Hiscox Ltd Report and Accounts 2009

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HISCOX

Our ambition remains to be a highly respected international specialist insurance and reinsurance company, built on a balance between volatile international catastrophe business and more steady local and regional business.

Robert Hiscox
Chairman

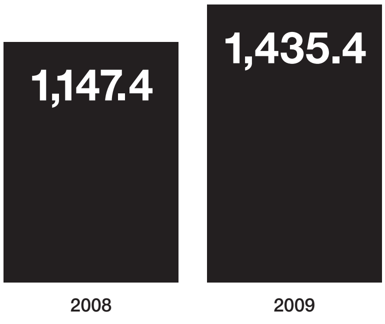
Corporate highlights

30.1%
Return on equity

Group key performance indicators

	2009	2008
Gross premiums written (£m)	**1,435.4**	1,147.4
Net premiums earned (£m)	**1,098.1**	928.1
Profit before tax (£m)	**320.6**	105.2
Profit after tax (£m)	**280.5**	70.8
Earnings per share (p)	**75.2**	18.8
Total dividend per share for year (p) – increased by 17.6%	**15.0**	12.75
Net asset value per share (p) – increased by 15.9%	**299.2**	258.1
Group combined ratio excluding foreign exchange (%)	**82.2**	91.6
Group combined ratio (%)	**86.0**	75.3
Return on equity (%)	**30.1**	9.2
Investment return (%)	**7.2**	(1.3)

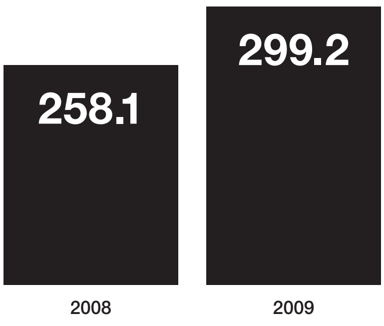
Gross premiums written £m



Operational highlights

- Insurance rates broadly stable and still very attractive in reinsurance
- Retail and specialty businesses continue to grow
- Ongoing investment in UK marketing benefits Group

Net asset value p per share



Why invest in Hiscox?

We are a leading specialist insurer with:
- **balance that creates opportunity throughout the cycle**
- **strong financial performance**
- **a transparent approach to risk**
- **specialist expertise that is valued by our customers.**

Our business

A balanced portfolio that creates opportunity throughout a cyclical market
Hiscox's strategy is to balance the more volatile catastrophe-exposed insurance and reinsurance with steady local specialty insurance. Our diversity by product and geography gives us great flexibility, particularly in a tough commercial environment. We are able to grow and shrink the catastrophe-exposed lines according to market conditions. Currently, rates for reinsurance, which makes up almost a third of our income, are close to an all-time high, and we are therefore making the most of this opportunity. However, we have the flexibility to shrink this side of the business when rates are no longer favourable. Our local specialty insurance business tends to be steadier throughout the insurance cycle and we have successfully grown our retail lines by 10% year-on-year over the last five years.

Our performance

Strong financial performance
Hiscox has a strong record of top-line growth with a focus on ROE. Performance highlights between 2005 and 2009 include:
- nearly doubled in size to produce gross written premiums of over £1.4 billion
- healthy combined ratio averaging 86.2%
- delivered average ROE of 22%
- maintained a progressive dividend policy with compound growth of 16.5%.

Our expertise

A transparent approach to risk
The very business of insurance is managing risk. The understanding of risk is intrinsic to every level of decision-making in the Group. We devote a great deal of expertise to understanding the impact of global events and model these rigorously. We also draw on over 100 years of history in insurance to assess these risks.

Catastrophes such as hurricanes and earthquakes could hit at any time, and naturally would have an impact on our business. Therefore twice a year, in our analysts' presentations and on our website, we publish estimates of what the Group's losses would be should such a catastrophe occur.

Our people

Specialist expertise that is valued by our customers
We are market leaders in many of our specialist areas and our customers value the expertise and cover we provide.
*What our UK customers said:**
- 96% of business insurance customers were satisfied that we spoke to them in a clear way and avoided using financial jargon
- 99% of home insurance customers were satisfied that we answered their questions and provided the information they needed today
- over 90% of our home insurance customers surveyed were satisfied with the way we settled their claim.

