the performance of operating segments on the basis of the combined operating ratio, being the ratio of combined costs (operating expenses, claims and commission, net of other income) to net earned premiums. Overall CISGIL performance is evaluated on the basis of profit or loss from operations before tax attributable to shareholders, adjusted for non-operating items outside the control of the management, including variances in investment performance resulting from significant changes in external market conditions.

There is no geographic segmental reporting as all business is conducted in the UK. Revenues are attributed to the segments in which they are generated.

Segmental results include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. The accounting policies of the business segments are the same as those described in the summary of significant accounting policies.

Business segments
CISGIL comprises the following segments:
- **Motor** – Private motor car and motor cycle, individual commercial vehicles.
- **Home** – Domestic buildings, contents and personal possessions.
- **Other** – Commercial risks covering property, liability, financial loss, and motor fleet. Other minor personal risks, pet, run off of inwards reinsurance liabilities, Financial Services Compensation Scheme levies and finance costs.

Segmented income statement for the year ended 31 December 2014

	Motor	**Home**	**Other**	**Total**
Net earned premiums	**233.3**	**137.5**	**1.8**	**372.6**
Net claims incurred	**(182.2)**	**(57.1)**	**(9.3)**	**(248.6)**
Net commission (expenses)/income	**(3.0)**	**(5.8)**	**1.6**	**(7.2)**
Operating expenses	**(81.9)**	**(53.3)**	**(2.4)**	**(137.6)**
Net investment return	**18.5**	**3.3**	**0.6**	**22.4**
Other expenses	**(6.8)**	**(1.4)**	**(0.2)**	**(8.4)**
Segmented operating (loss)/profit	**(22.1)**	**23.2**	**(7.9)**	**(6.8)**

Segmented income statement for the year ended 31 December 2013

	Motor	Home	Other	Total
Net earned premiums	314.6	158.8	3.1	476.5
Net claims incurred	(256.1)	(64.1)	(10.6)	(330.8)
Net commission (expenses)/income	(1.5)	(8.3)	3.3	(6.5)
Operating expenses	(77.4)	(58.9)	(2.0)	(138.3)
Net investment return	33.9	5.2	0.8	39.9
Other expenses	-	-	(7.2)	(7.2)
Segmented operating profit/(loss)	13.5	32.7	(12.6)	33.6

Reconciliation of segmental income to statutory income statement

Net earned premiums and claims are reported on a consistent basis for segmental and statutory reporting purposes.

	2014	2013
Operating expenses		
Total operating expenses for reportable segments	**(137.6)**	(138.3)
Items reported as significant within management information	**(6.0)**	(1.3)
Reclassification of investment expenses	**(1.2)**	(1.3)
Financial Services Compensation Scheme levies	**1.0**	(2.4)
Operating expenses	**(143.8)**	(143.3)

All amounts are stated in £m unless otherwise indicated

1. Segmental analysis (continued)

Reconciliation of segmental income to statutory income statement (continued)

	2014	2013
Commission expenses		
Total commission expenses for reportable segments	**(7.2)**	(6.5)
Reclassification of commission income	**(9.5)**	(13.3)
Fee and commission expenses	**(16.7)**	(19.8)
Other expenses is made up of:		
Financial Services Compensation Scheme levies	**1.0**	(2.4)
Items reported as significant within management information	**(6.0)**	(1.3)
Finance costs	**(3.4)**	(3.5)
	(8.4)	(7.2)
Investment return		
Total investment return for reportable segments	**22.4**	39.9
Reclassification of investment expenses	**1.2**	1.3
Reclassification of other operating income	**-**	(0.3)
Investment return (analysed as below in the income statement)	**23.6**	40.9
Investment income	**20.6**	27.9
Gains less losses arising from financial instruments	**3.0**	13.0
	23.6	40.9

2. Net earned premiums

	2014	2013
Gross premiums		
Gross written premiums	**365.2**	443.6
Change in unearned premium provision	**34.8**	65.4
Gross earned premiums	**400.0**	509.0
Outward reinsurance premiums		
Premiums ceded	**(25.7)**	(32.3)
Change in unearned premium provision	**(1.7)**	(0.2)
Premiums ceded to reinsurers	**(27.4)**	(32.5)
Net earned premiums	**372.6**	476.5

3. Fee and commission income

	2014	2013
Fee income	**6.5**	8.7
Reinsurance commission earned	**2.3**	3.7
Other commission	**0.7**	0.9
	9.5	13.3

Fee income is in respect of brokerage commission and one-off fee income primarily in respect of policy adjustments.

All amounts are stated in £m unless otherwise indicated

4. Investment income

	2014	2013
Interest and similar income from assets held at fair value through income or expense:		
Deposits with credit institutions	**0.7**	1.2
	0.7	1.2
Interest income (calculated using Effective Interest Rate) from available for sale assets:		
Listed debt securities	**19.9**	26.7
	20.6	27.9

5. Gains less losses arising from financial instruments

	2014	2013
Net gains arising on financial assets:		
Available for sale listed debt securities	**3.0**	13.0
	3.0	13.0

6. Other operating income

Other operating income includes £nil (2013: £0.3m) of interest income in respect of a loan to the Co-operative Group Limited. In February 2013 the Group repaid this loan in full.

7. Net policyholder claims and benefits paid

	2014	2013
Gross claims paid		
Current year claims	**136.7**	154.1
Prior year claims	**253.1**	282.6
Gross claims paid	**389.8**	436.7
Less salvage and subrogation		
Current year claims	**(10.7)**	(10.2)
Prior year claims	**(14.7)**	(16.5)
Salvage and subrogation received	**(25.4)**	(26.7)
Claims paid	**364.4**	410.0
Less amounts receivable from reinsurers		
Current year claims	**(4.0)**	(4.2)
Prior year claims	**(3.8)**	(2.6)
Amounts receivable from reinsurers	**(7.8)**	(6.8)
Net policyholder claims and benefits paid	**356.6**	403.2

8. Fee and commission expenses

	2014	2013
Commission paid	**16.1**	18.5
Change in deferred commission	**0.6**	1.3
	16.7	19.8

9. Operating expenses

	2014	2013
Administration expenses	**90.7**	93.4
Acquisition expenses	**47.1**	49.9
Costs related to the transformation programme	**6.0**	-
	143.8	143.3

CISGIL does not have any employees; all sales are effected by employees of CFS Management Services Limited (CFSMS) which also provides administration and other services. CFSMS is also responsible for the remuneration of all directors of the Banking Group, including directors of CISGIL. CISGIL's share is charged to the company, at cost, by way of a management service charge from CFSMS. Key management compensation is discussed in note 28.

Included within the recharge is £5.9m (2013: £7.6m) paid by CISGIL in respect of its share of regular pension contributions, which includes £1.9m (2013: £2.0m) in respect of the PACE pension deficit funding. The details of the PACE scheme are included in the financial statements of The Co-operative Group.

Operating expenses include the following payments to auditors and their associates:

	2014 £'000	2013 £'000
Audit of these financial statements	**173**	130
Amounts receivable by CISGIL's auditor and its associates in respect of:		
Audit-related assurance services	**79**	61
Other assurance services	**194**	33
	446	224

Audit-related assurance services are in respect of the audit of regulatory returns and half year review of interim financial information for consolidation into Interim Report for the Co-operative Group. Other assurance services relates to assurance reporting on CISGIL's preparations for Solvency II.

10. Income tax

	2014	2013
Current tax		
UK tax for the current year	**0.2**	7.5
UK tax adjustments in respect of prior years	**-**	(0.9)
Total current tax charge	**0.2**	6.6
Deferred tax		
Origination and reversal of temporary differences	**(0.1)**	0.1
Effect of tax rate change	**-**	(0.8)
Total deferred tax credit	**(0.1)**	(0.7)
Total tax charge recognised in the income statement	**0.1**	5.9

Further information about deferred income tax is presented in note 22.

Reconciliation of effective tax rate

The tax charge in the income statement differs from the theoretical amount that would arise using the corporation tax rate in the UK as follows:

	2014	2013
Profit before taxation	**(6.8)**	33.6
Tax calculated at domestic corporation tax rate of 21.49% (2013: 23.25%)	**(1.5)**	7.8
Effect of:		
Tax rate change on deferred tax	**-**	(0.9)
Other adjustments	**1.6**	(1.0)
Income tax charge	**0.1**	5.9

Other adjustments includes expenses not deductible for tax purposes and payment and surrender of group relief.

All amounts are stated in £m unless otherwise indicated

11. Property, plant and equipment

	Fixtures & Fittings	Assets in course of constuction	Total
2014			
Cost			
At the beginning of the financial year	-	-	-
Additions	0.4	0.1	0.5
Disposals	(0.1)	-	(0.1)
At the end of the financial year	0.3	0.1	0.4
Depreciation			
At the beginning of the financial year	-	-	-
Depreciation charge for the financial year	0.2	-	0.2
Disposal	-	-	-
At the end of the financial year	0.2	-	0.2
Carrying amount			
At the end of the financial year	0.1	0.1	0.2
At the beginning of the financial year	-	-	-

During 2014 £0.5m of tangible assets were transferred from CFSMS, a fellow subsidiary of Co-operative Banking Group Limited. No profit or loss arose on the transfer of the assets.

12. Intangible Assets

	Computer Software	Assets in course of construction	Total
2014			
Cost			
At the beginning of the financial year	-	-	-
Additions	-	1.6	1.6
Disposals	-	-	-
Transfers	0.1	(0.1)	-
At the end of the financial year	0.1	1.5	1.6
Amortisation			
At the beginning of the financial year	-	-	-
Amortisation charge for the financial year	-	-	-
Revaluation	-	-	-
At the end of the financial year	-	-	-
Carrying amount			
At the end of the financial year	0.1	1.5	1.6
At the beginning of the financial year	-	-	-

£1.6m of intangible assets include £1.4m that were transferred during the year from CFSMS, a fellow subsidiary of Co-operative Banking Group Limited. No profit or loss arose on the transfer of the assets.

13. Deferred acquisition costs

	2014	2013
At the beginning of the financial year	**35.3**	29.9
Deferred acquisition costs	**46.7**	70.4
Amortisation	**(61.8)**	(65.0)
At the end of the financial year	**20.2**	35.3

All amounts in the current and prior year are expected to be recovered within one year.

All amounts are stated in £m unless otherwise indicated

14. Financial investments at fair value through income or expense

	2014	2013
Deposits with credit institutions	**156.3**	207.6

All amounts in the current and prior year are expected to be recovered within one year. Within the above are reverse repo balances of £147.0m (2013: £180.0m). Collateral of £147.0m is held as security against this balance (2013: £178.8m). Please see the credit risk note on pages 31 to 33 for further details.

This category comprises short term fixed rate deposits which are designated as fair value through income and expense upon initial recognition. There has been no reclassification of financial assets between fair value and cost/amortised cost during the current or prior financial year.

15. Available for sale assets

	2014	2013
Listed debt securities - fixed rate	**715.6**	720.0
Listed debt securities - floating rate	**49.0**	43.4
	764.6	763.4

At 31 December 2014, debt securities of £661.3m (2013: £670.4m) are expected to be recovered more than 12 months after the reporting date.

16. Insurance receivables and other assets

	2014	2013
Receivables arising from insurance:		
Arising from insurance operations	**118.4**	100.0
Salvage and subrogation recoveries	**21.8**	24.5
Reinsurance operations	**0.7**	1.2
Other receivables:		
Accrued interest	**10.9**	12.6
Amounts receivable from Group companies	**7.0**	6.8
Prepayments	**0.4**	-
Investment receivables	**-**	63.4
	159.2	208.5

No amounts are due after more than one year.

Receivables arising from insurance operations are stated net of an impairment provision of £0.3m (2013: £0.5m). The provision is calculated based on an assessment of insurance receivables for objective evidence that an impairment loss has been incurred. Any adjustment to the level of the provision is recorded within the income statement as an adjustment to written premium.

Insurance receivables and other assets include amounts totalling £13.1m (2013: £13.3m) which are overdue; amounts overdue but not impaired are £12.8m (2013: £12.8m), being the overdue amount net of the impairment provision detailed above. £0.7m (2013: £1.1m) of amounts overdue primarily represent debts due from brokers and intermediaries which are considered fully recoverable. Amounts overdue are age analysed as follows:

	2014	2013
Amounts overdue:		
Less than 3 months	**12.7**	12.2
3 to 6 months	**0.1**	-
6 to 12 months	**0.3**	1.1
More than 12 months	**-**	-

Assets past due typically comprise high volume/low value balances for which CISGIL does not seek collateral but continues to work with counterparties to secure settlement.

All amounts are stated in £m unless otherwise indicated

17. Bank overdraft

Bank overdrafts are repayable on demand and form an integral part of CISGIL's cash management. As such they are included as cash and cash equivalents for the purpose of the statement of cash flows.

18. Share capital

	2014	2013
Authorised		
	268.0	183.0
Issued and fully paid		
268,000,000 ordinary shares of £1 each	**268.0**	183.0

Each shareholder has one vote and an additional vote for every 50 shares or fraction or part held by it in excess of the first 50 shares held.

During 2014, a total of 85,000,000 ordinary shares of £1 each were issued and fully paid at par.

19. Retained earnings and other reserves

	2014	2013
Retained earnings		
At the beginning of the financial year	**49.9**	22.2
(Loss)/profit for the year	**(6.9)**	27.7
At the end of the financial year	**43.0**	49.9

Any retained earnings would represent amounts available for dividend distribution to the equity shareholder of CISGIL, subject to certain conditions being met.

Other reserves of £70.4m (2013: £50.0m) constitute available for sale reserves and a capital reserve. The capital reserve represents a non-refundable capital contribution from the immediate parent company, the Co-operative Banking Group Limited, and is distributable. Further details are given within the statement of changes in equity on page 16.

20. Other borrowed funds

	2014	2013
Floating rate subordinated notes 2021	**-**	35.0
Floating rate perpetual subordinated notes	**-**	30.0
Fixed rate perpetual subordinated notes	**-**	20.0
	-	85.0

In December 2014, the following subordinated notes were repaid to the immediate parent company, the Co-operative Banking Group Limited:

Floating rate subordinated notes 2021
The notes were issued on 15 January 2006 at par.

Floating rate perpetual subordinated notes
The notes were issued in 2 tranches, £20m issued on 30 July 2007, followed by a further £10m on 15 August 2007.

Fixed rate perpetual subordinated notes
The notes were issued on 30 November 2011 at par.

There have been no defaults or breaches of contractual obligations attaching to the subordinated debt during the financial year.

Finance costs incurred during the financial period include £3.2m (2013: £3.3m) in relation to interest on the subordinated debt.

All amounts are stated in £m unless otherwise indicated

21. Insurance contract liabilities and reinsurance assets

(a) Analysis of insurance contract liabilities

	2014	2013
Gross		
Claims reported	**406.7**	495.3
Claims incurred but not reported	**135.1**	144.9
Claims settlement expenses	**12.6**	16.7
Unearned premiums	**172.4**	207.2
Unexpired risk provision	**10.8**	2.2
Total gross insurance liabilities	**737.6**	866.3
Recoverable from reinsurers		
Claims reported	**(39.2)**	(23.2)
Claims incurred but not reported	**(32.3)**	(31.5)
Unearned premiums	**(0.4)**	(2.1)
Total reinsurers' share of insurance liabilities	**(71.9)**	(56.8)
Net		
Claims reported	**367.5**	472.1
Claims incurred but not reported	**102.8**	113.4
Claims settlement expenses	**12.6**	16.7
Unearned premiums	**172.0**	205.1
Unexpired risk provision	**10.8**	2.2
Total net insurance liabilities	**665.7**	809.5

Reinsurance is used to limit risk to the balance sheet for the various classes of general insurance direct business. Proportional and non-proportional types of reinsurance cover have been purchased in accordance with assumptions made regarding the possible levels of losses and required returns on equity.

Indemnification agreement

On 15 January 2006, CISGIL assumed responsibility for the benefits and burdens arising from the run off of general insurance liabilities of the Co-operative Insurance Society Limited (CISL) under the terms of an indemnification agreement. Insurance contract liabilities at the end of 2013 included £63.5m of gross liabilities from the policies underwritten by CISL. These policies were formally novated by the Part VII transfer to CISGIL on 31 March 2014. Consequently, the analysis in note 21 v) shows claims development of all general insurance liabilities.

(b) General insurance contracts – assumptions, changes in assumptions and sensitivity

i) Basis of assessing liabilities

CISGIL has access to historical data and trends relating to the general insurance business of CISL for which it has now assumed responsibility.

CISGIL uses a combination of recognised actuarial and statistical techniques to assess the ultimate cost of claims. These include:

- projecting historic claims payment and recoveries data;
- projecting numbers of claims;
- adjusting case estimates for future inflation and onto a provisioning basis;
- deriving average costs per claim to apply to claim numbers; and
- projecting historic claims paid and incurred data (payment plus estimates) – statistical actuarial techniques including chain ladder, Bornhuetter-Ferguson and Cape Cod.

21. Insurance contract liabilities and reinsurance assets (continued)

(b) General insurance contracts – assumptions, changes in assumptions and sensitivity (continued)

Detailed claims data, including individual case estimates, is used to derive patterns in average claims costs and timings between occurrence and estimate/payment of claims. The most common method used is the chain ladder method. This technique involves the analysis of historical claims development trends and the selection of estimated development factors based on this historical pattern. The selected development factors are then applied to cumulative claims data for each accident year which is not yet fully developed to produce an estimated ultimate claims cost for each accident year. A degree of judgment is required in selecting the most appropriate development factors.

The chain ladder method can be volatile for relatively undeveloped origin periods so a Bornhuetter-Ferguson/Cape Cod method is often used in such cases. This method uses some prior expectation of the ultimate claims, and stabilises the projected ultimate by weighting between the prior expected ultimate and the projected based on the assumed development factors. The Cape Cod method differs from the Bornhuetter-Ferguson method in that it uses a trending of ratios (such as the average cost) to arrive at a prior expected ultimate for use in the projections.

The work is undertaken and supervised by suitably qualified personnel. Claims provisions are separately computed for each claim type such as bodily injury, accidental damage, storm, flood and subsidence. All provisions are calculated with explicit allowance for reinsurance and subrogation recoveries. Provisions are not discounted for investment return other than any required additional provision for unexpired risks, periodic payment settlements and provisions relating to exposure within the electric industry ('EIROS' claims).

Discounted reserves in respect of periodic payment settlements are £21.4m (2013: £23.8m) and EIROS discounted reserve amounts to £3.8m (2013: £2.7m). Further details around expected settlement patterns for claims arising on these reserves are disclosed within the insurance risk section on pages 27 and 28.

The EIROS reserve was based on a report produced for the industry at the end of 2013, by Towers Watson an actuarial consultancy. This gave Towers Watson's estimate of both the undiscounted and discounted incurred but not reported (IBNR) reserves as at the end of June 2013. This was the most recent report available when CISGIL calculated its year end 2014 reserves.

In respect of business yet to be earned, the adequacy of the premium to cover future claims costs and expenses was assessed to determine the requirement for an Unexpired Risk Provision (URP) by comparing the discounted premium and outgoings. As at the end of 2014 CISGIL held an URP of £10.8m (2013: £2.2m).