In a 2009 award voted for by independent brokers, Hiscox UK was named Insurance Times' 'Commercial Lines Insurer of the Year' for the third year running. We were also awarded 'General Insurer of the Year' at the British Insurance Awards 2009.

* Results from our monthly customer satisfaction survey for customers telephoning one of our UK-based contact centres.

Chairman's statement

It is an enormous pleasure to report a gross profit of £320.6 million – three times last year's profit and considerably higher than the previous record of £237 million in 2007. I know that Mother Nature was kind, but my definition of luck is when preparation meets opportunity, and our catastrophe underwriters did an immense amount of preparation and research to underwrite a carefully controlled exposure which could benefit from a benign catastrophe period, but not hurt us if nature turned vicious. I also believe that the stability of the general insurance industry during the recent banking bubble deserved a reward.

The investments yielded a cracking result.

And our strategy of growing our specialist retail businesses internationally to balance the catastrophe accounts continued apace.

Results

The result for the year ending 31 December 2009 was a profit before tax of £320.6 million (2008: £105.2 million) on a gross written premium income of £1,435.4 million (2008: £1,147.4 million). The combined ratio was 86.0% (2008: 75.3%). The combined ratio on a like-for-like basis excluding foreign exchange distortions was 82.2% (2008: 91.6%). Earnings per share on profits after tax were 75.2p (2008: 18.8p), and net assets per share increased to 299.2p (2008: 258.1p). The return on equity was 30.1% (2008: 9.2%).

Dividend and capital management

The Board proposes to pay a second interim dividend of 10.5p on 29 March 2010 to shareholders on the register on 5 March 2010 in place of a final dividend, making total dividends for the year of 15.0p (2008: 12.75p).

We remain prepared to buy back our shares if the share price drops to an unrealistic level. We are pleased we did not do a Rights Issue last year but decided to sweat our capital and avoid dilution. This excellent profit has allowed us to pay an increased dividend, added sufficient capital for our current plans, and enabled us to set aside a buffer of capital to maintain appropriate capital ratios in case of reduced investment income in 2010.

The insurance market

In my half year statement in 2007 I wrote that it seemed surreal to be announcing record results when our shares were rated so lowly. There was then a re-rating of the general insurance sector, but suspicion and malaise seems to have crept in again. Commentators seem cynical about our prospects and the insurance industry as a whole is valued at less than book value. Hiscox is rated at a small premium to assets and a ridiculously low multiple of earnings.

I agree that the general insurance industry has been blighted by poor underwriting in the past when investment profits were easier to make and underwriting didn't seem to matter too much. In my youth, insurance companies were described as investment trusts with an expensive habit. But the investment market is now offering slim pickings, so underwriting – our basic trade – matters totally, and there are firm signs that managements appreciate that fact. Reinsurance underwriting is dominated by models which we know are not right, but which impose a discipline and are an indispensable guide. The great attraction of the general insurance business is that everyone has to buy it; in fact, more and more so as governments continue to impose countless regulations, any breach of which can lead to litigation. Demand for our products is continuous; it is up to us to price them properly and to supply products which customers want at that price.

During 2009 we implemented a new marketing campaign to attract our chosen customers and to continue to strengthen the brand. We want people to reach for a Hiscox policy because they trust it to perform better than standard commodity products. We are differentiating ourselves from the herd which will build value for shareholders.

Since I have been at Hiscox we have grown from a premium income of around £3 million to nearly £1.5 billion, and from profits of a few thousand to £300 million. Not in a straight line of either income or profit as the nature of our business is to absorb the unpredictable from others, but I can guarantee you that this business has the determination and talent to continue that profitable growth.

The Hiscox businesses

As usual, I leave it to the CEO, Bronek Masojada, to report in detail the progress of our spreading but very focused businesses.

Robert Hiscox
Chairman

Chairman's statement
continued

In brief, our catastrophe reinsurance underwriting in Bermuda and London was extremely profitable which enabled us to continue to invest in our US start-ups and our direct business. Our UK business demonstrated strong profitable growth, Europe had a tough first half but recovered well in the second, and Guernsey was outstanding as usual. We have made a major investment in the US and it was extremely gratifying to see the core errors and omissions account, which Ed Donnelly joined in 2005 to build, coming into profit.

To return to the valuation of insurance companies, I can understand that the volatility of earnings from the catastrophe account makes a valuation based on earnings difficult. Conversely, our strategy of building more stable specialist accounts should be valued much more highly if they can demonstrate sustainable earnings which I believe some have and the others will.

In the meantime, we will strive to continue to add to the net assets year-on-year which will inevitably drive the share price up over time.

People

First I must record our sadness at the recent death of our Senior Independent Non Executive Director, Sir Mervyn Pedelty. He was a huge asset to our business through his knowledge and business acumen, and his warm and humorous personality made him a real pleasure to work with. Life was more fun and interesting when Sir Mervyn was around.

Our inestimable CEO, Bronek Masojada, leads an excellent team at the top, and the talent stretches throughout the Company. Over the years we have steadily been able to attract better talent, and the current frailty of the banks and the political attacks on them will help us by making more talent available. We are acutely aware that we are only as good as the people who work here, and it has been gratifying that our conscious efforts to be an employer of choice for the best people continues to be rewarded. We have great teams throughout the Group and I am deeply grateful to them not only for this great profit but for being so inspirational to work with.

Outlook

As I have said, there is more discipline in our industry than at any time in my long career. It is of course not perfect, but the general insurance industry and Lloyd's in particular have performed excellently through the financial chaos of the last few years. I just hope that the regulators and Government will appreciate the industry's conservatism and value, and not wound it with some collateral damage from its current bank bashing.

The Hiscox Group has a solid core of profitable businesses which, over the last few years, have enabled us to invest in creating exciting new ventures which will each become core profit earners and bring great value to shareholders. I admire the restless search for new methods of selling our specialist products. The world belongs to the discontented; we will never be satisfied; the profitable growth will continue.