As outlined within the risk management section, there is significant uncertainty in the assessment of liabilities, and provisions are set to be adequate to cover the anticipated eventual cost. Sensitivity analysis is performed to assist the selection of key parameters and, hence, the provisions adopted. Provisions are subject to detailed review regarding the appropriateness of key assumptions and the quantum of the provisions established.

The overall objective of CISGIL's reserving policy is to produce reliable and accurate reserves. Assumptions underlying the reserving calculations are agreed by the Quarterly Reserving Committee (QRC). Methodologies are peer reviewed throughout the calculation process. Provisions are approved and signed off by the QRC, and any margin above the actuarial best estimate reserve is set by the Chief Financial Officer.

Periodic reports are produced by the actuarial team and presented to the Periodic Reserving Committee in order to advise management of the performance of the business. More detailed reports are produced on a quarterly basis providing information on the performance of the business against plan. These reports are presented to the QRC and form the basis of reporting the performance to the Board.

ii) Key assumptions

Principal assumptions underlying the claims provisions include:

- Allowance for future inflation rates being different to those implied in the claims data; and
- for bodily injury claims allowance has been made for:
  i. use of the appropriate Ogden Tables;
  ii. awards for general damages in accordance with the 12th edition of the JSB guidelines;
  iii. a proportion of large claims being settled by periodic payments; and
  iv. improvements in the case estimation techniques resulting in earlier recognition of the size of claims.

All amounts are stated in £m unless otherwise indicated

21. Insurance contract liabilities and reinsurance assets (continued)

(b) Change in general insurance liabilities and reinsurance assets

The gross insurance provision for claims and loss adjustment expenses arising in respect of prior years of £392.7m (2013: £427.1m) includes a movement of £10.9m (2013: £47.3m) arising from a release of reserves, as follows:

	2014	2013
Fire and Accident (increase)/release of reserves	**(4.2)**	7.2
Motor release of reserves	**19.1**	42.8
(Increase) in claims handling reserves	**(4.0)**	(2.7)
Movement in gross insurance liabilities	**10.9**	47.3

iii) Sensitivity analysis

There is greater uncertainty over motor claims provisions than other provisions as they often involve claims for bodily injury and associated legal costs which typically have a longer period to settlement. Motor provisions represent the most significant proportion of the total general insurance outstanding claims liabilities (gross of salvage and subrogation). Sensitivity information is given for motor claims provisions together with limited information for all other classes. The following table indicates the effect on gross claims provisions (gross of reinsurance and salvage and subrogation) of changes in key assumptions. The impact of the increased uncertainty on the income statement risk is mitigated through holding management margin on the best estimate reserves that is proportional to the level of uncertainty.

2014	**Change in parameter**	**Effect on gross provision**	**% Effect**
Assumption			
Motor			
Average cost of claims for last three years - bodily injury and legal	**10%**	**47.1**	**11.4%**
Mean term to settlement - bodily injury and legal	**+½ year**	**8.1**	**2.0%**
Rate of future inflation - bodily injury and legal	**1%**	**12.6**	**3.1%**
Ogden discount rate - bodily injury	**-¼%**	**3.8**	**0.9%**
Other classes			
Mean term to settlement (liability)	**+½ year**	**0.6**	**2.1%**
Mean term to settlement (non-liability)	**+½ year**	**0.6**	**1.5%**
Rate of future inflation (liability)	**1%**	**1.7**	**6.4%**
Rate of future inflation (non-liability)	**1%**	**0.5**	**1.2%**

2013	Change in parameter	Effect on gross provision	% Effect
Assumption			
Motor			
Average cost of claims for last three years - bodily injury and legal	10%	65.0	12.3%
Mean term to settlement - bodily injury and legal	+½ year	10.3	1.9%
Rate of future inflation - bodily injury and legal	1%	18.4	3.5%
Ogden discount rate - bodily injury	-¼%	2.2	0.4%
Other classes			
Mean term to settlement (liability)	+½ year	0.4	2.1%
Mean term to settlement (non-liability)	+½ year	0.8	1.4%
Rate of future inflation (liability)	1%	0.9	4.9%
Rate of future inflation (non-liability)	1%	0.7	1.3%

(c) Change in general insurance liabilities and reinsurance assets

i) Change in insurance contract liabilities (net of salvage and subrogation)

2014	**Gross**	**Unexpired risk provision**	**Salvage & subrogation**	**Net**
At the beginning of the year	**656.9**	**2.2**	**(24.5)**	**634.6**
Movement in the year	**(102.4)**	**8.6**	**2.7**	**(91.1)**
At the end of the year	**554.5**	**10.8**	**(21.8)**	**543.5**

All amounts are stated in £m unless otherwise indicated

21. Insurance contract liabilities and reinsurance assets (continued)

(c) Change in general insurance liabilities and reinsurance assets (continued)

i) Change in insurance contract liabilities (net of salvage and subrogation)

	Gross	Unexpired risk provision	Salvage & subrogation	Net
2013				
At the beginning of the year	756.1	-	(61.4)	694.7
Movement in the year	(99.3)	2.2	36.9	(60.2)
At the end of the year	656.9	2.2	(24.5)	634.5

Salvage and subrogation is included within assets as part of insurance receivables (note 16).

ii) Claims and loss adjustment expenses

	Gross 2014	Reinsurance 2014	Net 2014	Gross 2013	Reinsurance 2013	Net 2013
Claims reported	**495.3**	**(23.2)**	**472.1**	557.5	(16.1)	541.4
Claims incurred but not reported	**144.9**	**(31.5)**	**113.4**	180.4	(26.4)	154.0
Claims settlement expenses	**16.7**	**-**	**16.7**	18.2	-	18.2
At the beginning of the year	**656.9**	**(54.7)**	**602.2**	756.1	(42.5)	713.6
Claims paid during the year	**(389.8)**	**7.8**	**(382.0)**	(436.7)	6.8	(429.9)
Increase/(decrease) in liabilities:						
Arising from current year claims	**298.3**	**(8.9)**	**289.4**	384.7	(17.2)	367.5
Arising from prior year claims	**(10.9)**	**(15.8)**	**(26.7)**	(47.3)	(1.8)	(49.1)
Total movement	**(102.4)**	**(16.9)**	**(119.3)**	(99.3)	(12.2)	(111.5)
Claims reported	**406.7**	**(39.2)**	**367.5**	495.3	(23.2)	472.1
Claims incurred but not reported	**135.1**	**(32.3)**	**102.8**	144.9	(31.5)	113.4
Claims settlement expenses	**12.6**	**-**	**12.6**	16.7	-	16.7
At the end of the year	**554.4**	**(71.5)**	**482.9**	656.9	(54.7)	602.2

iii) Provisions for unearned premiums

	Gross 2014	Reinsurance 2014	Net 2014	Gross 2013	Reinsurance 2013	Net 2013
At the beginning of the year	**207.2**	**(2.1)**	**205.1**	272.6	(2.3)	270.3
Increase in the year	**365.2**	**(25.7)**	**339.5**	443.6	(32.3)	411.3
Release in the year	**(400.0)**	**27.4**	**(372.6)**	(509.0)	32.5	(476.5)
Movement in the year	**(34.8)**	**1.7**	**(33.1)**	(65.4)	0.2	(65.2)
At the end of the year	**172.4**	**(0.4)**	**172.0**	207.2	(2.1)	205.1

iv) Unexpired risk provision

	Gross 2014	Reinsurance 2014	Net 2014	Gross 2013	Reinsurance 2013	Net 2013
At the beginning of the financial year	**2.2**	**-**	**2.2**	-	-	-
Increase in the financial year	**10.8**	**-**	**10.8**	2.2	-	2.2
Release in the financial year	**(2.2)**	**-**	**(2.2)**	-	-	-
Movement in the financial year	**8.6**	**-**	**8.6**	2.2	-	2.2
At the end of the financial year	**10.8**	**-**	**10.8**	2.2	-	2.2

Additional provision is made for unexpired risks where the claims and expense, likely to arise after the end of the financial year, in respect of contracts concluded before that date, are expected to exceed the unearned premiums at the end of the financial year. The provision related to the motor class of business. Further details can be found in the accounting policy on page 23.

All amounts are stated in £m unless otherwise indicated

21. Insurance contract liabilities and reinsurance assets (continued)

(v) Analysis of claims development

	Accident year											
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	**2014**	**Total**
Gross of reinsurance												
At end of the accident year:	550.5	480.1	419.3	384.5	347.3	325.9	411.3	497.0	502.1	368.1	284.7	**4,570.8**
One year later	527.1	468.3	412.1	387.8	319.7	333.1	455.4	530.2	473.3	346.9		**4,253.9**
Two years later	495.3	439.9	402.6	378.3	310.2	340.5	480.1	527.4	473.0			**3,847.3**
Three years later	467.2	414.0	393.5	364.2	300.3	328.7	465.5	518.1				**3,251.5**
Four years later	450.3	422.8	387.1	367.0	296.7	320.0	456.3					**2,700.2**
Five years later	453.9	418.6	387.7	366.3	293.6	320.4						**2,240.5**
Six years later	453.1	422.0	382.4	362.1	294.1							**1,913.7**
Seven years later	453.2	429.5	385.1	360.5								**1,628.3**
Eight years later	451.8	428.5	383.7									**1,264.0**
Nine years later	453.2	426.8										**880.0**
Ten years later	453.8											**453.8**
Estimate for cumulative claims	453.8	426.8	383.7	360.5	294.1	320.4	456.3	518.1	473.0	346.9	284.7	**4,318.3**
Cumulative payments to date	(448.5)	(404.1)	(370.8)	(348.9)	(291.3)	(306.4)	(432.7)	(472.0)	(381.1)	(247.4)	(129.1)	**(3,832.3)**
Gross outstanding claims liabilities before discounting	5.3	22.7	12.9	11.6	2.8	14.0	23.6	46.1	91.9	99.5	155.6	**486.0**
Provision for prior years before discounting												**57.2**
Discounting												**(1.5)**
Gross outstanding claims liabilities												**541.7**
Gross claims reported												**406.6**
Gross claims incurred but not reported												**135.1**
Gross outstanding claims liabilities												**541.7**

Gross ultimates have increased as the indemnification agreement came into force after the application of CIS Reinsurance contracts. Following the Part VII transfer, CISGIL have now taken on the Gross Liabilities that were previously reinsured under CIS Reinsurance contracts.

All amounts are stated in £m unless otherwise indicated

21. Insurance contract liabilities and reinsurance assets (continued)

(v) Analysis of claims development (continued)

	Accident year											
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	**2014**	**Total**
Net of reinsurance												
At end of the accident year:	547.2	477.6	416.6	372.6	334.6	313.1	398.4	481.2	489.8	350.9	**275.9**	**4,457.9**
One year later	525.1	465.8	408.9	377.8	305.5	320.7	434.3	514.8	456.3	330.4		**4,139.6**
Two years later	493.3	437.4	400.8	369.8	296.3	325.4	458.6	516.5	458.7			**3,756.8**
Three years later	465.2	411.0	392.5	357.8	291.8	317.6	445.2	509.4				**3,190.5**
Four years later	448.0	420.1	386.0	359.4	289.6	310.0	439.4					**2,652.5**
Five years later	451.5	414.1	385.2	359.2	287.2	307.3						**2,204.5**
Six years later	450.8	414.8	380.2	355.2	287.8							**1,888.8**
Seven years later	451.1	420.6	379.7	353.7								**1,605.1**
Eight years later	449.8	420.6	379.3									**1,249.7**
Nine years later	451.1	419.3										**870.4**
Ten years later	451.7											**451.7**
Estimate for cumulative claims	451.7	419.3	379.3	353.7	287.8	307.3	439.4	509.4	458.7	330.4	**275.9**	**4,212.9**
Cumulative payments to date	(446.5)	(402.9)	(370.4)	(342.1)	(285.0)	(300.9)	(425.3)	(466.5)	(375.8)	(242.0)	**(125.2)**	**(3,782.6)**
Net outstanding claims liabilities before discounting	5.2	16.4	8.9	11.6	2.8	6.4	14.1	42.9	82.9	88.4	150.7	**430.3**
Provision for prior years before discounting												**41.3**
Discounting												**(1.5)**
Net outstanding claims liabilities												**470.1**
Net claims reported												**367.4**
Net claims incurred but not reported												**102.7**
Net outstanding claims liabilities												**470.1**

It is to be expected that releases will normally be made to prior years claims as current reserves are set such that no adverse deterioration is expected. However, from time to time the random occurrence of significant large individual claims or events being worse than expected can give rise to a required strengthening, in addition to normal claims development being adverse. The 2014 result includes movement on prior year reserves of £26.7m (2013: £49.1m).

All amounts are stated in £m unless otherwise indicated

22. Taxation

	2014	2013
Current tax		
Liability at the beginning of the financial year	**(4.9)**	(4.0)
Tax charged to the income statement	**(0.2)**	(6.6)
Tax (charged)/credited directly to other comprehensive income:		
Changes in fair value on available for sale assets recognised through other comprehensive income	**(5.5)**	6.3
Tax received during the financial year	**-**	(0.6)
Liability at the end of the financial year	**(10.6)**	(4.9)

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 20% (2013: 20%).

	2014	2013
Deferred tax liability		
Liability at the beginning of the financial year	**(5.7)**	(6.4)
Tax credited to the income statement	**0.1**	0.7
Liability at the end of the financial year	**(5.6)**	(5.7)
Analysis of deferred tax liability		
Claims equalisation reserve	**(5.9)**	(6.0)
Other timing differences	**0.3**	0.3
Liability at the end of the financial year	**(5.6)**	(5.7)

Transfers to the equalisation reserve totalling £29.6m as at 31 December 2014 have been treated as tax deductible, however for accounts purposes the corresponding value is nil. The difference has been recognised as part of the Deferred Tax liability at 20%.

The Finance Act 2013 reduced the main rate of corporation tax from 23% to 21% from 1 April 2014. This will be further reduced to 20% from 1 April 2015. The rate reductions will reduce the company's future current tax charge and deferred tax liability accordingly.

23. Other reinsurance liabilities

	2014	2013
Arising from reinsurance operations	**0.5**	-
	0.5	-

All amounts are due within one year.

24. Insurance and other payables

	2014	2013
Arising out of direct insurance operations	**1.4**	1.7
Accruals and deferred income	**16.8**	5.7
Insurance premium taxation payable	**6.6**	7.6
Other payables	**5.6**	2.9
	30.4	17.9

All amounts are due within one year.

25. Contingent assets and liabilities

CISGIL has a contract with Parabis Ltd for the provision of claims handling services for third party motor claims. These services are currently treated as VAT exempt within the annual report and accounts. However, this treatment has been challenged by Her Majesty's Revenue & Customs (HMRC). If the view of HMRC is upheld, CISGIL will be liable for a VAT charge (from 2010) of up to £2.6m (2013: £2.1m). Legal Counsel has indicated that it is probable that HMRC's view will be successfully challenged, and therefore a provision has not been made in the financial statements.

During 2012, a provision was raised by CISL, at the time a fellow subsidiary of the Co-operative Banking Group Limited, to cover the present value of lease commitments arising from the failure of a counterparty to which a number of leases had previously been assigned. As CISGIL benefited from the original assignment transaction, CISGIL made a cash contribution in 2012 of £2.6m towards the initial provision. In 2013, the provision and CISGIL's cash contribution was transferred into CFSMS. CISGIL has an agreement with CFSMS, to contribute to any additional costs in excess of the original provision it incurs. However the timing and size of this contribution is uncertain and as such a provision has not been made in CISGIL's year end accounts.

CISGIL is party to a Deed of Guarantee with the Trustee for the benefit of the Co-operative Group Pension Scheme (PACE) that, if CFSMS does not pay any amount due in respect of its funding obligations to PACE, CISGIL will pay to PACE its share of the amount due as if it were the principal obligor for such share. As explained in note 9, CISGIL is currently recharged by CFSMS for its share of the pension contributions, including an element of the PACE deficit funding. The directors have no reason to believe that CFSMS will not be able to continue making payments to PACE when due and therefore, at the current time, do not expect any payments to be required under the guarantee.

As a financial services provider, CISGIL is subject to extensive and comprehensive regulation. It must comply with numerous laws and regulations, including the Consumer Credit Act, which significantly affect the way it does business. Whilst CISGIL believes there are no unidentified areas or failures to comply with these laws and regulations which would have a material impact on the financial statements, there can be no guarantee that all issues have been identified. The Financial Conduct Authority (FCA) has recently conducted a thematic review in respect of how insurers sell premium finance alongside insurance products. Once the review findings are published CISGIL will further assess potential implications in light of its consumer credit activity.

26. Commitments

No commitments were in place as at 31 December 2014 (2013: £nil).

27. Parent company

CIS General Insurance Limited, a subsidiary of the Co-operative Banking Group Limited, is incorporated as a Registered society under the Co-operative and Community Benefit Societies Act 2014 and is registered in England and Wales.

The Co-operative Group Limited is the ultimate parent and is incorporated as an Registered society under the Co-operative and Community Benefit Societies Act 2014 and is registered in England and Wales. The results of CIS General Insurance Limited are consolidated in the group headed by the Co-operative Group Limited. The financial statements of the immediate and ultimate holding organisations are available from 1 Angel Square, Manchester, M60 0AG.

All amounts are stated in £m unless otherwise indicated

28. Related party transactions

A number of transactions have been entered into during the course of the year with related parties. These have been conducted in the normal course of business and at arm's length. These include the provision of insurance products to members of the wider Co-operative Group and key management personnel.

	Balances with parent undertaking 2014	**Balances with other related parties 2014**	Balances with parent undertaking 2013	Balances with other related parties 2013
Balances with related parties				
At the beginning of the financial year	**(85.0)**	**(55.8)**	(85.0)	(55.5)
Movement in capital value	**85.0**	**64.0**	-	(0.3)
At the end of the financial year	**-**	**8.2**	(85.0)	(55.8)

In December 2014 capital quality was improved through the issuance of new equity to its immediate parent, the Co-operative Banking Group Limited. Proceeds of the issuance were used to repay existing subordinated debt to its immediate parent. Interest during the financial period amounted to £3.2m (2013: £3.3m).

CISGIL has bank accounts with The Co-operative Bank plc. At the end of 2014, the aggregate balance stood at £1.2m (2013: £0.9m). During the year project costs of £0.7m (2013: £0.7m), included in operating expenses, were charged to CISGIL from The Co-operative Bank plc.

Co-operative Legal Services Limited, a subsidiary of the Co-operative Group Limited, provides legal cover to CISGIL motor and home policyholders. CISGIL has paid £1.8m (2013: £2.7m) in relation to this cover.

CISGIL has an indemnification agreement, accounted for as an intra-group guarantee under IFRS 4, with CFSMS in which CISGIL has agreed to indemnify CFSMS against all and any liability, loss, damage, costs and expense arising from the agreement.

During the year management fees of £132.0m (2013: £163.4m) included in operating expenses and claims handling costs incurred were charged to CISGIL from CFSMS. £nil (2013: £0.1m) was charged for capital utilisation.

Key management (as defined by IAS 24) is considered to include the executive committee members of CISGIL. Details of transactions and balances during the financial period are provided below.

All staff costs are borne by CFSMS and charged out to other companies within the Banking Group at cost.

Key management compensation

	2014	2013
Salaries and short term benefits	**2.1**	1.1
	2.1	1.1

All amounts are stated in £m unless otherwise indicated

29. Fair values of financial assets and liabilities

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the annual report and accounts:

(a) Financial investments at fair value through income or expense

The fair value of financial assets designated at fair value through income or expense, being short term (less than one month) fixed rate deposits, approximates to their nominal amount.

(b) Available for sale assets

Fair value of listed debt securities is based on clean bid prices at the balance sheet date without any deduction for transaction costs.

Available for sale assets are regularly reviewed for impairment. Objective evidence of impairment can include default by a borrower or issuer, indications that a borrower or issuer will enter bankruptcy or the disappearance of an active market for that financial asset because of financial difficulties.

These reviews give particular consideration to evidence of any significant financial difficulty of the issuer or measurable decrease in the estimated cash flows from the investments.

(c) Borrowed funds

Fair value measurement is calculated on a discounted cash flow basis using prevailing market interest rates.

(d) Receivables and payables

For receivables and payables with a remaining life of less than one year, the nominal amount is deemed to reflect the fair value, where the effect of discounting is immaterial.

The table below shows a comparison of the carrying value and fair values of financial instruments .

Financial liabilities	**Carrying value 2014**	**Fair value 2014**	Carrying value 2013	Fair value 2013
Other borrowed funds	**-**	**-**	85.0	85.1

Financial asset and liability classification

The table below analyses financial instruments by measurement basis as detailed by IAS 39 (Financial Instruments: Recognition and Measurement).

Balance sheet categories 2014	**Designated at fair value**	**Loans and receivables**	**Available for sale**	**Other amortised cost**	**Total**
Assets					
Financial assets at fair value through income or expense	**156.3**	**-**	**-**	**-**	**156.3**
Available for sale assets	**-**	**-**	**764.6**	**-**	**764.6**
Other financial assets	**-**	**137.4**	**-**	**-**	**137.4**
Total financial assets	**156.3**	**137.4**	**764.6**	**-**	**1,058.3**
Non-financial assets					**115.7**
Total assets					**1,174.0**
Liabilities					
Overdrafts	**-**	**-**	**-**	**7.9**	**7.9**
Other financial liabilities	**-**	**-**	**-**	**30.4**	**30.4**
Total financial liabilities	**-**	**-**	**-**	**38.3**	**38.3**
Non-financial liabilities					**754.3**
Total liabilities					**792.6**
Capital and reserves					**381.4**
Total liabilities and equity					**1,174.0**

All amounts are stated in £m unless otherwise indicated

29. Fair values of financial assets and liabilities (continued)

Financial asset and liability classification

2013	Designated at fair value	Loans and receivables	Available for sale	Other amortised cost	Total
Assets					
Financial assets at fair value through income or expense	207.6	-	-	-	207.6
Available for sale assets	-	-	763.4	-	763.4
Other financial assets	-	184.0	-	-	184.0
Total financial assets	207.6	184.0	763.4	-	1,155.0
Non-financial assets					116.6
Total assets					1,271.6
Liabilities					
Other borrowed funds	-	-	-	85.0	85.0
Overdrafts	-	-	-	8.9	8.9
Other financial liabilities	-	-	-	17.9	17.9
Total financial liabilities	-	-	-	111.8	111.8
Non-financial liabilities					876.9
Total liabilities					988.7
Capital and reserves					282.9
Total liabilities and equity					1,271.6

The following table provides an analysis of financial assets and liabilities that are valued or disclosed at fair value, by the three level fair value hierarchy as defined within IFRS 7 (Financial Instruments: Disclosure):

- Level 1 - fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 - fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (ie derived from prices).
- Level 3 - fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Based upon guidance issued by The Committee of European Securities Regulators (CESR), CISGIL classifies debt securities in Level 1 only if it can be demonstrated on an individual security by security basis that these are quoted in an active market, ie that the price quotes obtained are representative of actual trades in the market (through obtaining binding quotes or through corroboration to published market prices). Pricing providers cannot guarantee that the prices that they provide are based on actual trades in the market. Therefore all of the corporate bonds are classified as Level 2.

All amounts are stated in £m unless otherwise indicated

29. Fair values of financial assets and liabilities (continued)

Valuation of financial instruments 2014	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Financial assets at fair value through income or expense	**-**	**156.3**	**-**	**156.3**
Available for sale assets	**-**	**764.6**	**-**	**764.6**
Total financial assets at fair value	**-**	**920.9**	**-**	**920.9**

Valuation of financial instruments 2013	Level 1	Level 2	Level 3	Total
Assets				
Financial assets at fair value through income or expense	-	207.6	-	207.6
Available for sale assets	-	763.4	-	763.4
Total financial assets at fair value	-	971.0	-	971.0
Liabilities				
Other borrowed funds	-	85.1	-	85.1
Total financial liabilities at fair value	-	85.1	-	85.1

The valuation techniques using observable inputs relate to debt securities that would otherwise be fair valued using quoted market prices but where there has been short term temporary market inactivity and borrowed funds with no active market price. In obtaining relevant fair values for financial assets, CISGIL has obtained security specific prices from third party market makers based on what the third parties would have traded these particular securities for at the year end date. Financial liabilities have been valued using observable inputs including discounted cash flows and comparable credit spreads.

The following table allows comparison of debt securities (other than those classified at fair value through income or expense) on the basis of the current carrying amount, fair value and amortised cost (pre impairment).

Investments in debt securities as:	**Carrying amount 2014**	**Fair value 2014**	**Amortised cost 2014**
Available for sale financial assets	**764.6**	**764.6**	**747.8**

Investments in debt securities as:	Carrying Amount 2013	Fair value 2013	Amortised cost 2013
Available for sale financial assets	763.4	763.4	772.5

Independent auditor's report

Independent auditor's report to the members of CIS General Insurance Limited

We have audited the annual report and accounts of CIS General Insurance Limited (CISGIL) for the year ended 31 December 2013 set out on pages 10 to 21, in notes E, F, H and I, on pages 25 to 31, and on pages 32 to 51. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU.

This report is made solely to CISGIL's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 as applied to CISGIL and as modified by the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008 and to facilitate compliance with section 496 of the Companies Act 2006. Our audit work has been undertaken so that we might state to CISGIL's members those matters we are required to state to them in an auditor's report and to facilitate compliance by CISGIL's directors with the requirement relating to section 496 of the Companies Act 2006, as applied to CISGIL by Regulation 3 of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than CISGIL and CISGIL'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 8, the directors are responsible for the preparation of the annual report and accounts and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the annual report and accounts 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 annual report and accounts

A description of the scope of an audit of annual report and accounts is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on annual report and accounts

In our opinion the annual report and accounts:

- give a true and fair view of the state of CISGIL's affairs as at 31 December 2013 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the EU, as applied in accordance with the provisions of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, which apply the provisions of chapters 4 and 5 of part 15 of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, which modify and apply the Industrial and Provident Societies Acts 1965 to 2003.

Opinion in order to facilitate compliance by CISGIL's directors with the requirement relating to section 496 of the Companies Act 2006, as applied to CISGIL by Regulation 3 of the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the annual report and accounts are prepared is consistent with the annual report and accounts.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Industrial and Provident Societies Acts 1965 to 2003 require us to report to you if, in our opinion:

- a satisfactory system of control over transactions has not been maintained; or
- 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 annual report and accounts are not in agreement with the books of account; 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.

Karen Orr
Senior Statutory Auditor
for and on behalf of KPMG Audit Plc,
Statutory Auditor
Chartered Accountants
St James Square
Manchester
M2 6DS
16 April 2014

Income statement

For the year ended 31 December 2013

All amounts are stated in £m unless otherwise indicated

	Notes	2013	2012
Income			
Gross earned premiums		**509.0**	610.4
Less premiums ceded to reinsurers		**(32.5)**	(30.8)
Net earned premiums	2	**476.5**	579.6
Fee and commission income	3	**13.3**	10.7
Investment income	4	**27.9**	51.6
Gains less losses arising from financial instruments	5	**13.0**	23.2
Other operating income	6	**0.3**	3.6
Net income		**531.0**	668.7
Claims paid		**(410.0)**	(482.8)
Less amounts receivable from reinsurers		**6.8**	9.9
Net policyholder claims and benefits paid	7	**(403.2)**	(472.9)
Change in insurance contract liabilities	20	**60.2**	(25.0)
Change in reinsurance assets	20	**12.2**	(4.1)
Net policyholder claims and benefits incurred		**(330.8)**	(502.0)
Fee and commission expenses	8	**(19.8)**	(21.7)
Operating expenses	9	**(140.9)**	(132.1)
Financial Services Compensation Scheme levies		**(2.4)**	(1.4)
Finance costs		**(3.5)**	(3.6)
Profit before taxation and significant items		**33.6**	7.9
Significant items	9	**–**	(4.9)
Profit before taxation		**33.6**	3.0
Income tax	10	**(5.9)**	(0.5)
Profit for the financial year		**27.7**	2.5

Profit for the financial year is attributable to the equity shareholder and relates to continuing activities.

2012 significant items relate to expenditure associated with the Banking Group programme of investment and integration.

The accounting policies and notes on pages 15 to 51 form part of these financial statements

Statement of comprehensive income

For the year ended 31 December 2013

All amounts are stated in £m unless otherwise indicated

	Notes	2013	2012
Profit for the financial year		**27.7**	2.5
Changes in available for sale assets:			
Net changes in fair value recognised directly in equity		**(14.2)**	59.7
Net gains transferred from equity to the income statement		**(13.0)**	(22.9)
Income tax	21	**6.3**	(9.0)
Other comprehensive (expense)/income for the financial year, net of income tax		**(20.9)**	27.8
Total comprehensive income for the financial year		**6.8**	30.3

Total comprehensive income for the financial year is attributable to CISGIL's equity holders and relates to continuing activities. All items will be reclassified subsequently to the income statement when assets are sold.

The accounting policies and notes on pages 15 to 51 form part of these financial statements

Balance sheet

At 31 December 2013

All amounts are stated in £m unless otherwise indicated

	Notes	2013	2012
Assets			
Deferred acquisition costs	11	**35.3**	29.9
Reinsurance assets	20	**56.8**	44.8
Financial investments at fair value through income or expense	12	**207.6**	314.0
Available for sale assets	13	**763.4**	773.5
Insurance receivables and other assets	14	**208.5**	224.7
Loans and receivables	15	**–**	50.0
Total assets		**1,271.6**	1,436.9
Capital and reserves attributable to equity holders			
Share capital	17	**183.0**	183.0
Retained earnings	18	**49.9**	22.2
Other reserves	18	**50.0**	70.9
Total equity		**282.9**	276.1
Liabilities			
Insurance contract liabilities	20	**866.3**	1,028.7
Other borrowed funds	19	**85.0**	85.0
Deferred tax liabilities	21	**5.7**	6.4
Current tax liabilities	21	**4.9**	4.0
Other reinsurance liabilities	22	**–**	2.3
Insurance and other payables	23	**17.9**	21.9
Bank overdraft	16	**8.9**	12.5
Total liabilities		**988.7**	1,160.8
Total equity and liabilities		**1,271.6**	1,436.9

Approved by the Board of Directors on 16 April 2014 and signed on its behalf by:

Robert Newton, Chairman
Mark Summerfield, Director
Liz Blackham, Deputy Secretary

The accounting policies and notes on pages 15 to 51 form part of these financial statements

Statement of cash flows

For the year ended 31 December 2013

All amounts are stated in £m unless otherwise indicated

	Notes	2013	2012
Cash flows from operating activities			
Profit before taxation		**33.6**	3.0
Adjustment for:			
Interest payable		**3.5**	3.6
Amortisation of investments		**10.4**	7.0
(Increase)/decrease in deferred acquisition costs		**(5.4)**	3.7
(Increase)/decrease in reinsurance assets		**(12.0)**	5.5
(Increase)/decrease in available for sale assets		**(27.5)**	225.6
Decrease/(increase) in financial investments at fair value through income and expense		**106.4**	(250.4)
Decrease in insurance receivables and other assets		**16.2**	13.0
Decrease in insurance contract liabilities		**(162.4)**	(14.9)
Decrease in derivative financial instruments		**–**	(0.3)
Decrease in other reinsurance liabilities		**(2.3)**	(6.3)
Decrease in insurance and other payables		**(4.0)**	(2.3)
Income tax received	21	**0.6**	12.7
Net cash flows from operating activities		**(42.9)**	(0.1)
Cash flows from investing activities			
Disposal of property, plant and equipment		**–**	39.0
Disposal of investment property		**–**	11.0
Decrease/(Increase) in loans and receivables		**50.0**	(50.0)
Net cash flows from investing activities		**50.0**	–
Cash flows from financing activities			
Interest paid		**(3.5)**	(3.6)
Net cash flows from financing activities		**(3.5)**	(3.6)
Net increase/(decrease) in cash and cash equivalents		**3.6**	(3.7)
Cash and cash equivalents at the beginning of the financial year		**(12.5)**	(8.8)
Cash and cash equivalents at the end of the financial year	16	**(8.9)**	(12.5)

Cash flows from operating activities

CIS General Insurance Limited (CISGIL) classifies the cash flows for the acquisition and disposal of financial assets as operating cash flows. This is because purchases are funded from the cash flows associated with the origination of insurance contracts, net of the cash flows for payments of benefits and claims incurred for insurance contracts, which are classified under operating activities. Additionally, operating cash flows include interest received of £31.4m (2012: £48.0m).

Bank overdrafts are included within cash and cash equivalents in the statement of cash flows.

The accounting policies and notes on pages 15 to 51 form part of these financial statements

Statement of changes in equity

For the year ended 31 December 2013

All amounts are stated in £m unless otherwise indicated

	Share capital	Available for sale reserve	Capital reserve	Retained earnings	Total
2013					
Balance at the beginning of the financial year	**183.0**	**13.8**	**57.1**	**22.2**	**276.1**
Total comprehensive (expense)/income for the financial year	**–**	**(20.9)**	**–**	**27.7**	**6.8**
Balance at the end of the financial year	**183.0**	**(7.1)**	**57.1**	**49.9**	**282.9**
2012					
Balance at the beginning of the financial year	183.0	(14.0)	57.1	19.7	245.8
Total comprehensive income for the financial year	–	27.8	–	2.5	30.3
Balance at the end of the financial year	183.0	13.8	57.1	22.2	276.1

The accounting policies and notes on pages 15 to 51 form part of these financial statements

Basis of preparation and significant accounting policies

For the year ended 31 December 2013

CIS General Insurance Limited (CISGIL) is a co-operative society registered in England under the Industrial and Provident Societies Acts and not a company registered under the Companies Act. The annual report and accounts were authorised for issue by the directors on 16 April 2014.

Statement of compliance

The annual report and accounts have been prepared in accordance with the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 2008, which modified the Industrial and Provident Societies Acts 1965 to 2003. The Regulations require CISGIL to prepare its annual report and accounts substantially as though it were a company registered under the Companies Act 2006 (the Act), and apply, with certain exemptions, the provisions of Parts 15 and 16 of the Act.

Basis of preparation

The annual report and accounts have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), and IFRS Interpretations Committee (IFRIC) guidance, both of which have been adopted by the European Union (EU). The annual report and accounts also follow the provisions of the Revised Statement of Recommended Practice on Accounting for Insurance Business (SORP) issued by the Association of British Insurers in December 2005 (as amended in December 2006) in so far as these are compatible with the requirements of IFRS.

The financial information has been prepared under the historic cost convention as modified by the revaluation of available for sale financial assets, derivative contracts, investment properties and certain other financial assets and financial liabilities held at fair value. CISGIL applies the recognition, measurement and disclosure requirements of IFRS in issue that are endorsed by the EU and are effective for accounting periods beginning on or after 1 January 2013.

Standards and interpretations issued and effective

In preparing these annual report and accounts, CISGIL has adopted the following pronouncements during the year that are new or revised:

- IFRS 13 (Fair Value Measurement (2011))

  This new standard defines fair value and also acts as its single authority, dealing primarily with both its measurement and disclosure. It does not require fair value measurements in addition to those already required, or permitted by other IFRSs, and is not intended to establish valuation standards or affect valuation practices outside of financial reporting. The amendment to IFRS 13 has no material impact on the financial information of CISGIL.

- Amended IAS 1 (Presentation of Items of Other Comprehensive Income)

  This amendment's objective is to split the presentation of other comprehensive income into two sections. The different sections will distinguish between items which may or may not be recycled into any future income or expense. The amendment to IAS 1 has no material impact on the financial information of CISGIL.

- Amendments to IFRS 7 (Disclosures Offsetting Financial Assets and Liabilities)

  This amendment requires disclosures to include information that will enable users of an entity's financial information to evaluate the effect of netting arrangements, on the entity's financial position. The amendment to IFRS 7 has no material impact on the financial information of CISGIL.

- Amendments to IAS 32 (Offsetting Financial Assets and Financial Liabilities)

  The current offsetting model in IAS 32 requires an entity to offset a financial asset and financial liability only when the entity currently has a legally enforceable right of set-off and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. This amendment clarifies the position when offsetting financial assets and financial liabilities. The legal right of set-off must be available today and legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy. The amendment will require more extensive disclosures than are currently required. The disclosures focus on quantitative information about recognised financial instruments that are offset in the balance sheet, as well as those recognised financial instruments that are subject to master netting or similar arrangements irrespective of whether they are offset.

  It becomes effective for accounting periods beginning on or after 1 January 2014. It has been adopted for use within the EU for accounting periods beginning on or after 1 January 2014. The impact of the amendment to IAS 32 is likely to be immaterial to CISGIL.

Other standards and interpretations have been issued but these are not considered to be relevant to CISGIL's operations.

Basis of preparation continued

Going concern

CISGIL's business activities, together with its financial position and the factors likely to affect its future development and performance are set out in the strategic report and the directors' report. In addition, the risk management section on pages 22 to 31 of the annual report and accounts includes CISGIL's objectives, policies and processes for managing its risk, including its exposure to risk. The capital management section on page 32 provides information on CISGIL's capital policies and capital resources. Details of financial instruments are disclosed in note 28.

The assessment of the going concern basis of preparation has been subject to a thorough process involving analysis and discussion by management, the Board Audit Committee and the Board, in line with the governance processes discussed in the risk management sections of these accounts. The analysis covered forecast information for the strategic planning period, stress tests and reverse stress tests, as well as management actions and focused on the profitability, liquidity and capital requirements of CISGIL.

CISGIL delivered a profit for the year of £27.7m. Looking ahead, CISGIL expects to remain profitable.

As can be seen in note 12 on page 37, CISGIL has significant deposits with credit institutions of £207.6m, considerably in excess of the Board's target minimum requirement.