Robert Hiscox
Chairman
1 March 2010

Chief Executive's report

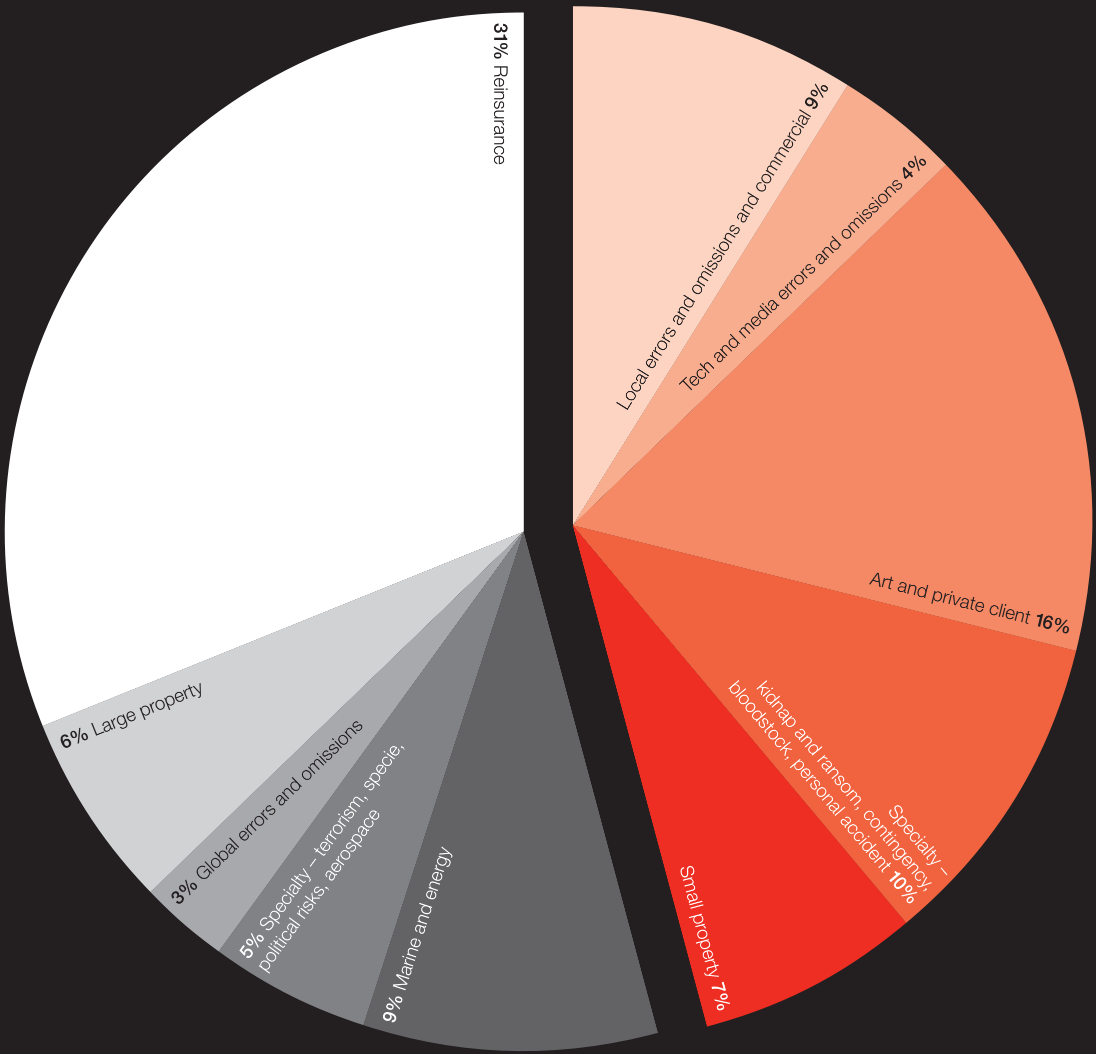
In 2009 we made a pre-tax profit of £320.6 million – the best result in the Group's history. Good underwriting and top-class investment management drove this result, helped by the absence of any major catastrophes. Our record profit has not come by sacrificing the future growth of the Group – in 2009 we continued to invest in building our brand in the UK and rapidly expanding our US operations.

Our strategy is to establish operations in Europe, the UK and the US that focus on our core specialty products to balance our more volatile business written in London and Bermuda. This strategy works: in 2005 when Hurricanes Katrina, Rita and Wilma drove some of our competitors deep into the red we made a healthy profit thanks to the contribution of our specialty businesses.

The market outlook for 2010 is positive, though with lower expected investment returns and the easing of rates it will probably not be as good a vintage as 2009. We will seek to grow in those specialist areas where margin remains strong and we will maintain our commitment to reinsurance.