As explained on page 32, there are a number of regulatory capital requirements with which CISGIL must comply. Total regulatory capital was £335.1m at 31 December 2013, which is in excess of all externally imposed capital requirements. The Board also determine a capital requirement over and above the externally imposed measures in line with risk appetite – at the year end the capital position was within risk appetite. Current forecasts show that CISGIL will remain above all regulatory capital requirements for the foreseeable future. CISGIL has also considered a number of stress and reverse stress tests on capital, none of which result in a breach of existing externally imposed capital requirements although some would require management action to remain within the Board's risk appetite. In considering these scenarios management has identified actions that could be taken to improve the capital position.

There are also a number of risks that could affect the future performance and capital position of CISGIL, as a result of the bank separation exercise, notably in respect of the separation activities themselves and the impact on the pension scheme arrangements, over which the directors do not have direct control of all possible mitigating actions.

- Whilst none of the separation costs will be borne by CISGIL, there are operational risks associated with the shared services arrangements in the short term. The separation presents CISGIL with risks around IT, shared assets and service providers. These risks are being actively managed by management and the Board. CISGIL management has utilised the programme team established to lead business separation during the sale process. This team has already given the business a high level of understanding of the requirements for separating CISGIL; and
- As disclosed on page 46, CISGIL has an agreement with CFSMS to pay an appropriate share of the pension contributions relating to staff employed by CFSMS that are assigned to work for CISGIL. As a consequence, CISGIL is exposed to potential future increases in contributions and deficit funding. The scheme was last valued as at 5 April 2013, with revised contribution rates scheduled for June 2014. Management is working closely with the parent company who manage this pension risk. At present CISGIL is not aware of any actions being undertaken by the parent that would have a material adverse impact on CISGIL.

After consideration of the above, and making relevant enquiries of the Group, the directors are satisfied that CISGIL has the resources to continue to meet its liabilities as they fall due and has therefore continued to adopt the going concern basis in preparing the annual report and accounts.

Use of estimates and judgments

The preparation of the annual report and accounts requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the annual report and accounts, are described within the significant accounting policies below, with specific focus on the classification elements of financial instruments (1) and insurance accounting policies (15). Furthermore the valuation of financial instruments is considered a significant judgment as described further in note 28.

Information about estimation uncertainty, that has the most significant effect on the amounts recognised in the annual report and accounts, relates to the determination of the ultimate liability arising from claims made under insurance contracts. Details of the methodology, key assumptions and sensitivities are provided in note 20 (b). Additionally further reference is made within the risk management section in relation to insurance risk on pages 25 and 26.

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these annual report and accounts. The accounting policies are split between non-insurance specific accounting policies and insurance accounting policies. The insurance accounting policies are detailed in accounting policy 15 on pages 20 and 21.

1. Financial instruments (excluding derivatives)

CISGIL classifies its financial assets (excluding derivatives) as either:

- available for sale; or
- financial assets at fair value through income or expense; or
- loans and receivables.

i. Recognition of financial assets and financial liabilities

Financial assets are recognised by CISGIL on the trade date which is the date it commits to purchase the instruments. Loans and receivables are recognised when the funds are advanced.

All other financial instruments are recognised on the date that they are originated.

ii. Derecognition of financial assets and financial liabilities

Financial assets are derecognised when they are qualifying transfers and:

- the rights to receive cash flows from the assets have ceased; or
- CISGIL has transferred substantially all the risks and rewards of ownership of the assets.

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires. When an existing liability is replaced by the same counterparty on substantially different terms or the terms of an existing liability are substantially modified, the original liability is derecognised and a new liability is recognised, with any difference in carrying amounts recognised in the income statement.

iii. Financial assets designated as available for sale

CISGIL classifies the holdings in debt securities as available for sale. Initial measurement is at fair value, being purchase price upon the date on which CISGIL commits to purchase plus directly attributable transaction costs.

Subsequent valuation is at fair value with movements recognised in other comprehensive income as they arise. Where there is evidence of impairment, the extent of any impairment loss is recognised in the income statement. For further information refer to (3(vii)).

On disposal, gains or losses previously recognised in other comprehensive income are transferred to the income statement.

iv. Financial investments at fair value through income or expense

Investments, other than those in debt securities, are designated as financial assets at fair value through income or expense, where they are managed and their performance is evaluated on a fair value basis in accordance with a documented risk management or investment strategy, and information is provided internally to key management personnel on that basis. Initial measurement is at fair value, being purchase price upon the date on which CISGIL commits to purchase. Directly attributable transaction costs are expensed immediately on recognition.

Subsequent valuation is at fair value with changes in fair value being recognised in gains less losses within the income statement in the period in which they arise. On disposal, gains or losses (being proceeds less carrying amount) are recognised in gains less losses arising from financial instruments within the income statement. Where there is no active market or the investments are unlisted, the fair values are based on commonly used valuation techniques.

v. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and CISGIL does not intend to sell immediately or in the near term. For CISGIL this includes insurance premium debt receivables but excludes salvage and subrogation. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently these are measured at amortised cost. The amortised cost is the initial amount at recognition less principal repayments and impairment provisions for incurred losses.

vi. Financial liabilities

Financial liabilities are contractual obligations to deliver cash or other financial assets. Financial liabilities are recognised initially at fair value, net of directly attributable transaction costs. Financial liabilities, other than derivatives, are subsequently measured at amortised cost.

Financial liabilities primarily represent borrowed funds. Borrowings are recognised initially at fair value, which equates to issue proceeds net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Significant accounting policies continued

vii. Impairment of financial assets

Assessment

At the balance sheet date, CISGIL assesses its financial assets not carried at fair value through income or expense for objective evidence that an impairment loss has occurred.

Objective evidence that financial assets are impaired can include default by a borrower or issuer, indications that a borrower or issuer will enter bankruptcy or the disappearance of an active market for that financial asset because of financial difficulties.

Measurement

Any impairment loss on assets carried at amortised cost is recognised immediately through the income statement and a corresponding reduction in the carrying value of the financial asset is recognised through the use of an allowance account.

The amount of the loss is the difference between:

- the asset's carrying amount; and
- the present value of estimated future cash flows (discounted at the asset's original or variable effective interest rate for amortised cost assets or at the current market rate for available for sale assets).

Impairment of financial assets classified as available for sale

Available for sale assets are assessed at each balance sheet date to see whether there is objective evidence of impairment. In such cases, any impairment losses are recognised by transferring the cumulative loss that has been recognised directly in equity to the income statement.

When a subsequent event causes the amount of impaired loss on available for sale investment securities to decrease, and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the income statement. However any further recovery in fair value of an impaired available for sale equity security is recognised directly in equity.

Impairment of financial assets carried at amortised cost

The amount of the impairment loss on assets carried at amortised cost is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

A write off is made when all or part of an asset is deemed uncollectable or forgiven after all the possible collection procedures have been completed and the amount of loss has been determined. Write offs are charged against previously established provisions for impairment or directly to the income statement.

Any additional recoveries from borrowers, counterparties or other third parties made in future periods are offset against the write off charge in the income statement once they are received.

Provisions are released at the point when it is deemed that following a subsequent event the risk of loss has reduced to the extent that a provision is no longer required.

viii. Gains less losses arising from financial assets

Gains less losses arising from financial assets represents unrealised fair value movements of assets held at fair value through income or expense as well as realised gains/losses on available for sale assets.

2. Derivative financial instruments

Derivatives are accounted for as trading instruments. Derivatives are initially recognised at fair value on the date upon which the derivative contract is entered into and are subsequently re-measured at their fair value. Any resultant gain or loss is recognised in the income statement.

Embedded derivatives that are not closely related to their host contracts, and meet the definition of a derivative, are separated and fair valued through the income statement.

CISGIL enters into futures derivative contracts as a means of efficient portfolio management.

3. Sale and repurchase arrangements

CISGIL participates in sale and repurchase (repo) arrangements in connection with its portfolio of government guaranteed securities (gilts). Under these arrangements, CISGIL sells gilts but is contractually obliged to repurchase them at a fixed price on a fixed future date. Securities which are the subject of repo arrangements at the balance sheet date are included in financial instruments at fair value through income or expense in the balance sheet at their bid value and the associated liability is recognised, being the capital amount owing under the repo arrangements.

CISGIL also participates in reverse repo transactions whereby CISGIL buys gilts but is contractually obliged to sell them at a fixed price on a fixed future date. Cash collateral pledged under reverse repo arrangements are classified as deposits with credit institutions within financial investments at fair value through income or expense on the balance sheet as a result of CISGIL's documented risk management policy. CISGIL requires all reverse repo transactions to be fully collateralised in an agreed form for their duration and equivalent collateral is returned at the completion of the loan period. Collateral is required in the form of cash or gilts.

Significant accounting policies continued

4. Cash and cash equivalents

Cash and cash equivalents comprises cash balances and balances with a maturity of three months or less from the acquisition date, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Bank overdrafts that are repayable on demand and form an integral part of CISGIL's cash management are included as a component of cash and cash equivalents for the purpose of the cash flow statement.

5. Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

6. Impairment of non-financial assets

The carrying value of CISGIL's non-financial assets, excluding deferred tax assets, are reviewed at the balance sheet date to determine whether there is any indication of impairment. If impairment is indicated, the asset's recoverable amount (being the greater of fair value less cost to sell and value in use is assessed by reference to discounted future cash flows) is estimated.

An impairment loss is recognised in the income statement to the extent that the carrying value of an asset exceeds its recoverable amount. An impairment loss is reversed if there has been an increase in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent of the asset's carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

7. Provisions

A provision is recognised in the balance sheet if CISGIL has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

8. Revenue recognition

Revenue principally comprises:

Premium income from insurance contracts

CISGIL's accounting policy in respect of revenue arising from insurance contracts is set out within the insurance specific accounting policy (15i) on page 20.

Investment income

Interest income on financial assets designated as available for sale and loans and receivables are recognised within investment income on an effective interest rate (EIR) basis, inclusive of directly attributable incremental transaction costs and fees, and discounts and premiums where appropriate.

The EIR basis spreads the interest income over the expected life of the instrument. The EIR is the rate that, at inception of the instrument, exactly discounts expected future cash payments and receipts through the expected life of the instrument back to the initial carrying amount. When calculating EIR, CISGIL estimates cash flows considering all contractual terms of the instrument (for example prepayment options) but does not consider future credit losses.

Interest income on assets designated as fair value through income or expense is recognised within investment income in the income statement as it accrues on an effective interest basis.

Fee and commission income

Fees and commission receivable mainly relates to sundry fee/commission income from CISGIL's aggregator partner and is earned over the lifetime of the related policy or when services are provided, as deemed appropriate. All other fee and commission income is recognised on an accruals basis.

9. Fee and commission expenses

Fees and commission payable mainly relates to commission payable to broker intermediaries that is incurred over the lifetime of the related policy. All other fee and commission payable is recognised on an accruals basis as the service is provided.

Significant accounting policies continued

10. Income tax

Tax on the income statement for the year comprises current and deferred tax, which is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in the statement of comprehensive income.

Current tax

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax

Deferred tax is provided using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided for is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

11. Foreign currencies

The functional and presentational currency for CISGIL is sterling. All transactions conducted by CISGIL are in sterling. All amounts presented are stated in pound sterling and millions, unless stated otherwise.

12. Significant items

Items which are material by both size and nature (ie outside the normal operating activities of CISGIL) are treated as significant items and disclosed separately on the face of the income statement.

The separate reporting of significant items helps provide an indication of CISGIL's underlying business performance. Events which may give rise to the classification of items as significant include individually significant investment and integration costs.

13. Profit based payments to members of The Co-operative Group

Members of The Co-operative Group may receive a dividend based on their transactions with The Co-operative Group and its subsidiaries, including CISGIL. Once these profit based payments are approved by the Co-operative Group Limited, CISGIL is recharged an amount which reflects its eligible products' contribution to the overall Co-operative Group member dividend. There were no such payments in the year.

14. Dividends

Dividends are only recognised in the annual report and accounts by CISGIL once they have been approved by the shareholders in a general meeting.

15. Insurance accounting policies

Contracts under which CISGIL accepts significant insurance risk from another party (the policyholder), by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary are classified as insurance contracts. A contract that qualifies as insurance remains an insurance contract until all the risks and obligations are extinguished or expire.

All contracts of general insurance business written by CISGIL are classified as insurance contracts. General insurance business is accounted for on an annual basis.

i. Premiums

Gross written premiums comprise premiums receivable on those contracts which incepted during the financial year, irrespective of whether they relate in whole or in part to a later accounting period, together with any necessary adjustments to amounts reported in prior periods.

Gross written premiums:

- are stated gross of commission and exclude any taxes or levies based on premiums; and
- include an estimate of the premiums receivable on those contracts which incepted prior to the year end but which have not been notified by the balance sheet date ('pipeline premium'). When calculating pipeline premiums it is assumed, where appropriate, that options to renew contracts automatically will be exercised.

Gross written premium (whether paid in advance or by instalments) is earned evenly over the period of the contract (usually twelve months). The treatment of outward reinsurance premiums is similar to gross premiums written.

Significant accounting policies continued

ii. Unearned premium provision

For general insurance business, the proportion of written premiums relating to periods of risk beyond the year end is carried forward to future accounting periods. The relevant proportion is calculated using the daily pro rata basis.

Outward reinsurance premiums are treated as earned in accordance with the profile of the reinsured contracts.

iii. Claims incurred

Insurance claims incurred comprise claims paid during the year, together with related handling costs and the change in the gross liability for claims in the period net of related recoveries including salvage and subrogation.

iv. Claims outstanding

Claims outstanding comprises provisions representing the estimated ultimate cost of settling:

- estimates on claims reported by the balance sheet date ('claims reported'); and
- expected additional cost in excess of claims reported for all claims occurring by the balance sheet date ('claims incurred but not reported').

Aggregate claims provisions, which include attributable claims handling expenses, are set at a level such that no adverse run off deviations are envisaged. Adverse run off deviations, which are material in the context of the business as a whole, would be separately disclosed in the notes to the annual report and accounts including the claims development tables.

Anticipated reinsurance recoveries and estimates of salvage and subrogation recoveries are disclosed separately within assets under the headings of 'reinsurance assets' and 'insurance receivables and other assets' respectively.

In accordance with accounting regulations, discounting of outstanding claims is permitted in certain circumstances. For statutory accounts the outstanding reserves are discounted in respect of periodical payments and a portion of liability type claims from the electric industry ('EIROS') for which separate assets are held of appropriate term and nature.

v. Unexpired risk provision

Additional provision is made for unexpired risks where the claims and expenses, likely to arise after the end of the financial year in respect of contracts concluded before that date, are expected to exceed the unearned premiums less deferred acquisition costs carried forward for those contracts.

Unexpired risk provision is calculated for each category of business. Where categories of business are managed together a combined calculation is performed. Surpluses and deficits within each category are offset within the calculation. The provision is determined after taking account of future investment return arising on investments supporting the unearned premium provision and unexpired risk provision.

Such provisions ensure that the carrying amount of unearned premiums provision less related deferred acquisition costs is sufficient to cover the current estimated future cash flows, including claims handling expenses and therefore meets the requirements of the liability adequacy test as set out in IFRS 4 (Insurance Contracts).

vi. Acquisition costs

Costs directly associated with the acquisition of new business, including commission, are capitalised and amortised in accordance with the rate at which the gross written premiums associated with the underlying contract are earned.

vii. Reinsurance

Contracts with reinsurers that give rise to a significant transfer of insurance risk are accounted for as reinsurance contracts. Amounts recoverable under such contracts are recognised in the same period as the related claim. Premiums, claims and receivables are presented on a gross basis in the income statement and balance sheet.

Amounts recoverable under reinsurance contracts are assessed for impairment at each balance sheet date. If objective evidence of impairment exists, reinsurance assets are reduced to the level at which they are considered to be recoverable and an impairment loss is recognised in the income statement.

Risk management

For the year ended 31 December 2013

All amounts are stated in £m unless otherwise indicated

CIS General Insurance Limited (CISGIL) issues contracts that transfer insurance risk and is exposed to financial risk through its holdings of financial assets and liabilities. This section summarises these risks and the way CISGIL manages them.

Developments during 2013

Prior to 2013 CISGIL's risk management framework was integrated with The Co-operative Banking Group Limited (the Banking Group). During 2013 CISGIL established its own risk management framework appropriate to a stand-alone general insurer. As a result, over the course of 2013 CISGIL:

- revised its risk classification and established a comprehensive risk register;
- revised its risk appetite and limits;
- established its own suite of risk policies and control standards;
- created a stand-alone 2nd Line Risk function; and
- revised and enhanced its governance structure and delegated authority framework.

The following section summarises the risk management structure that was in place at the end of 2013.

Our approach to risk management

CISGIL operates a three lines of defence governance model to ensure appropriate responsibility and accountability is allocated to the management, reporting and escalation of risks.

Business management is the first line of defence. It is responsible for implementing and operating processes to identify, measure, manage, monitor and report risks. This includes those risks deriving from the development of new products, processes or other business change. It manages the risks that reside within the business areas on a day-to-day basis and implements effective monitoring and control processes to ensure that the business risk profile is understood and maintained within Board defined risk appetite.

The Chief Risk Officer and 2nd Line Risk function are the second line of defence. They own the risk management framework, oversee and challenge its implementation and operation by the first line of defence, and consider current and emerging risks across CISGIL. They also provide review and challenge of the delegated authority framework and oversee appropriate escalation of breaches, mitigating actions and reporting to the Executive Risk Committee and Board.

Internal audit act as the third line of defence. They independently challenge the overall management of the framework and provide assurance to the Board Audit Committee and senior management on the adequacy of both the first and second lines. The Chair of the Board Audit Committee oversees the internal audit function and risk-based audit plan. CISGIL has contracts in place with external consultants to provide internal audit capability.

Risk management structure

The Board is responsible for approving the general insurance strategy, its principal markets and the level of acceptable risks articulated through its statement of risk appetite. It is also responsible for overall corporate governance which includes ensuring that there is an adequate system of risk management in place.

CISGIL has developed and implemented a governance and organisation structure, which supports the Board. The Board has established risk and audit sub-committees, and senior management committees, to:

- oversee the risk management process;
- identify the key risks facing the business; and
- assess the effectiveness of planned management actions.

Specific Board authority has been delegated to the Board sub-committees and the Managing Director, Co-operative Banking Group who may, in turn, delegate elements of these discretions to appropriate members of the senior management team.

Risk management committees

The CIS General Insurance Board (Board)

The responsibilities of the Board include:

- setting the overall Risk Strategy;
- approving the design and implementation of risk management approaches, including the Risk Management Framework Policy and the Risk Appetite Statements and metrics that underpin them;
- delegating authority for oversight of the risk management framework, systems and high-level limits to the Board Risk Committee;
- delegating authority for cascading the setting and approval of the more granular risk limits and tolerances to the Managing Director, Co-operative Banking Group;
- using the output of the semi-annual certification process, to approve the effectiveness of the Risk Management Framework with support from internal audit through their risk-based review programme; and
- reviewing and challenging Board Risk Committee reports on the effectiveness of the risk management framework and systems.

Risk management committees continued

CISGIL Board Risk Committee (BRC)

BRC responsibilities include:

- providing oversight and advice to the Board on current and potential risks and the overall risk framework including risk appetite, risk tolerance and risk management strategies;
- reviewing and challenging the design of the Risk Management Framework, Risk Appetite limits and tolerances and recommending to the Board for approval;
- reviewing and challenging the implementation of the Risk Management Framework through the semi-annual certification process and reviewing the quality and effectiveness of the Risk Management Framework, systems and function;
- reviewing and challenging internal controls and process of risk management including the coverage of the risk taxonomy;
- monitoring the organisation's performance and compliance against high-level risk appetite limits and tolerances;
- in co-operation with the Board Audit Committee, monitoring identified risk control failings and weaknesses and management actions taken to resolve them; and
- reporting on the effectiveness of the Risk Management Framework and systems to the Board.

CISGIL Board Audit Committee (BAC)

BAC responsibilities include:

- review and oversight of financial statements and annual reports before submission to the Board;
- assisting the Board in carrying out its responsibilities relating to internal control, including control breaches and remediation;
- exercising oversight of identified risk control framework failings and weaknesses as well as management actions taken to resolve them; and
- oversight of internal and external assurance and audit.

CISGIL Executive Committee (ExCo)

The ExCo responsibilities include:

- overseeing the establishment and maintenance of appropriate risk management systems and controls in line with the Board agreed Risk Management Framework;
- supporting the Managing Director, Co-operative Banking Group in developing, reviewing and approving detailed risk appetite limits and tolerances as delegated by the Board;
- ensuring the implementation of the risk strategy set by the Board so as to deliver an effective risk management environment for CISGIL.

CISGIL Executive Audit Committee (EAC)

The EAC responsibilities include ensuring the timely issue resolution and decision making governance on the results of audits relating to CISGIL from regulators, external auditors and internal audit.

CISGIL Executive Risk Committee (ERC)

The ERC responsibilities include:

- driving the detailed implementation of the CISGIL Risk Management Framework approved by the Board;
- providing a mechanism for ensuring that the CISGIL-wide risk and capital management requirements, developments, and processes are in place;
- supporting the Managing Director, Co-operative Banking Group in developing the Risk Strategy, Risk Management Framework, and Risk Appetite Statement and recommending to the Board Risk Committee for review, challenge and recommendation to the Board for approval;
- supporting the Managing Director, Co-operative Banking Group in approving risk policies, proposing risk appetite limits and tolerances to the Board Risk Committee for review, challenge and recommendation to the Board for approval;
- reviewing approaches to stress testing, risk management reporting and governance, and referring them to the Board Risk Committee for review, challenge and recommendation for approval by the Board;
- supporting the Managing Director, Co-operative Banking Group in semi-annually reviewing the effectiveness of the Risk Management Framework, systems and function and providing a report to the Board Risk Committee;
- on a periodic basis, assessing the performance of the Risk Management Framework; and
- monitoring the business's risk profile against the agreed limits and tolerances and reporting on these to the Board Risk Committee.

Senior Management Committees

CISGIL has other committees that advise and support the Managing Director, Co-operative Banking Group and members of the senior management team in carrying out their responsibilities.

Remuneration Committee

Remuneration is authorised by a combined committee covering CISGIL and other Banking Group entities.

All amounts are stated in £m unless otherwise indicated

Principal risks

The following are considered to be the principal risks facing CISGIL:

	Risk Type	Definition	Page
A	**Strategic and business risks***	The risk to earnings and capital that may arise as a result of strategic/management decisions or business choices or lack of responsiveness to changes in the business environment	24
B	**Reputation risk***	The risk associated with an issue which could in some way be damaging to the brand of the organisation among all or any stakeholders	24
C	**Conduct risk***	The risk that CISGIL's behaviours, offerings or interactions will result in unfair outcomes for customers	24
D	**Regulatory risk***	The risk of fines, public censure, limitation on business, or restitution costs arising from failing to understand, interpret, implement and comply with UK and EU regulatory requirements	25
E	**Insurance risk**	The inherent uncertainties as to the occurrence, amount and timing of insurance liabilities	25
F	**Market risk**	The risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers e.g. interest rates, market prices of assets and liabilities	26
G	**Operational risk***	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events	28
H	**Liquidity risk**	The current and prospective risk to earnings or capital arising from CISGIL's inability to meet its obligations when they come due without incurring unacceptable losses	28
I	**Credit risk**	The risk to earnings and capital arising from a counterparty's failure to meet their legal and contractual obligations	30
J	**Pension risk***	The risk to capital and company funds from exposure to scheme liabilities (to the extent liabilities are not met by scheme assets) and risks inherent in the valuation of scheme liabilities and assets	31

Risks marked with an asterisk (*) above are termed unaudited as they are outside the scope of the external audit.

For each of the principal risks, CISGIL Board has approved risk policies and risk appetite statements with underpinning metrics. The metrics have approved limits within which business operations are to be conducted, along with thresholds to give early warning of emerging issues.

CISGIL is exposed to Group risks as a result of being part of The Co-operative Group (the Group). CISGIL does not classify Group risks as a risk-type and instead captures them within other risk-types. In particular, strategic and business risks include impacts of the Group's strategy upon CISGIL, reputation risk includes impacts of reputational issues arising elsewhere in the Group, operational risk includes risks from services shared with other parts of the Group and pension risk includes risks with CISGIL's contributions to the Group pension scheme.

A) Strategic and business risks (unaudited)

Strategic and business risks to earnings and capital arise as a result of strategic/management decisions or business choices or lack of responsiveness to changes in the business environment. Specific strategic and business risks, and management actions, are regularly reported and reviewed by the ERC and the Board. CISGIL's objective in managing these risks is to maintain a sufficient capital buffer in excess of minimum regulatory capital requirements to cover projected risks and maintain market confidence, and obtain a sufficient, stable and sustainable return on equity. The Board have defined detailed metrics and limits underpinning these objectives, which are measured, monitored and reported regularly to the ERC and the Board.

B) Reputation risk (unaudited)

Reputation risk is defined as the risk associated with an issue which could in some way be damaging to the brand of CISGIL either through its strategic decisions, business performance, an operational failure or external perception. CISGIL's objective is to maintain a strong reputation in line with our values and principles through robust operational standards, continual monitoring of our corporate reputation and brand, commitment to our Social Goals Strategy and proactive public relations.

As part of the assessment and control of this risk, our business performance and risk profile across all of our risk themes are closely monitored and reviewed. CISGIL proactively monitors and manages media, public and customer opinion and works closely with external rating agencies to ensure fair and balanced representation. This approach helps maintain member, customer and market confidence. This risk is regularly monitored and reported to the Conduct and Operational Risk Committee, ERC and the Board.

Reputational issues with the Banking Group during 2013 have impacted upon the reputation of CISGIL.

C) Conduct risk (unaudited)

Conduct risk is the risk that CISGIL's behaviours, offerings or interactions will result in unfair outcomes for customers. Accordingly, conduct risk may arise from any aspect of the way a business is conducted, the sole test being whether the outcome is an unfair one for customers. Conduct risk is a key area of focus across the financial services industry, with increasing scrutiny from the Financial Conduct Authority. CISGIL's objective is to ensure our conduct and treatment of customers and the quality of our customer experience is maintained through the application of systems and controls in conjunction with ongoing oversight and monitoring from risk functions.

CISGIL mitigates and prevents emerging conduct risk through established systems and controls including ongoing oversight and monitoring from risk functions. A full review of all products was completed in 2013, and a rigorous assessment is carried out for all new products and changes. Conduct risks are reported through management structures and regularly monitored and reported to the Conduct and Operational Risk Committee, ERC and the Board.

Principal risks continued

D) Regulatory risk (unaudited)

Regulatory risk is the risk of fines, public censure, limitation on business, or restitution costs arising from failing to understand, interpret, implement and comply with UK and EU regulatory requirements. CISGIL's objective is to maintain a robust process to ensure that all regulatory expectations and requirements are met within agreed or mandated timeframes, by promoting and embedding a compliance culture and developing positive regulatory relationships.

Regulatory risks are reported through management structures and regularly monitored and reported to the Conduct and Operational Risk Committee, ERC and the Board.

E) Insurance risk

Insurance risk comprises risks that arise in respect of claims that have already occurred and for which reserves are already held (reserving risk) and of claims that are yet to occur (underwriting risk). Underwriting risk includes risks from claims arising from natural or man-made catastrophe events.

The major classes of general insurance business written are motor and property, together with some commercial liability, pecuniary loss, pet insurance and personal accident. CISGIL underwrites motor and home personal lines business written directly or through brokers, and therefore bears the insurance risk on these policies. Most commercial business is underwritten by Aviva with CISGIL receiving commission and not bearing the insurance risk. A small number of commercial accounts are underwritten by CISGIL and 100% reinsured with Aviva, due to which CISGIL bears the ultimate insurance risk although the risk of Aviva failing to meet its commitments is minimal. CISGIL bears the insurance risk for pet insurance written historically but new pet business is underwritten by Allianz. Almost all general insurance policies are written in the UK market covering risks over a 12 month duration.

Motor cover is principally in respect of private vehicles and commercial vehicles, with limited fleet business. CISGIL underwrites and bears the insurance risk for private vehicles. Commercial vehicle cover generally refers to small businesses with a single vehicle. This has been underwritten by CISGIL historically but is currently in the process of being migrated to an external broker Bollington, who are placing the policies with other insurers. Fleet motor cover is underwritten by Aviva. Principal risks under motor policies where CISGIL bears the insurance risks are bodily injury to third parties, accidental damage to property including policyholders' and third parties' vehicles, and theft of or from policyholders' vehicles. The most significant factors affecting the frequency and severity of motor claims are judicial, legislative and inflationary changes and the frequency and severity of large bodily injury claims.

Property cover is primarily residential household, which is underwritten by CISGIL, with commercial property business being 100% reinsured with Aviva. Principal risks under property policies where CISGIL bears the insurance risks are damage from storm and flood, fire, escape of water and subsidence and theft of or accidental damage to contents.

CISGIL has entered into an indemnification agreement with Royal London (CIS) Limited, formerly Co-operative Insurance Society Limited (CISL), now a subsidiary of Royal London Group, to assume financial responsibility for the run off of general insurance business formerly written by CISL. In return, CISGIL received a premium in 2006, settled by transfer of assets, equivalent to the net technical liabilities of this business included in CISL's annual report and accounts at 2005 year end. This exposes CISGIL to the risk of these assets being insufficient to cover the claims arising from this business, although this risk is diminishing over time. A Part VII transfer from CISL to CISGIL of this business in run off took place on 31 March 2014. This transfer will not affect how CISGIL manages the risks in its business.

Objectives and strategy

CISGIL's objectives in managing general insurance risk are:

- to achieve acceptable returns by ensuring that insurance risks are carefully selected in accordance with risk appetite, underwritten in accordance with risk strategy and priced to reflect the underlying risk;
- reserve risk volatility is minimised through robust reserving and modelling approaches; and
- catastrophe risk is mitigated through the use of appropriate reinsurance arrangements.

Insurance risk is managed through the underwriting strategy, reinsurance arrangements, proactive claims handling and the claims provisioning process. The objective of the underwriting strategy is to ensure that the underwritten risks are diversified in terms of type and amount of risk, industry/demographic profile and geography, and only those risks which conform with underwriting criteria are accepted. Exposure mix and the frequency and average costs of claims are monitored throughout the year and, where significant deviations from expectation are identified, remedial action is taken. A programme of reinsurance is in place which is determined in accordance with the risk appetite of the business as further described below.

The overriding objective in claims handling is to ensure that claims are properly scrutinised and paid where they fall within the terms and conditions of the policy. The proper scrutiny of claims is facilitated by the use of various technical aids such as weather validation and fraud databases, and the use of claims specialists. The basis for assessing claims provisions is set out in note 20.

The nature of insurance contracts is that the obligations of the insurer are uncertain as to the timing or quantum of liabilities arising from contracts. CISGIL takes all reasonable steps to ensure that it has information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established. CISGIL manage this risk through the Reserving Committee which formally reviews claims reserves on a quarterly basis.

Principal risks continued

Reinsurance

Part of the CISGIL insurance risk strategy includes a reinsurance programme to reduce its losses to large exposures. There are two major reinsurance programmes in place;

- catastrophe excess of loss cover to restrict losses from a single weather event such as flood or storm; and
- individual excess of loss cover to restrict losses from individual large claims, particularly large bodily injury claims on the motor book.

The appropriate level of reinsurance is determined by management and approved by the Board. Management relies on outputs from CISGIL's capital model. The choice of reinsurance optimises the risk/reward trade off and ensures an objective, risk-based approach to decision making which makes efficient use of capital.

F) Market risk

Market risk is the risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers such as interest rates and market prices of assets and liabilities.

CISGIL invests primarily in high-quality fixed and variable interest bonds issued by corporations ('corporate bonds') and in short-term sterling deposits with financial institutions ('cash'). The value of, or income from, assets held is subject to volatility from changes in both market interest-rates and additional spreads related to the specific credit-worthiness of the issuer ('credit-spreads'). Proceeds from maturing investments are also subject to risk over the future return on reinvestment.

CISGIL is also exposed to market interest-rates through:

- the discounted present value placed upon future claims. All future claims are discounted for economic assessment purposes including the Individual Capital Assessment (ICA). However, IFRS short term insurance reserves (normally less than five years) are not directly affected by market interest-rates as they are undiscounted; and
- £65.0m of issued subordinated debt, from a total of £85.0m, which pays interest at varying margins above three month LIBOR. The remaining £20.0m pays a fixed coupon of 10% per annum.

CISGIL writes contracts of insurance in the United Kingdom and insurance liabilities and borrowings are denominated in sterling. Funds are invested solely in assets denominated in sterling and consequently there is no direct exposure to currency risk.

In summary, the principal market risks that CISGIL is exposed to are:

- changes in interest-rates, which impact both asset and liability values, and investment income;
- movements in credit-spreads which impact the market value of corporate bonds; and
- default or delay in payments due upon corporate bonds or cash.

Objective and strategy

CISGIL's objective is to achieve acceptable returns through the use of highly rated government and corporate bonds while minimising volatility through minimal exposure to equities and other volatile instruments. To enhance certainty over the investment return generated from these assets, management practice is generally to maintain holdings to maturity.

CISGIL determines its strategic asset allocation through considering the risk/reward trade off and the impact upon capital adequacy and solvency of the overall company, which relies on outputs from CISGIL's capital model. CISGIL's investments are managed by Royal London Asset Management (CIS) Limited (RLAM) with whom CISGIL have an agreed investment mandate with limits for exposure by credit-rating, maximum terms and maximum exposure to individual counterparties. The Investment Committee oversees RLAM, monitoring and managing asset exposures against the strategic asset allocation and approved limits.

CISGIL manages credit-spread and default risks from corporate bonds through the limits for exposure to credit-ratings and individual counterparties. Other risk mitigation techniques employed to manage exposure to counterparty default include transacting only through a diversified range of authorised counterparties and the requirement for certain transactions (including cash, investment and trading in futures, stock lending and gilt repo transactions) to be fully collateralised on a daily basis. The Investment Committee oversees the monitoring and management of these risks and exposures against limits.

Interest-rate risk is managed through investing in fixed interest securities with a similar duration profile to the liabilities under the general insurance contracts. CISGIL matches cash flows of assets and liabilities in this portfolio by estimating their mean duration. The mean duration of liabilities is calculated using historical claims data to determine the expected settlement pattern for claims arising from insurance contracts in force at the balance sheet date (both incurred claims and future claims arising from the unexpired risks at the balance sheet date). Index-linked investments and other specific debt securities are used to match periodical payment liabilities and provisions relating to asbestos exposure within the electric industry ('EIROS' claims) by amount and duration. In order to do this, an expert opinion on life expectancy is used along with an expectation of long term average earnings.

Principal risks continued

Mean durations are:

	2013	2012
Insurance liabilities	**3.20 years**	2.99 years
Financial assets	**2.53 years**	1.99 years

	Amount (£m)	**Duration**
Periodical payments		
Insurance liabilities	**38.6**	**17.0 years**
Financial assets	**40.9**	**16.1 years**
EIROS claims		
Insurance liabilities	**2.4**	**10.4 years**
Financial assets	**2.6**	**13.7 years**

Sensitivity analysis

The most significant aspect of market risk to which CISGIL is exposed is changes in credit-spreads upon corporate bonds. The resulting movements in the market values of corporate bonds directly affect CISGIL's internal economic assessment of solvency, including the Individual Capital Assessment (ICA). As CISGIL has adopted a policy of recognising most investment assets on an 'available for sale' basis, movements in market values of these assets are recognised in other comprehensive income and so have limited impact upon reported IFRS profits.

An increase of 100 basis points in credit-spreads would reduce the carrying value of CISGIL's assets at the end of the financial year by £17.9m (2012: £20.6m). This would reduce the value placed upon these assets in CISGIL's internal economic assessment of solvency, including the ICA, by the same amount. On an IFRS basis it would result in a reduction in other comprehensive income of £13.7m net of tax (2012: £15.6m). The impact of a decrease of 100 basis points in credit-spreads would have similar but opposite effects.

The method used for this calculation increases the implied redemption yield by 100 basis points and uses this modified yield to calculate the revised market value of each bond in the portfolio. The calculation assumes that a change in credit-spreads would have an immediate and equal impact at all points on the yield curve and upon all corporate bonds regardless of their credit-rating. The probability of this credit-spread change over one year is assessed as 24% (2012: 19%) using the CISGIL capital model.

CISGIL has £65.0m (2012: £65.0m) of issued subordinated debt at varying margins above three month LIBOR. The effect on profit of a 100 basis point movement in three month LIBOR would be £0.5m per annum net of tax (2012: £0.5m). Additionally, CISGIL has a further £20.0m of subordinated debt with a fixed coupon of 10% which is not sensitive to a change in LIBOR.

All amounts are stated in £m unless otherwise indicated

Principal risks continued

G) Operational risk (unaudited)

Operational risk includes internal and external fraud, loss or theft of confidential customer information, loss of key personnel, system capacity issues or programme failure and external events over which CISGIL has limited controls, such as terrorist attack. CISGIL's objective is to minimise operational risk through the implementation of a robust control environment which minimises the potential for loss as a result of the failure of processes, people, technology and due to external events.

CISGIL has defined the following sub-categories within operational risk, which represent the major areas of operational risk exposure. Each sub-category has its own policy, approved by the ERC, supported by underlying control standards:

- financial reporting risk;
- model risk;
- technology risk;
- physical assets and security;
- third party supplier risk;
- change risk;
- product approval risk;
- information risk;
- financial crime risk;
- people risk;
- legal risk;
- business continuity planning; and
- anti-money laundering and counter terrorist financing.

Operational risks are identified, managed and mitigated through ongoing risk management practices including risk assessments, formal control procedures and contingency planning. Operational risks and key controls are regularly reviewed by the Conduct and Operational Risk Committee. Significant operational risks are reported to the ERC and the Board.

A programme is underway to separate CISGIL's IT from an infrastructure that is currently shared with other companies in the Banking Group, the Co-operative Bank (the Bank) and Royal London Group. Business continuity arrangements will continue to be reviewed and refreshed to take account of the changes in external environment and operating model due to the Bank separation.