Bronek Masojada
Chief Executive

Strategic focus
Total Group controlled income for 2009
100% = £1,713m



Chief Executive's report
continued

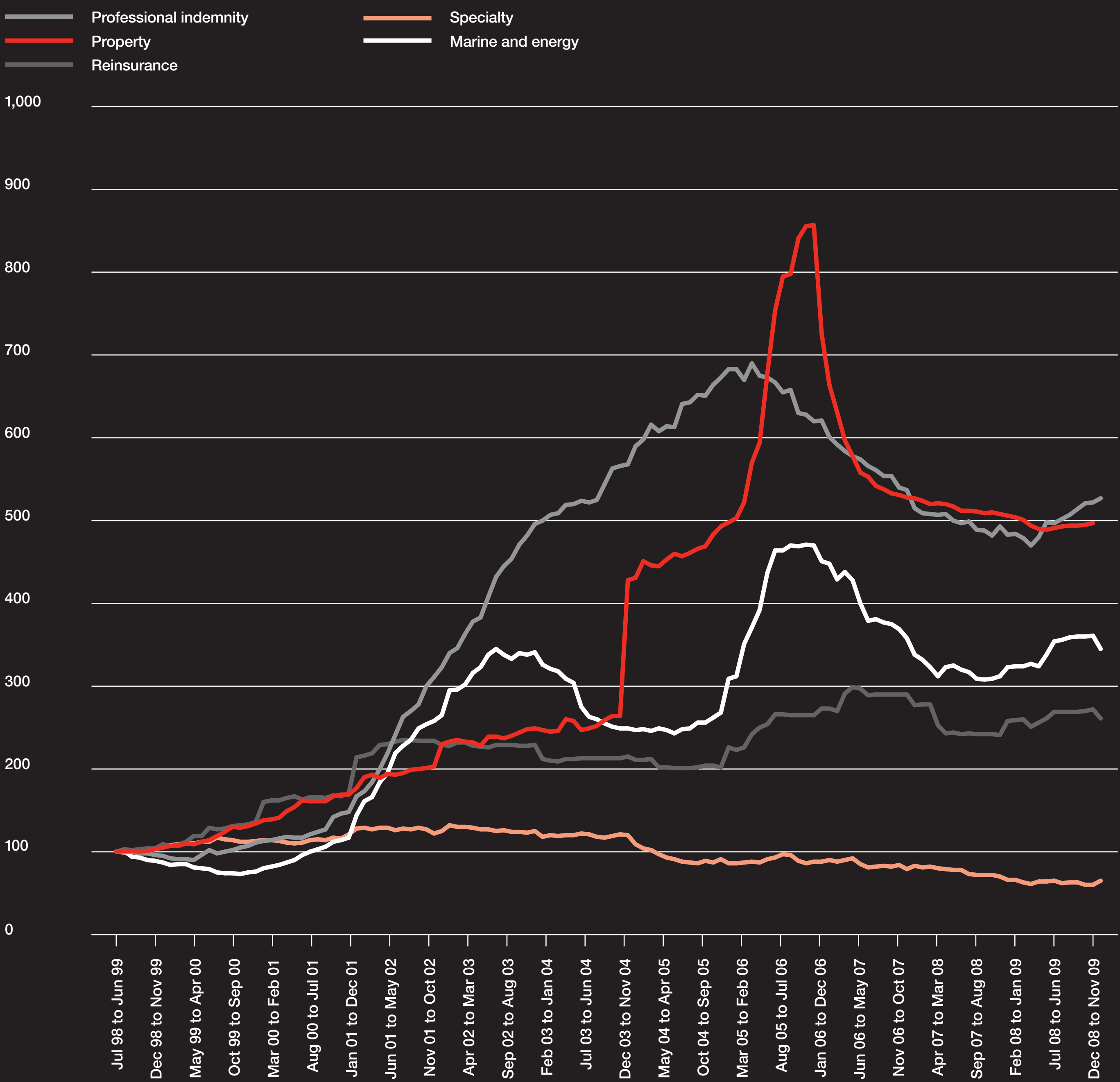
Group performance

In 2009 our pre-tax profit was £320.6 million (2008: £105.2 million). Gross written premium grew by 25.1% to £1,435.4 million (2008: £1,147.4 million). Part of this growth was driven by exchange rate fluctuations and in constant exchange rate terms our gross written premium grew by 5.6%. Return on equity was 30.1% (2008: 9.2%) and our net asset value increased to 299.2p (2008: 258.1p).

The dividend has been increased to 15.0p (2008: 12.75p). Over the past five years our dividend has risen by 16.5% compounded, and we have returned £114 million, net of a £176 million capital raising, to investors.

I review the individual performance of our business units opposite.

Hiscox London Market rating index
Index level (%). 12 month rolling period



Hiscox London Market
Hiscox London Market was again the main profit generator in the Group, contributing £179.9 million (2008: £137.0 million). This was achieved through underwriting £663.0 million of business (2008: £545.9 million).