CISGIL has a corporate insurance programme to transfer specific risks to insurers as part of its risk management approach.

H) Liquidity risk

Liquidity risk is the current and prospective risk to earnings or capital arising from an inability to meet obligations when they come due without incurring unacceptable losses. CISGIL's objective is to meet all funding obligations as they fall due primarily through the use of highly liquid investment instruments.

The Board's risk appetite is that liquid assets should be at least equal to 20% of the ultimate cost of a 1-in-100 year windstorm loss before reinsurance recoveries. The ultimate cost is calculated based upon the catastrophe component of CISGIL's capital model. The latest model assesses the ultimate cost of a 1-in-100 year windstorm as £147.0m (2012: £158.0m), giving a minimum requirement for £29.4m (2012: £31.6m) of liquid assets against actual liquid assets of £763.6m (2012: £773.0m).

Liquid assets are considered to be:

Asset type		Value included as liquid assets
Gilts		100%
Cash		100%
Corporate bonds:	AAA	80%
	AA	70%
	A	60%
	BBB	50%
Al other investments		0%

All amounts are stated in £m unless otherwise indicated

Principal risks continued

The level of cash and other assets held are monitored regularly and managed through the Investment Committee, with oversight by the ERC and the Board. This includes monthly reporting of liquid assets against risk appetite limits.

In addition, CISGIL has access to overnight borrowing facilities with the Bank. Overnight borrowings are subject to the Bank's regulatory exposure limits for related counterparties. These borrowings are on normal commercial terms and represent an unsecured, uncollateralised obligation of CISGIL.

The following table indicates the time profile of undiscounted cash flows arising from financial liabilities (based upon contractual maturity), and the discounted cash flows arising from insurance liabilities (based upon estimated timing of amounts recognised in the balance sheet). Included in the analysis on insurance contract liabilities below is £40.0m (2012: £35.8m) of discounted reserves relating to PPO and EIROS. Further details are included in note 20.

	Carrying value	Gross nominal out flow	Up to 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	More than 5 years
As at 31 December 2013								
Insurance contract liabilities	**866.3**	**866.3**	**470.2**	**132.2**	**66.3**	**42.0**	**26.5**	**129.1**
Financial liabilities at amortised cost:								
Subordinated debt	**85.0**	**92.3**	**33.0**	**2.5**	**2.5**	**54.3**	**–**	**–**
Insurance and other payables	**17.9**	**17.9**	**17.9**	**–**	**–**	**–**	**–**	**–**
Cash and cash equivalents	**8.9**	**8.9**	**8.9**	**–**	**–**	**–**	**–**	**–**
	978.1	**985.4**	**530.0**	**134.7**	**68.8**	**96.3**	**26.5**	**129.1**
Other liabilities	**10.6**							
Total recognised liabilities	**988.7**							

	Carrying value	Gross nominal out flow	Up to 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	More than 5 years
As at 31 December 2012								
Insurance contract liabilities	1,028.7	1,028.7	560.1	132.9	86.5	54.0	43.0	152.2
Financial liabilities at amortised cost:								
Subordinated debt	85.0	94.9	33.0	2.5	2.5	56.9	–	–
Other reinsurance liabilities	2.3	2.3	2.3	–	–	–	–	–
Insurance and other payables	21.9	21.9	21.9	–	–	–	–	–
Cash and cash equivalents	12.5	12.5	12.5	–	–	–	–	–
	1,150.4	1,160.3	629.8	135.4	89.0	110.9	43.0	152.2
Other liabilities	10.4							
Total recognised liabilities	1,160.8							

All amounts are stated in £m unless otherwise indicated

Principal risks continued

I) Credit risk

Credit risk is the risk to earnings and capital arising from a debtor's failure to meet their legal and contractual obligations. CISGIL does not aim to earn a return from credit risk hence its appetite for credit risk is very low. Potential losses arising from credit risk are minimised by the use of high quality reinsurers and highly rated investments.

CISGIL's principal credit risk exposures are as follows:

- default upon cash, being deposits with approved financial institutions;
- movements in credit-spreads which impact the market value of corporate bonds, and default or delay in payments due upon corporate bonds or cash;
- reinsurance counterparties failing to meet financial obligations or entering into restructuring arrangements that may adversely affect reinsurance recoveries;
- default or delay in repayment upon loans and receivables; and
- default or delay in repayment of insurance receivables and other assets.

CISGIL manages credit risks associated with cash and corporate bonds as part of market risk. See market risk section above for details.

Where reinsurance is used to manage insurance risk, there is a risk that the reinsurer fails to meet its obligations in the event of a claim. CISGIL places limits over exposure to a single reinsurance counterparty, or counterparty group, based upon their credit-worthiness. These limits apply when reinsurance is initially placed, usually annually, and then regularly monitored and managed by the Investment Committee. Where concern exists over reinsurer credit quality, watch lists are maintained and actively managed.

Loans and receivables of £50.0m were repaid from the Co-operative Group Limited during 2013.

Insurance receivable and other assets are primarily premium debtors, with an element of salvage and subrogation recoveries and some accrued interest.

At the balance sheet date there were no significant concentrations of credit risk. The table below provides an analysis at the balance sheet date of the credit rating of those assets subject to credit risk, and excludes any assets that were classed as impaired at that date. CISGIL's policy for making provisions for possible impairment is described within the accounting policy section on page 19. Credit ratings are determined by taking an average of ratings provided by Moody's Investors Service, Standard & Poor's and Fitch.

As at 31 December 2013	AAA	AA	A	BBB and below	Not rated	Total
Financial assets at fair value through income or expense:						
Deposits with approved credit institutions (fixed rate)	**–**	**–**	**207.6**	**–**	**–**	**207.6**
Available for sale assets:						
Listed debt (fixed rate)	**73.3**	**179.4**	**429.6**	**37.7**	**–**	**720.0**
Listed debt (variable rate)	**–**	**–**	**31.9**	**11.5**	**–**	**43.4**
Reinsurance assets	**–**	**25.0**	**28.9**	**–**	**2.9**	**56.8**
Insurance receivables and other assets	**1.1**	**1.6**	**7.8**	**0.4**	**197.6**	**208.5**
	74.4	**206.0**	**705.8**	**49.6**	**200.5**	**1,236.3**
Assets not subject to credit risk						**35.3**
						1,271.6

As at 31 December 2012	AAA	AA	A	BBB and below	Not rated	Total
Financial assets at fair value through income or expense:						
Deposits with approved credit institutions (fixed rate)	–	–	314.0	–	–	314.0
Available for sale assets:						
Listed debt (fixed rate)	27.8	76.8	494.5	110.5	26.9	736.5
Listed debt (variable rate)	–	–	33.5	3.5	–	37.0
Loans and receivables at amortised cost	–	–	–	–	50.0	50.0
Reinsurance assets	–	15.6	21.9	–	7.3	44.8
Insurance receivables and other assets	0.2	1.9	8.9	2.9	210.8	224.7
	28.0	94.3	872.8	116.9	295.0	1,407.0
Assets not subject to credit risk						29.9
						1,436.9

All amounts are stated in £m unless otherwise indicated

Principal risks continued

The maximum exposure to credit risk, before making allowance for collateral held, is represented by the carrying value of each financial asset in the table. Collateral of £178.8m (2012: £ 281.8m) is held as security against a reverse repo with balance of £180.0m as at 31 December 2013 (2012: £275.0m). Cash collateral pledged sits within deposits with approved credit institutions within financial investments at fair value through income or expense on the balance sheet as a result of CISGIL's documented risk management policy.

Eurozone risk

CISGIL has no direct exposure to the sovereign debt of European countries. There is currently limited detailed knowledge of indirect exposure to European sovereign debt. Indirect exposure is managed as knowledge of an institution's direct exposure is made public. At this point, if the exposure is considered to be in excess of the risk appetite, action will be taken to reduce the risk through the sale of the relevant holdings. Indirect exposure to European countries is also considered as part of the reinsurance placement. The asset profile of the prospective companies is analysed and those which are over exposed are not included in placement of the programme.

The table below shows exposure to European countries arising from corporate bonds. CISGIL has no exposures to European countries as a result of repo arrangements.

As at 31 December 2013	Up to 1 year	1 to 5 years	5 to 10 years	Total
France	–	**7.2**	–	**7.2**
Germany	–	**43.0**	**28.3**	**71.3**
Netherlands	–	**9.4**	–	**9.4**
Spain	–	**29.3**	–	**29.3**
Sweden	–	**29.9**	**34.4**	**64.3**
Switzerland	–	–	–	–
	–	**118.8**	**62.7**	**181.5**

As at 31 December 2012	Up to 1 year	1 to 5 years	5 to 10 years	Total
France	–	7.3	25.7	33.0
Germany	–	–	8.1	8.1
Norway	–	10.8	–	10.8
Spain	19.4	5.9	–	25.3
Sweden	–	60.0	12.9	72.9
Switzerland	–	7.3	–	7.3
	19.4	91.3	46.7	157.4

J) Pension risk (unaudited)

Pension risk is defined as the risk to capital and company funds from exposure to scheme liabilities and risks inherent in the valuation of scheme liabilities and assets.

CISGIL has an agreement to pay pension contributions relating to staff employed by CFS Management Services Limited (CFSMS) that are assigned to work for CISGIL. This means that CISGIL is exposed to pension risk through The Co-operative Group pension scheme (PACE). The PACE trustee, in consultation with The Co-operative Group, is responsible for the risk management arrangements for PACE, agreeing suitable contribution rates, investment strategy and for taking professional advice as appropriate. The scheme is managed at The Co-operative Group level.

CISGIL is exposed to potential future increases in required contributions and capital set aside for pension risk. The impact of any potential changes to contributions is assessed under CISGIL's risk management framework and internal economic assessment of solvency, including the ICA. CISGIL actively engages with The Co-operative Group with the aim that the volatility in the pension funding position is appropriately managed through continuous monitoring, adjustments to scheme contributions, engagement of external advisors and review of investment and pension strategies.

Capital management

For the year ended 31 December 2013

All amounts are stated in £m unless otherwise indicated

Objectives when managing capital

For regulatory solvency capital purposes, CISGIL defines capital as share capital and reserves (after regulatory capital deductions and equalisation provisions) plus subordinated debt. The strategy in respect of capital management is to ensure that the following objectives are met:

- it has sufficient capital to meet all regulatory requirements;
- it has sufficient capital to support all the risks in the business, over the internally agreed time horizon and to the internally agreed level of confidence, in order to protect policyholders and meet the Board's risk appetite; and
- subject to the above objectives being met, it makes the required post tax return on equity.

Required capital

CISGIL is required to hold regulatory capital for its general insurance business in compliance with the rules issued by the Prudential Regulation Authority (PRA).

a) Regulatory required capital

CISGIL is required to hold capital at the greatest of three measures, namely the Individual Capital Assessment (ICA), the Individual Capital Guidance (ICG) and the Minimum Capital Requirement (MCR). Each of these measures is further described below:

i. ICA: In accordance with the Prudential Sourcebook for Insurers (INSPRU), each firm must have internal models to calculate its own capital requirements. The ICA is an economic risk-based assessment using CISGIL's capital model. 2nd Line Risk has responsibility for the overall design and governance of the capital model, which is developed and operated within the actuarial team. Capital model methodology and results are reviewed and approved by the Model Governance Committee, ERC and the Board. Outputs from the capital model are used in areas such as investment and reinsurance decisions, determining the risk in the business plans with regard to risk appetite and return on capital in pricing.

ii. ICG: The PRA reviews the ICA calculation periodically to assess whether it believes the models and controls surrounding the models are adequate and, if it deems it necessary, an 'add-on' is applied to reflect risks that were inadequately captured. The total ICA plus 'add-on' is known as the ICG.

iii. MCR: In accordance with the General Prudential Sourcebook (GENPRU) 2.1, CISGIL must hold capital resources equal to or in excess of its capital resources requirement. For a company writing general insurance this is termed the MCR and is defined as being the higher of a base capital resource requirement and the general insurance capital requirement (a formulaic hurdle where the calculation is based upon premiums, claims or the brought forward amount).

CISGIL has complied with all externally imposed solvency capital requirements throughout the period. CISGIL ensured continuous solvency through weekly, or when appropriate daily, monitoring. Monthly reports were provided to the Executive Risk Committee and Board.

The new solvency framework for insurers being developed by the EU, referred to as 'Solvency II', is intended to achieve greater harmonisation of approach across EU member states to assessing capital resources and requirements. Solvency II is expected to come into force on 1 January 2016. Under Solvency II, the Solvency Capital Requirement (SCR) will replace the ICA and ICG, and the MCR will be re-defined. CISGIL is actively progressing with activities to meet the required standards and with preparations to apply to the PRA for approval to use CISGIL's internal capital model to calculate the SCR.

b) Internal required capital

CISGIL has articulated a risk appetite which defines the confidence level with which the Board wants to meet the above requirements. This appetite in turn is used to calculate the additional capital that the Board mandate is held over and above the regulatory required capital.

c) Capital composition

CISGIL regulatory MCR capital resources comprise total shareholders' equity and subordinated debt, excluding inadmissible assets and equalisation provisions recognised in equity.

	2013	2012
Capital and reserves per the financial statements	**282.9**	276.1
Subordinated debt	**85.0**	85.0
Inadmissible assets	**(1.8)**	(6.2)
Statutory claims equalisation reserve	**(30.1)**	(29.5)
Discounting on technical provisions	**(0.9)**	(1.4)
Regulatory capital	**335.1**	324.0

Notes to the annual report and accounts

All amounts are stated in £m unless otherwise indicated

1. Segmental analysis

The business segments of CIS General Insurance Limited (CISGIL) are presented in line with the management information as reported to the Managing Director, Co-operative Banking Group, the Chief Operating Decision Maker (CODM).

CISGIL evaluates the performance of operating segments on the basis of the combined operating ratio, being the ratio of combined costs (operating expenses, claims and commission, net of other income) to net earned premiums. Overall CISGIL performance is evaluated on the basis of profit or loss from operations before tax attributable to shareholders, adjusted for non-operating items outside the control of the management, including variances in investment performance resulting from significant changes in external market conditions.

There is no geographic segmental reporting as all business is conducted in the UK. Revenues are attributed to the segments in which they are generated.

Segmental results include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. The accounting policies of the business segments are the same as those described in the summary of significant accounting policies.

Business segments

CISGIL comprises the following segments:

- **Motor** – Private motor car and motor cycle, individual commercial vehicles.
- **Home** – Domestic buildings, contents and personal possessions.
- **Other** – Commercial risks covering property, liability, financial loss, pet and motor fleet. Other minor personal risks, run off of inwards reinsurance liabilities, Financial Services Compensation Scheme levies and finance costs.

Segmented income statement for the year ended 31 December 2013	Motor	Home	Other	Total
Net earned premiums	**314.6**	**158.8**	**3.1**	**476.5**
Net claims incurred	**(256.1)**	**(64.1)**	**(10.6)**	**(330.8)**
Net commission expenses	**(1.5)**	**(8.3)**	**3.3**	**(6.5)**
Operating expenses	**(77.4)**	**(58.9)**	**(2.0)**	**(138.3)**
Net investment return	**33.9**	**5.2**	**0.8**	**39.9**
Other expenses	**–**	**–**	**(5.9)**	**(5.9)**
Segmented operating profit/(loss)	**13.5**	**32.7**	**(11.3)**	**34.9**

Segmented income statement for the year ended 31 December 2012	Motor	Home	Other	Total
Net earned premiums	417.3	158.1	4.2	579.6
Net claims incurred	(424.4)	(76.1)	(1.5)	(502.0)
Net commission expenses	(4.3)	(8.3)	1.6	(11.0)
Operating expenses	(89.1)	(40.4)	(1.3)	(130.8)
Net investment return	65.0	10.8	1.3	77.1
Other expenses	–	–	(5.0)	(5.0)
Segmented operating profit/(loss)	(35.5)	44.1	(0.7)	7.9

Reconciliation of segmental income to statutory income statement

Net earned premiums and claims are reported on a consistent basis for segmental and statutory reporting purposes.

	2013	2012
Operating expenses		
Total operating expenses for reportable segments	**(138.3)**	(130.8)
Items reported as significant within management information	**(1.3)**	–
Reclassification of investment expenses	**(1.3)**	(1.3)
Operating expenses	**(140.9)**	(132.1)
Commission expenses		
Total commission expenses for reportable segments	**(6.5)**	(11.0)
Reclassification of commission income	**(13.3)**	(10.7)
Fee and commission expenses	**(19.8)**	(21.7)
Other expenses is made up of:		
Financial Services Compensation Scheme levies	**(2.4)**	(1.4)
Finance costs	**(3.5)**	(3.6)
	(5.9)	(5.0)

All amounts are stated in £m unless otherwise indicated

1. Segmental analysis continued

Reconciliation of segmental income to statutory income statement

	2013	2012
Investment return		
Total investment return for reportable segments	**39.9**	77.1
Reclassification of investment expenses	**1.3**	1.3
Reclassification of other operating income	**(0.3)**	(3.6)
Investment return (analysed as below in the income statement)	**40.9**	74.8
Investment income	**27.9**	51.6
Gains less losses arising from financial instruments	**13.0**	23.2
	40.9	74.8

2. Net earned premiums

	2013	2012
Gross premiums		
Gross written premiums	**443.6**	555.7
Change in unearned premium provision	**65.4**	54.7
Gross earned premiums	**509.0**	610.4
Outward reinsurance premiums		
Premiums ceded	**(32.3)**	(29.4)
Change in unearned premium provision	**(0.2)**	(1.4)
Premiums ceded to reinsurers	**(32.5)**	(30.8)
Net earned premiums	**476.5**	579.6

3. Fee and commission income

	2013	2012
Fee income	**8.7**	7.9
Reinsurance commission earned	**3.7**	1.8
Other commission	**0.9**	1.0
	13.3	10.7

4. Investment income

	2013	2012
Interest and similar income from assets held at fair value through income or expense:		
Rental income from investment properties	**–**	0.1
Deposits with credit institutions	**1.2**	0.3
	1.2	0.4
Interest income (calculated using Effective Interest Rate) from available for sale assets:		
Listed debt securities	**26.7**	51.2
Total investment income	**27.9**	51.6

All amounts are stated in £m unless otherwise indicated

5. Gains less losses arising from financial instruments

	2013	2012
Net gains arising on financial assets:		
Available for sale listed debt securities	**13.0**	22.9
Derivatives	**–**	0.3
	13.0	23.2

Derivative gains relate to futures contracts; these contracts do not qualify for hedge accounting treatment under IAS 39 (Financial Instruments: Recognition and Measurement).

6. Other operating income

Other operating income includes £nil (2012: £3.0m) of rental income from owner occupied investment properties rented to other group companies, as these properties were sold during 2012, and £0.3m (2012: £0.6m) of interest income in respect of a loan to the Co-operative Group Limited.

7. Net policyholder claims and benefits paid

	2013	2012
Gross claims paid		
Current year claims	**154.1**	203.2
Prior year claims	**282.6**	322.0
Gross claims paid	**436.7**	525.2
Less salvage and subrogation		
Current year claims	**(10.2)**	(18.1)
Prior year claims	**(16.5)**	(24.3)
Salvage and subrogation received	**(26.7)**	(42.4)
Claims paid	**410.0**	482.8
Less amounts receivable from reinsurers		
Current year claims	**(4.2)**	(3.4)
Prior year claims	**(2.6)**	(6.5)
Amounts receivable from reinsurers	**(6.8)**	(9.9)
Net policyholder claims and benefits paid	**403.2**	472.9

8. Fee and commission expenses

	2013	2012
Commission paid	**18.5**	19.9
Change in deferred commission	**1.3**	1.8
	19.8	21.7

9. Operating expenses

	2013	2012
Administration expenses	**91.0**	82.3
Acquisition expenses	**49.9**	49.8
Significant items	**–**	4.9
	140.9	137.0

CISGIL does not have any employees; all sales are effected by employees of CFS Management Services Limited (CFSMS) which also provides administration and other services. CFSMS is also responsible for the remuneration of all directors of the Banking Group, including directors of CISGIL. CISGIL's share is charged to the company, at cost, by way of a management service charge from CFSMS. Key management compensation is discussed in note 27.

Included within the recharges is £7.6m (2012: £7.7m) paid by CISGIL in respect of its share of regular pension contributions, which includes £2.0m (2012: £2.1m paid) in respect of the PACE pension deficit funding. The details of the PACE scheme are included in the financial statements of The Co-operative Group.

Operating expenses include the following payments to auditors and their associates:

	2013 £'000	2012 £'000
Audit of these financial statements	**174**	116
Amounts receivable by CISGIL's auditor and its associates in respect of:		
Audit-related assurance services	**31**	30
Other assurance services	**–**	28
All other services	**19**	205
	224	379

10. Income tax

	2013	2012
Current tax		
UK tax for the current year	**7.5**	0.8
UK tax adjustments in respect of prior years	**(0.9)**	–
Total current tax charge	**6.6**	0.8
Deferred tax		
Origination and reversal of temporary differences	**0.1**	(0.1)
Effect of tax rate change	**(0.8)**	(0.2)
Total deferred tax credit	**(0.7)**	(0.3)
Total tax charge recognised in the income statement	**5.9**	0.5

Further information about deferred income tax is presented in note 21.

All amounts are stated in £m unless otherwise indicated

10. Income tax continued

Reconciliation of effective tax rate

The tax charge in the income statement differs from the theoretical amount that would arise using the corporation tax rate in the UK as follows:

	2013	2012
Profit before taxation	**33.6**	3.0
Tax calculated at domestic corporation tax rate of 23.25% (2012: 24.50%)	**7.8**	0.7
Effect of:		
Tax rate change on deferred tax	**(0.9)**	(0.2)
Other adjustments	**(1.0)**	–
Income tax charge	**5.9**	0.5

11. Deferred acquisition costs

	2013	2012
At the beginning of the financial year	**29.9**	33.6
Deferred acquisition costs	**70.4**	60.7
Amortisation	**(65.0)**	(64.4)
At the end of the financial year	**35.3**	29.9

All amounts in the current and prior year are expected to be recovered within one year.

12. Financial investments at fair value through income or expense

	2013	2012
Deposits with credit institutions	**207.6**	314.0

All amounts in the current and prior year are expected to be recovered within one year. Within the above are reverse repo balances of £180.0m (2012: £275.0m). Collateral of £178.8m is held as security against this balance (2012: £281.8m). Please see the credit risk note on pages 30 and 31 for further details.

This category comprises short term fixed rate deposits which are designated as fair value through income and expense upon initial recognition.

There has been no reclassification of financial assets between fair value and cost/amortised cost during the current or prior financial year.

13. Available for sale assets

	2013	2012
Listed debt securities – fixed rate	**720.0**	736.5
Listed debt securities – floating rate	**43.4**	37.0
	763.4	773.5

Of the total available for sale assets, £92.9m (2012: £151.5m) matures and is expected to be received within one year; the remainder is non-current.

All amounts are stated in £m unless otherwise indicated

14. Insurance receivables and other assets

	2013	2012
Receivables arising from insurance:		
Arising from insurance operations	**100.0**	137.1
Salvage and subrogation recoveries	**24.5**	61.4
Reinsurance operations	**1.2**	1.0
Other receivables:		
Accrued interest	**12.6**	16.1
Amounts receivable from Group companies	**6.8**	9.1
Investment receivables	**63.4**	–
	208.5	224.7

No amounts are due after more than one year.

Receivables arising from insurance operations are stated net of an impairment provision of £0.5m (2012: £0.1m). The provision is calculated based on an assessment of insurance receivables for objective evidence that an impairment loss has been incurred. Any adjustment to the level of the provision is recorded within the income statement as an adjustment to written premium.

Insurance receivables and other assets include amounts totalling £13.3m (2012: £16.5m) which are overdue; amounts overdue but not impaired are £12.8m (2012: £16.4m), being the overdue amount net of the impairment provision detailed above. £1.1m (2012: £1.2m) of amounts overdue primarily represent debts due from brokers and intermediaries which are considered fully recoverable. Amounts overdue are age analysed as follows:

	2013	2012
Amounts overdue:		
Less than 3 months	**12.2**	15.3
3 to 6 months	**–**	0.7
6 to 12 months	**1.1**	0.5

Assets past due typically comprise high volume/low value balances for which CISGIL does not seek collateral but continues to work with counterparties to secure settlement.

15. Loans and receivables

	2013	2012
Amounts due from the Co-operative Group Limited	**–**	50.0

The 2012 receivable arose from the sale of £39.0m of property, plant and equipment and £11.0m of investment property to the Co-operative Group Limited. The loan was secured on property and was repaid in full in February 2013.

16. Bank overdraft

Bank overdrafts are repayable on demand and form an integral part of CISGIL's cash management. As such they are included as cash and cash equivalents for the purpose of the statement of cash flows.

17. Share capital

	2013	2012
Authorised		
183,000,000 ordinary shares of £1 each	**183.0**	183.0
Allotted and called up		
183,000,000 ordinary shares of £1 each	**183.0**	183.0

Each shareholder has one vote and an additional vote for every 50 shares or fraction or part held by it in excess of the first 50 shares held.

All amounts are stated in £m unless otherwise indicated

18. Retained earnings and other reserves

	2013	2012
Retained earnings		
At the beginning of the financial year	**22.2**	19.7
Profit for the year	**27.7**	2.5
At the end of the financial year	**49.9**	22.2

Any retained earnings would represent amounts available for dividend distribution to the equity shareholder of CISGIL, subject to certain conditions being met.

Other reserves of £50.0m (2012: £70.9m) constitute available for sale reserves and a capital reserve. The capital reserve represents a non-refundable capital contribution from the immediate parent company, the Co-operative Banking Group Limited, and is distributable. Further details are given within the statement of changes in equity on page 14.

19. Other borrowed funds

	2013	2012
Floating rate subordinated notes 2021	**35.0**	35.0
Floating rate perpetual subordinated notes	**30.0**	30.0
Fixed rate perpetual subordinated notes	**20.0**	20.0
	85.0	85.0

Financial liabilities in respect of subordinated debt are unsecured, uncollateralised obligations. In the event of the winding-up of CISGIL, payment obligation is subordinated in favour of claims from all other unsubordinated creditors.

Finance costs incurred during the financial period include £3.3m (2012: £3.4m) in relation to interest on the subordinated debt.

There have been no defaults or breaches of contractual obligations attaching to the subordinated debt during the financial year.

Floating rate subordinated notes 2021

£75m of subordinated debt was issued to the immediate parent, the Co-operative Banking Group Limited, on 15 January 2006 at par. The debt has a fifteen year term with an option to repay in full at the tenth anniversary. Interest is payable quarterly in arrears at 1% above three month LIBOR up to the tenth anniversary and at 2% above three month LIBOR for the remainder of the term. During 2010, CISGIL redeemed £40m of the subordinated debt at par.

Floating rate perpetual subordinated notes

During 2007, £30m of additional perpetual subordinated debt was issued to the Co-operative Banking Group Limited in two tranches. £20m was issued on 30 July 2007 followed by a further £10m on 15 August 2007. In both cases the issue was at par. Both tranches provide for interest payable at 1.5% above three month LIBOR for the first five years and 2% above three month LIBOR thereafter. The agreements provided the option of full repayment at the fifth anniversary and continues to provide for repayment at quarterly intervals thereafter subject to certain conditions.

Fixed rate perpetual subordinated notes

A £20m tranche of perpetual subordinated debt was issued at par to the Co-operative Banking Group Limited during 2011. The subordinated debt has a coupon of 10% and has the option of full repayment at the fifth anniversary or at quarterly intervals thereafter subject to certain conditions.

All amounts are stated in £m unless otherwise indicated

20. Insurance contract liabilities and reinsurance assets

a) Analysis of insurance contract liabilities

	2013	2012
Gross		
Claims reported	**495.3**	557.5
Claims incurred but not reported	**144.9**	180.4
Claims settlement expenses	**16.7**	18.2
Unearned premiums	**207.2**	272.6
Unexpired risk provision	**2.2**	–
Total gross insurance liabilities	**866.3**	1,028.7
Recoverable from reinsurers		
Claims reported	**(23.2)**	(16.1)
Claims incurred but not reported	**(31.5)**	(26.4)
Unearned premiums	**(2.1)**	(2.3)
Total reinsurers' share of insurance liabilities	**(56.8)**	(44.8)
Net		
Claims reported	**472.1**	541.4
Claims incurred but not reported	**113.4**	154.0
Claims settlement expenses	**16.7**	18.2
Unearned premiums	**205.1**	270.3
Unexpired risk provision	**2.2**	–
Total net insurance liabilities	**809.5**	983.9

Reinsurance is used to limit risk to the balance sheet for the various classes of general insurance direct business. Proportional and non-proportional types of reinsurance cover have been purchased in accordance with assumptions made regarding the possible levels of losses and required returns on equity.

Indemnification agreement

On 15 January 2006, CISGIL assumed responsibility for the benefits and burdens arising from the run off of general insurance liabilities of the Co-operative Insurance Society Limited (CISL) under the terms of an indemnification agreement. Insurance contract liabilities at the end of the year include the following liabilities from the policies written by CISL:

	2013	2012
Outstanding claims	**41.3**	47.5
Claims incurred but not reported	**22.2**	17.3
Total gross insurance liabilities	**63.5**	64.8

20. Insurance contract liabilities and reinsurance assets continued

b) General insurance contracts – assumptions, changes in assumptions and sensitivity

i. Basis of assessing liabilities

CISGIL has access to historical data and trends relating to the general insurance business of CISL for which it has now assumed responsibility.

CISGIL uses a combination of recognised actuarial and statistical techniques to assess the ultimate cost of claims. These include:

- projecting historic claims payment and recoveries data;
- projecting numbers of claims;
- adjusting case estimates for future inflation and onto a provisioning basis;
- deriving average costs per claim to apply to claim numbers; and
- projecting historic claims paid and incurred data (payment plus estimates) – statistical actuarial techniques including chain ladder, Bornhuetter-Ferguson and Cape Cod.

Detailed claims data, including individual case estimates, is used to derive patterns in average claims costs and timings between occurrence and estimate/payment of claims. The most common method used is the chain ladder method. This technique involves the analysis of historical claims development trends and the selection of estimated development factors based on this historical pattern. The selected development factors are then applied to cumulative claims data for each accident year which is not yet fully developed to produce an estimated ultimate claims cost for each accident year. A degree of judgment is required in selecting the most appropriate development factors.

The chain ladder method can be quite volatile for relatively undeveloped origin periods so a Bornhuetter-Ferguson/Cape Cod method is often used in such cases. This method uses some prior expectation of the ultimate claims, and stabilises the projected ultimate by weighting between the prior expected ultimate and the projected based on the assumed development factors. The Cape Cod method differs from the Bornhuetter-Ferguson method in that it uses a trending of ratios (such as the average cost) to arrive at a prior expected ultimate for use in the projections.

The work is undertaken and supervised by suitably qualified personnel. Claims provisions are separately computed for each claim type such as bodily injury, accidental damage, storm, flood and subsidence. All provisions are calculated with explicit allowance for reinsurance and subrogation recoveries. Provisions are not discounted for investment return other than any required additional provision for unexpired risks, periodic payment settlements and provisions relating to asbestos exposure within the electric industry ('EIROS' claims).

Discounted reserves in respect of periodic payment settlements are £23.8m (2012: £23.2m) and EIROS discounted reserve amounts to £2.7m (2012: £2.5m). Further details around expected settlement patterns for claims arising on these reserves are disclosed within the insurance risk section on pages 25 and 26.

The EIROS reserve was based on a report produced for the industry by Towers Watson (an actuarial consultancy) at the end of 2013, which gave Towers Watson's estimate of both the undiscounted and discounted incurred but not reported (IBNR) reserves as at the end of June 2013. This was the most recent report available when we calculated our year end 2013 reserves.

In respect of business yet to be earned, the adequacy of the premium to cover future claims costs and expenses is assessed to determine the need for an Unexpired Risk Provision (URP) by comparing the discounted premium and outgoings. As at the end of 2013 there is a need for an URP of £2.2m.

As outlined within the risk management section, there is significant uncertainty in the assessment of liabilities, and provisions are set to be adequate to cover the anticipated eventual cost. Sensitivity analysis is performed to assist the selection of key parameters and, hence, the provisions adopted. Provisions are subject to detailed review regarding the appropriateness of key assumptions and the quantum of the provisions established.

The overall objective of CISGIL's reserving policy is to produce reliable and accurate reserves. Assumptions underlying the reserving calculations are agreed by the Quarterly Reserving Committee (QRC). Methodologies are peer reviewed throughout the calculation process. Provisions are approved and signed off by the QRC, and any margin above the actuarial best estimate reserve is set by the Chief Financial Officer.

Periodic reports are produced by the actuarial team and presented to the Periodic Reserving Committee in order to advise management of the performance of the business. More detailed reports are produced on a quarterly basis providing information on the performance of the business against plan. These reports are presented to the QRC and form the basis of reporting the performance to the Board.

ii. Key assumptions

Principal assumptions underlying the claims provisions include:

- Future inflation rates are in line with those recently implied in the claims data; and
- for bodily injury claims allowance has been made for:
  - i. use of the appropriate Ogden Tables;
  - ii. awards for general damages in accordance with the 10th edition of the JSB guidelines;
  - iii. a proportion of large claims being settled by periodic payments; and
  - iv. improvements in the case estimation techniques resulting in earlier recognition of the size of claims.

All amounts are stated in £m unless otherwise indicated

20. Insurance contract liabilities and reinsurance assets continued

The gross insurance provision for claims and loss adjustment expenses arising in respect of prior years of £427.1m (2012: £439.9m) includes a movement of £47.3m (2012: £43.8m) arising from an release/(increase) of reserves, as follows:

	2013	2012
Fire and Accident release of reserves	**7.2**	3.1
Motor release/(increase) of reserves	**42.8**	(43.1)
Increase in claims handling reserves	**(2.7)**	(3.8)
Movement in gross insurance liabilities	**47.3**	(43.8)

iii. Sensitivity analysis

There is greater uncertainty over motor claims provisions than other provisions as they often involve claims for bodily injury and associated legal costs which typically have a longer period to settlement. Motor provisions represent the most significant proportion of the total general insurance outstanding claims liabilities (gross of salvage and subrogation). Sensitivity information is given for motor claims provisions together with limited information for all other classes. The following table indicates the effect on gross claims provisions (gross of reinsurance and salvage and subrogation) of changes in key assumptions. The impact of the increased uncertainty on the income statement risk is mitigated through holding management margin on the best estimate reserves that is proportional to the level of uncertainty.

	Change in parameter	Effect on gross provision	% Effect
2013			
Assumption			
Motor			
Average cost of claims for last three years – bodily injury and legal	**10%**	**65.0**	**12.3%**
Mean term to settlement – bodily injury and legal	**+½ year**	**10.3**	**1.9%**
Rate of future inflation – bodily injury and legal	**1%**	**18.4**	**3.5%**
Ogden discount rate – bodily injury	**-¼%**	**2.2**	**0.4%**
Other classes			
Mean term to settlement (liability)	**+½ year**	**0.4**	**2.1%**
Mean term to settlement (non-liability)	**+½ year**	**0.8**	**1.4%**
Rate of future inflation (liability)	**1%**	**0.9**	**4.9%**
Rate of future inflation (non-liability)	**1%**	**0.7**	**1.3%**

	Change in parameter	Effect on gross provision	% Effect
2012			
Assumption			
Motor			
Average cost of claims for last three years – bodily injury and legal	10%	66.9	13.7%
Mean term to settlement – bodily injury and legal	+½ year	10.8	1.9%
Rate of future inflation – bodily injury and legal	1%	18.7	3.2%
Ogden discount rate – bodily injury	-¼%	4.6	0.8%
Other classes			
Mean term to settlement (liability)	+½ year	0.2	2.1%
Mean term to settlement (non-liability)	+½ year	0.8	1.3%
Rate of future inflation (liability)	1%	0.6	5.2%
Rate of future inflation (non-liability)	1%	0.9	1.3%

All amounts are stated in £m unless otherwise indicated

20. Insurance contract liabilities and reinsurance assets continued

c) Change in general insurance liabilities and reinsurance assets

i. Change in insurance contract liabilities (net of salvage and subrogation)

	Gross 2013	Unexpired risk provision 2013	Salvage & subrogation 2013	Net 2013	Gross 2012	Unexpired risk provision 2012	Salvage & subrogation 2012	Net 2012
At the beginning of the year	**756.1**	**–**	**(61.4)**	**694.7**	716.3	–	(46.6)	669.7
Movement in the year	**(99.3)**	**2.2**	**36.9**	**(60.2)**	39.8	–	(14.8)	25.0
At the end of the year	**656.9**	**2.2**	**(24.5)**	**634.5**	756.1	–	(61.4)	694.7

Salvage and subrogation is included within assets as part of insurance receivables (note 14).

ii. Claims and loss adjustment expenses

	Gross 2013	Reinsurance 2013	Net 2013	Gross 2012	Reinsurance 2012	Net 2012
Claims reported	**557.5**	**(16.1)**	**541.4**	587.8	(17.3)	570.5
Claims incurred but not reported	**180.4**	**(26.4)**	**154.0**	111.2	(29.3)	81.9
Claims settlement expenses	**18.2**	**–**	**18.2**	17.3	–	17.3
At the beginning of the year	**756.1**	**(42.5)**	**713.6**	716.3	(46.6)	669.7
Claims paid during the year	**(436.7)**	**6.8**	**(429.9)**	(525.2)	9.9	(515.3)
Increase/(decrease) in liabilities:						
Arising from current year claims	**384.7**	**(17.2)**	**367.5**	521.2	(12.3)	508.9
Arising from prior year claims	**(47.3)**	**(1.8)**	**(49.1)**	43.8	6.5	50.3
Total movement	**(99.3)**	**(12.2)**	**(111.5)**	39.8	4.1	43.9
Claims reported	**495.3**	**(23.2)**	**472.1**	557.5	(16.1)	541.4
Claims incurred but not reported	**144.9**	**(31.5)**	**113.4**	180.4	(26.4)	154.0
Claims settlement expenses	**16.7**	**–**	**16.7**	18.2	–	18.2
At the end of the year	**656.9**	**(54.7)**	**602.2**	756.1	(42.5)	713.6

iii. Provisions for unearned premiums

	Gross 2013	Reinsurance 2013	Net 2013	Gross 2012	Reinsurance 2012	Net 2012
At the beginning of the year	**272.6**	**(2.3)**	**270.3**	327.3	(3.7)	323.6
Increase in the year	**443.6**	**(32.3)**	**411.3**	555.7	(29.4)	526.3
Release in the year	**(509.0)**	**32.5**	**(476.5)**	(610.4)	30.8	(579.6)
Movement in the year	**(65.4)**	**0.2**	**(65.2)**	(54.7)	1.4	(53.3)
At the end of the year	**207.2**	**(2.1)**	**205.1**	272.6	(2.3)	270.3