The London Market business is managed through five divisions whose performance is reviewed below:

- **Reinsurance**: Our reinsurance business performed well yet again. Having made a profit in 2008 despite the impact of Hurricane Ike, it is not surprising that it made a very good return in a year largely free of major losses. Our expertise in reinsurance is widely recognised, reflected by the fact that a number of third-party capital providers have chosen us to underwrite on their behalf. In 2009 Syndicate 6104 – a syndicate funded entirely by third-party capital – supported us. This support has been extended into 2010. We have a number of similar arrangements with other insurance companies. Overall, reinsurance prices softened in the January renewals, although I believe that in 2010 we will see rates largely similar to or better than those in 2008 – a year in which we achieved a good result despite the impact of Hurricane Ike.

- **Specialty**: This division underwrites a spread of specialist risks: personal accident, bloodstock, kidnap and ransom, terrorism, political risks and aviation war. Good performance across most of these lines was offset by political risk losses, largely due to credit defaults. We took a very cautious approach early in the year in reserving for these claims in view of the continuing fragile state of the global economy. There is a possibility, however, that, as conditions improve, these political risk losses may reduce, which is what we experienced in the last big financial crisis in 1998. In keeping with our belief that you should advance to the sound of gunfire we expect to expand our political risk underwriting this year as client demand and pricing increases due to the turbulent global economic situation.

- **Marine and energy**: This division had a good year. Energy rates rose in 2009 following Hurricane Ike. We were able to take advantage of these rates and better terms to write a larger book of business and have been well rewarded for doing so in 2010.

- **Property**: Our primary focus is on catastrophe exposed property for global companies, homeowners and small businesses. Rates have been under pressure and we expect to reduce the size of this account significantly. In 2010 this reduction will be partially offset by a scheme to underwrite mechanical equipment – a non-cat area which we expect will serve us well.

- **Casualty**: Our London team now focuses on professional indemnity written in Lloyd's and its results exclude the technology and media book which is now accounted for as part of Hiscox USA. We have shrunk as rates have come under pressure and have taken a cautious reserving approach in view of the economic climate. We have, however, had a net benefit from releases on prior underwriting years.

The division saw a change of leadership during the year. Richard Watson got the year off to a great start before moving to the USA to head up our business there. Russell Merrett, who led our reinsurance business for the last four years, was promoted to lead the division. He has settled into the role well. We took advantage of this management change to focus the division on serving those brokers – large and small – who bring business to London, instead of being distracted by opportunities in other regions. London has recently experienced a renaissance as an insurance market and we see plenty of opportunities to grow our business with London brokers in the years ahead.

Hiscox UK and Hiscox Europe – specialty retail
Our specialist retail businesses in the UK and mainland Europe grew well in 2009. In underwriting terms, the UK had a very good year, while Europe did not.

- **Hiscox UK**: In the UK we saw premium growth of 16.1% to £304.0 million (2008: £261.9 million). Growth was particularly strong in fine art due to the acquisition of some global polices insured in London. The professions and specialty commercial business has continued to develop and for the first time it now exceeds the size of the UK focused art and private client business. The UK direct business continued to see strong growth and is near break even net of all its marketing costs.

  Our substantial marketing investment over the past four years, masterminded by Steve Langan, has turned Hiscox into a recognised consumer brand in the UK, one known not only for the quality of its products but also for its claims management. Of our household claimants 92% reported that they were either 'satisfied' or 'very satisfied' with the claims service they received. Our success has also been recognised by brokers. In a 2009 award voted for by independent brokers, we were named Insurance Times' 'Commercial

London has recently experienced a renaissance as an insurance market and we see plenty of opportunities to grow our business with London brokers in the years ahead.

Hiscox London Market

	2009 £m	2008 £m
Gross premiums written	**663.0**	545.9
Net premiums earned	**453.3**	427.8
Underwriting profit	**136.0**	34.2
Investment result	**79.7**	(5.5)
Foreign exchange	**(35.8)**	108.3
Profit before tax	**179.9**	137.0
Combined ratio	**78.8%**	65.8%
Combined ratio excluding foreign exchange	**71.0%**	94.5%

Hiscox UK and Europe

	2009 £m	2008 £m
Gross premiums written	**421.0**	357.1
Net premiums earned	**367.3**	303.3
Underwriting (loss)/profit	**(9.3)**	21.7
Investment result	**36.9**	(22.4)
Foreign exchange	**(7.1)**	32.5
Profit before tax	**20.5**	31.8
Combined ratio	**105.1%**	81.6%
Combined ratio excluding foreign exchange	**103.3%**	92.3%

Chief Executive's report continued

Insurer of the Year' for the third year running, and also won the title of 'General Insurer of the Year' at the British Insurance Awards.