All amounts are stated in £m unless otherwise indicated

20. Insurance contract liabilities and reinsurance assets continued

iv. Unexpired risk provision

	Gross 2013	Reinsurance 2013	Net 2013	Gross 2012	Reinsurance 2012	Net 2012
At the beginning of the financial year	–	–	–	–	–	–
Increase in the financial year	2.2	–	2.2	–	–	–
Release in the financial year	–	–	–	–	–	–
Movement in the financial year	2.2	–	2.2	–	–	–
At the end of the financial year	2.2	–	2.2	–	–	–

Additional provision is made for unexpired risks where the claims and expense, likely to arise after the end of the financial year, in respect of contracts concluded before that date, are expected to exceed the unearned premiums at the end of the financial year. The provision related to the motor class of business. Further details can be found in the accounting policy on page 21.

v. Analysis of claims development

	Accident year								
	2006	2007	2008	2009	2010	2011	2012	2013	Total
Gross of reinsurance									
At end of the accident year:	1,367.9	384.5	347.3	325.8	411.3	498.0	502.1	368.1	4,205.0
One year later	1,264.7	387.8	319.7	333.0	456.3	531.2	473.4	–	3,766.1
Two years later	1,199.3	378.3	310.2	340.7	481.0	528.4	–	–	3,237.9
Three years later	1,206.8	364.2	300.8	328.9	466.5	–	–	–	2,667.2
Four years later	1,195.9	367.4	297.2	320.2	–	–	–	–	2,180.7
Five years later	1,185.9	366.6	294.1	–	–	–	–	–	1,846.6
Six years later	1,184.1	362.5	–	–	–	–	–	–	1,546.6
Seven years later	1,195.8	–	–	–	–	–	–	–	1,195.8
Estimate for cumulative claims	1,195.8	362.5	294.1	320.2	466.5	528.4	473.4	368.1	4,009.0
Cumulative payments to date	(1,115.5)	(348.0)	(288.8)	(299.5)	(409.8)	(431.3)	(328.1)	(146.8)	(3,367.8)
Gross outstanding claims liabilities before discounting	80.3	14.5	5.3	20.7	56.7	97.1	145.3	221.3	641.2
Discounting									(1.0)
Gross outstanding claims liabilities									640.2
Gross claims reported									495.3
Gross claims incurred but not reported									144.9
Gross outstanding claims liabilities									640.2

All amounts are stated in £m unless otherwise indicated

20. Insurance contract liabilities and reinsurance assets continued

	Accident year								
	2006	2007	2008	2009	2010	2011	2012	**2013**	**Total**
Net of reinsurance									
At end of the accident year:	1,362.9	372.6	334.6	313.0	398.4	482.2	489.8	**350.9**	**4,104.4**
One year later	1,261.4	377.6	305.5	320.6	434.1	515.8	456.3	**–**	**3,671.3**
Two years later	1,195.9	369.6	296.3	325.6	458.4	516.6	–	**–**	**3,162.4**
Three years later	1,203.9	357.6	292.3	317.8	445.3	–	–	**–**	**2,616.9**
Four years later	1,192.8	359.6	290.2	310.0	–	–	–	**–**	**2,152.6**
Five years later	1,181.4	359.4	287.3	–	–	–	–	**–**	**1,828.1**
Six years later	1,179.8	355.2	–	–	–	–	–	**–**	**1,535.0**
Seven years later	1,188.5	–	–	–	–	–	–	**–**	**1,188.5**
Estimate for cumulative claims	1,188.5	355.2	287.3	310.0	445.3	516.6	456.3	**350.9**	**3,910.1**
Cumulative payments to date	(1,113.2)	(340.8)	(282.1)	(293.9)	(402.4)	(425.3)	(323.3)	**(142.6)**	**(3,323.6)**
Net outstanding claims liabilities before discounting	75.3	14.4	5.2	16.1	42.9	91.3	133.0	**208.3**	**586.5**
Discounting									**(1.0)**
Net outstanding claims liabilities									**585.5**
Net claims reported									**472.1**
Net claims incurred but not reported									**113.4**
Net outstanding claims liabilities									**585.5**

It is to be expected that releases will normally be made to prior years claims as current reserves are set such that no adverse deterioration is expected. However, from time to time the random occurrence of significant large individual claims or events being worse than expected can give rise to a required strengthening, in addition to normal claims development being adverse. The 2013 result includes movement on prior year reserves of £49.1m (2012: £50.3m). This is largely due to a change in the basis of estimation for salvage and subrogation.

21. Taxation

	2013	2012
Current tax		
(Liability)/asset at the beginning of the financial year	**(4.0)**	18.5
Tax charged to the income statement	**(6.6)**	(0.8)
Tax credited/(charged) directly to other comprehensive income:		
Changes in fair value on available for sale assets recognised through other comprehensive income	**6.3**	(9.0)
Tax received during the financial year	**(0.6)**	(12.7)
Liability at the end of the financial year	**(4.9)**	(4.0)

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 20% (2012: 23%).

	2013	2012
Deferred tax liability		
Liability at the beginning of the financial year	**(6.4)**	(6.7)
Tax credited to the income statement	**0.7**	0.3
Liability at the end of the financial year	**(5.7)**	(6.4)
Analysis of deferred tax liability		
Claims equalisation reserve	**(6.0)**	(6.8)
Other timing differences	**0.3**	0.4
Liability at the end of the financial year	**(5.7)**	(6.4)

The 2013 Budget on 20 March 2013 announced that the UK corporation tax rate will reduce to 20% with effect from 1 April 2015. Reductions in the rate from 24% (effective from 1 April 2012) to 23% (effective from 1 April 2013), and to 21% (effective from 1 April 2014) were substantively enacted on 26 March 2012, 3 July 2012 and 17 July 2013 respectively. This will reduce the company's future current tax charge accordingly. The deferred tax liability at 31 December 2013 has been calculated based on the rate of 20% substantively enacted at the balance sheet date.

All amounts are stated in £m unless otherwise indicated

22. Other reinsurance liabilities

	2013	2012
Arising from reinsurance operations	–	2.3

All amounts are due within one year.

23. Insurance and other payables

	2013	2012
Arising out of direct insurance operations	**1.7**	2.0
Accruals and deferred income	**5.7**	5.4
Insurance premium taxation payable	**7.6**	9.9
Amounts due to Group companies	–	0.1
Other payables	**2.9**	4.5
	17.9	21.9

All amounts are due within one year.

24. Contingent assets and liabilities

CISGIL has a contract with Parabis Ltd, for the provision of claims handling services for third party motor claims. These services are currently treated as VAT exempt within the annual report and accounts. However, this treatment has been challenged by Her Majesty's Revenue & Customs (HMRC). If the view of HMRC is upheld, CISGIL will be liable for a VAT charge (from 2010) of up to £2.1m (2012: £1.4m). Legal Counsel has indicated that it is probable that HMRC's view will be successfully challenged, and therefore a provision has not been made in the financial statements.

During 2012, a provision was raised by CISL, at the time a fellow subsidiary of the Co-operative Banking Group Limited, to cover the present value of lease commitments arising from the failure of a counterparty to which a number of leases had previously been assigned. As CISGIL benefited from the original assignment transaction, CISGIL made a cash contribution in 2012 of £2.6m towards the initial provision. In 2013, the provision and CISGIL's cash contribution was transferred into CFSMS. CISGIL has an agreement with CFSMS, to contribute to any additional costs in excess of the original provision it incurs. However the timing and size of this contribution is uncertain and as such a provision has not been made in CISGIL's year end accounts.

CISGIL is party to a Deed of Guarantee with the Trustee for the benefit of The Co-operative Group Pension Scheme (PACE) that, if CFSMS does not pay any amount due in respect of its funding obligations to PACE, CISGIL will pay to PACE its share of the amount due as if it were the principal obligor for such share. As explained in note 9, CISGIL is currently recharged by CFSMS for its share of the pension contributions, including an element of the PACE deficit funding. The directors have no reason to believe that CFSMS will not be able to continue making payments to PACE when due and therefore, at the current time, do not expect any payments to be required under the guarantee.

No other contingent assets or liabilities were identified as at 31 December 2013 (2012: £nil).

25. Commitments

No commitments were in place as at 31 December 2013 (2012: £nil).

26. Parent undertaking

CIS General Insurance Limited, a subsidiary of the Co-operative Banking Group Limited, is incorporated as an Industrial & Provident Society and is registered in England and Wales.

The Co-operative Group Limited is the ultimate parent and is incorporated as an Industrial & Provident Society and is registered in England and Wales.
The results of CIS General Insurance Limited are consolidated in the group headed by the Co-operative Group Limited. The financial statements of the immediate and ultimate holding organisations are available from 1 Angel Square, Manchester, M60 0AG.

All amounts are stated in £m unless otherwise indicated

27. Related party transactions

A number of transactions have been entered into during the course of the year with related parties. These have been conducted in the normal course of business and at arm's length. These include the provision of insurance products to members of the wider Co-operative Group and key management personnel.

	Balances with parent undertaking 2013	**Balances with other related parties 2013**	Balances with parent undertaking 2012	Balances with other related parties 2012
Balances with related parties				
At the beginning of the financial year	**(85.0)**	**(55.5)**	(85.0)	(73.9)
Movement in capital value	**–**	**(0.3)**	–	18.4
At the end of the financial year	**(85.0)**	**(55.8)**	(85.0)	(55.5)

During the financial period, CISGIL settled claims of £9.0m (2012: £17.1m) under the terms of an indemnification agreement to reinsure the general insurance liabilities of CISL in run off. Gross technical provisions in the balance sheet include £63.5m (2012: £64.8m), being outstanding claims liabilities.

CISGIL issued subordinated debt to its intermediate parent, the Co-operative Banking Group Limited. Interest during the financial period amounted to £3.3m (2012: £3.4m).

CISGIL has bank accounts with The Co-operative Bank plc. At the end of 2013, the aggregate balance stood at £0.9m (2012: £0.3m). During the year project costs of £0.7m (2012: £0.8m), included in operating expenses, were charged to CISGIL from The Co-operative Bank plc.

Co-operative Legal Services Limited, a subsidiary of the Co-operative Group Limited, provides legal cover to CISGIL motor and home policyholders. CISGIL has paid £2.7m (2012: received £0.1m) in relation to this cover.

CISGIL has an indemnification agreement, accounted for as an intra-group guarantee under IFRS 4, with CFSMS in which CISGIL has agreed to indemnify CFSMS against all and any liability, loss, damage, costs and expense arising from the agreement.

During the year management fees of £163.4m (2012: £150.7m) included in operating expenses and claims handling costs incurred were charged to CISGIL from CFSMS. £0.1m (2012: £0.2m) was charged for capital utilisation.

During the year, investment asset management fees of £0.7m (2012: £1.1m), included in operating expenses, were charged to CISGIL from the Co-operative Asset Management Limited (TCAM). TCAM ceased to be a related party from August 2013 onwards.

During 2012, CISGIL disposed of its investment property of £11.0m and property, plant and equipment of £39.0m to the Group in exchange for a loan of £50.0m. In February 2013, the Group repaid this loan in full. Interest income of £0.2m (2012: £0.6m) is included within other operating income in respect of the loan.

Key management (as defined by IAS 24) is considered to include the executive committee members of CISGIL and their close family members. Details of transactions and balances during the financial period are provided below.

All staff costs are borne by CFSMS and charged out to other companies within the Banking Group at cost.

Key management compensation

	2013	2012
Salaries and short term benefits	**1.1**	3.0
Termination benefits	**–**	1.4
	1.1	4.4

In 2012, key management was defined as Board and executive members of the wider Banking Group.

28. Fair values of financial assets and liabilities

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the annual report and accounts:

a) Financial investments at fair value through income or expense

The fair value of financial assets designated at fair value through income or expense, being short term (less than one month) fixed rate deposits, approximates to their nominal amount.

All amounts are stated in £m unless otherwise indicated

28. Fair values of financial assets and liabilities continued

b) Available for sale assets

Fair value of listed debt securities is based on clean bid prices at the balance sheet date without any deduction for transaction costs.

Available for sale assets are regularly reviewed for impairment. Objective evidence of impairment can include default by a borrower or issuer, indications that a borrower or issuer will enter bankruptcy or the disappearance of an active market for that financial asset because of financial difficulties.

These reviews give particular consideration to evidence of any significant financial difficulty of the issuer or measurable decrease in the estimated cash flows from the investments.

c) Borrowed funds

Fair value measurement is calculated on a discounted cash flow basis using prevailing market interest rates.

d) Receivables and payables

For receivables and payables with a remaining life of less than one year, the nominal amount is deemed to reflect the fair value, where the effect of discounting is immaterial.

The table below shows a comparison of the carrying value and fair values of financial instruments where the value is significantly different. In all other instances fair values are not materially different from carrying values.

Financial liabilities

	Carrying value 2013	**Fair value 2013**	Carrying value 2012	Fair value 2012
Other borrowed funds	**85.0**	**85.1**	85.0	82.6

Financial asset and liability classification

The table below analyses financial instruments by measurement basis as detailed by IAS 39 (Financial Instruments: Recognition and Measurement).

Balance sheet categories

	Designated at fair value	**Loans and receivables**	**Available for sale**	**Other amortised cost**	**Total**
2013					
Assets					
Financial assets at fair value through income or expense	**207.6**	**–**	**–**	**–**	**207.6**
Available for sale assets	**–**	**–**	**763.4**	**–**	**763.4**
Other financial assets	**–**	**184.0**	**–**	**–**	**184.0**
Total financial assets	**207.6**	**184.0**	**763.4**	**–**	**1,155.0**
Non-financial assets					**116.6**
Total assets					**1,271.6**
Liabilities					
Other borrowed funds	**–**	**–**	**–**	**85.0**	**85.0**
Overdrafts	**–**	**–**	**–**	**8.9**	**8.9**
Other financial liabilities	**–**	**–**	**–**	**17.9**	**17.9**
Total financial liabilities	**–**	**–**	**–**	**111.8**	**111.8**
Non-financial liabilities					**876.9**
Total liabilities					**988.7**
Capital and reserves					**282.9**
Total liabilities and equity					**1,271.6**

All amounts are stated in £m unless otherwise indicated

28. Fair values of financial assets and liabilities continued

Financial asset and liability classification

	Designated at fair value	Loans and receivables	Available for sale	Other amortised cost	Total
2012					
Assets					
Financial assets at fair value through income or expense	314.0	–	–	–	314.0
Available for sale assets	–	–	773.5	–	773.5
Other financial assets	–	213.3	–	–	213.3
Total financial assets	314.0	213.3	773.5	–	1,300.8
Non-financial assets					136.1
Total assets					1,436.9
Liabilities					
Other borrowed funds	–	–	–	85.0	85.0
Overdrafts	–	–	–	12.5	12.5
Other financial liabilities	–	–	–	24.2	24.2
Total financial liabilities	–	–	–	121.7	121.7
Non-financial liabilities					1,039.1
Total liabilities					1,160.8
Capital and reserves					276.1
Total liabilities and equity					1,436.9

The following table provides an analysis of financial assets and liabilities that are valued or disclosed at fair value, by the three level fair value hierarchy as defined within IFRS7 (Financial Instruments: Disclosure):

- Level 1 – fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 – fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (ie derived from prices).
- Level 3 – fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Based upon guidance issued by The Committee of European Securities Regulators (CESR), CISGIL classifies debt securities in Level 1 only if it can be demonstrated on an individual security by security basis that these are quoted in an active market, ie that the price quotes obtained are representative of actual trades in the market (through obtaining binding quotes or through corroboration to published market prices).

All amounts are stated in £m unless otherwise indicated

28. Fair values of financial assets and liabilities continued

Valuation of financial instruments

	Level 1	Level 2	Level 3	Total
2013				
Assets				
Financial assets at fair value through income or expense	–	**207.6**	–	**207.6**
Available for sale assets	–	**763.4**	–	**763.4**
Total financial assets at fair value	–	**971.0**	–	**971.0**
Liabilities				
Other borrowed funds	–	**85.1**	–	**85.1**
Total financial liabilities at fair value	–	**85.1**	–	**85.1**

Valuation of financial instruments

	Level 1	Level 2	Level 3	Total
2012				
Assets				
Financial assets at fair value through income or expense	–	314.0	–	314.0
Available for sale assets	–	773.5	–	773.5
Total financial assets at fair value	–	1,087.5	–	1,087.5
Liabilities				
Other borrowed funds	–	82.6	–	82.6
Total financial liabilities at fair value	–	82.6	–	82.6

The valuation techniques using observable inputs relate to debt securities that would otherwise be fair valued using quoted market prices but where there has been short term temporary market inactivity and borrowed funds with no active market price. In obtaining relevant fair values for financial assets, CISGIL has obtained security specific prices from third party market makers based on what the third parties would have traded these particular securities for at the year end date. Financial liabilities have been valued using observable inputs including discounted cash flows and comparable credit spreads.

The following table allows comparison of debt securities (other than those classified at fair value through income or expense) on the basis of the current carrying amount, fair value and amortised cost (pre impairment).

	Carrying amount 2013	Fair value 2013	Amortised cost 2013
Investments in debt securities as:			
Available for sale financial assets	**763.4**	**763.4**	**772.5**

	Carrying Amount 2012	Fair value 2012	Amortised cost 2012
Investments in debt securities as:			
Available for sale financial assets	773.5	773.5	775.4

All amounts are stated in £m unless otherwise indicated

29. Post balance sheet events

In March 2013 The Co-operative Group announced plans to sell CISGIL, with proceeds of the sale envisaged to be a part of the Group's planned £1bn contribution to the recapitalisation of The Co-operative Bank. In January 2014, having considered the sale process and in light of changed requirements under the Bank recapitalisation process, it was decided to reverse the decision to sell. CISGIL's significant growth potential was taken into account in reaching this decision.

CISGIL has entered into an indemnification agreement with Royal London (CIS) Limited, formerly Co-operative Insurance Society Limited (CISL), to assume financial responsibility for the run off of the general insurance business formerly written by CISL. A High Court hearing took place on 17 March 2014, where the Court was asked to approve the Part VII transfer, to CISGIL, of this business in run off. The approval of the Court was received, and the Part VII transfer took effect from 31 March 2014.

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