We are not resting on our laurels. In 2010, we will seek to grow our direct business further, pushing it into profit. We foresee a tougher claims environment in some sectors as professional firms get blamed for their customers' recession-related misfortunes. Prices will have to rise to reflect this.

— **Hiscox Europe**: 2009 was a disappointing year for Europe, in spite of premium growth of 6.8% to €131.6 million (2008: €123.2 million). Its underwriting performance in 2009 was significantly worse than 2008, due to a series of unconnected large losses. In 2009, after a few poor years, our German operation succeeded in making a profit through a rigorous re-underwriting of its high net worth book and new focus on expanding in commercial lines.

We have been building a business in Europe for the past decade, but we know that the ROE – the return on effort that is – is below expectations. Pierre-Olivier Desaulle, who we appointed Managing Director of Hiscox Europe during the year, will inject new energy into the operation. As MD of Hiscox France since 2000 he grew it six-fold and delivered sustainable profits. The European Management Team is focused on repeating this success across the continent.

Hiscox International

Hiscox International comprises our businesses located in Bermuda, Guernsey and the US. The businesses faced quite different challenges in 2009:

— **Bermuda**: Had a fantastic year. Its primary focus is property catastrophe insurance. After shrinking its top line in 2008, it responded aggressively to the rebounding rates and grew by 24.2% to $262.9 million (2008: $211.7 million). We also created a healthcare insurance and reinsurance team, who will focus on catastrophic exposures in the medical sector. In addition, we are building a small portfolio of catastrophe bonds issued by insurers and others. As this is an alternative route to assuming catastrophe risk we regard this as an extension of our reinsurance underwriting business and consider it when we look at our aggregate exposure to insurance events. During the year Charles Dupplin assumed leadership of Hiscox Bermuda from Robert Childs, its founding CEO. Robert and a small team went to Bermuda in late 2005. Since then Hiscox Bermuda has underwritten $943 million of premium income, generated significant profits and grown the balance sheet from $500 million (of which $200 million was borrowed) to $1 billion before paying a dividend to the Group at the end of 2009. This is a fantastic achievement and one for which we are all very grateful.

— **Hiscox Guernsey**: Had another good year. Its focus is on kidnap and ransom, piracy, fine art and terrorism. Premiums grew considerably, particularly in the piracy sector, due to the increased threat around the Horn of Africa. Our success is a reflection of both our risk appetite and our excellent client service. Our team in Guernsey is able to provide a quote, confirm cover, issue a policy and collect the premium in a few hours. This is a testament to the good cooperation between its underwriting and operations teams. Looking forward we see Guernsey continuing to be the leader for the Group in the kidnap and ransom and piracy areas. The Guernsey fine art book saw a small reduction in size due to the reduction in values of insured works.

— **Hiscox USA**: Saw a year of dramatic expansion. We took advantage of the broader financial difficulties in 2008 and set out on an ambitious plan to attract quality staff. We were able to hire seasoned experts in inland marine, property, construction, terrorism, kidnap and ransom and media, among other lines. We also opened new offices in Los Angeles, Boston, Miami, Atlanta and Kansas City, and expanded our existing offices in San Francisco, Chicago, New York City and Armonk. In all we recruited 84 people, pushing our total headcount up to 184 people.

In order to provide the clarity of focus to accompany our big investment, we created a single US business, merging the New York based London Market activities with our smaller ticket professional lines business. Richard Watson has moved to the US to head up the overall business. Ed Donnelly continues as President of our activities and will drive forward our specialist lines and all of our branch offices. Under Ed's leadership our smaller ticket professional lines activities reached break even in 2008, and we believe that working together, Ed and Richard will build a very successful business.

Hiscox International

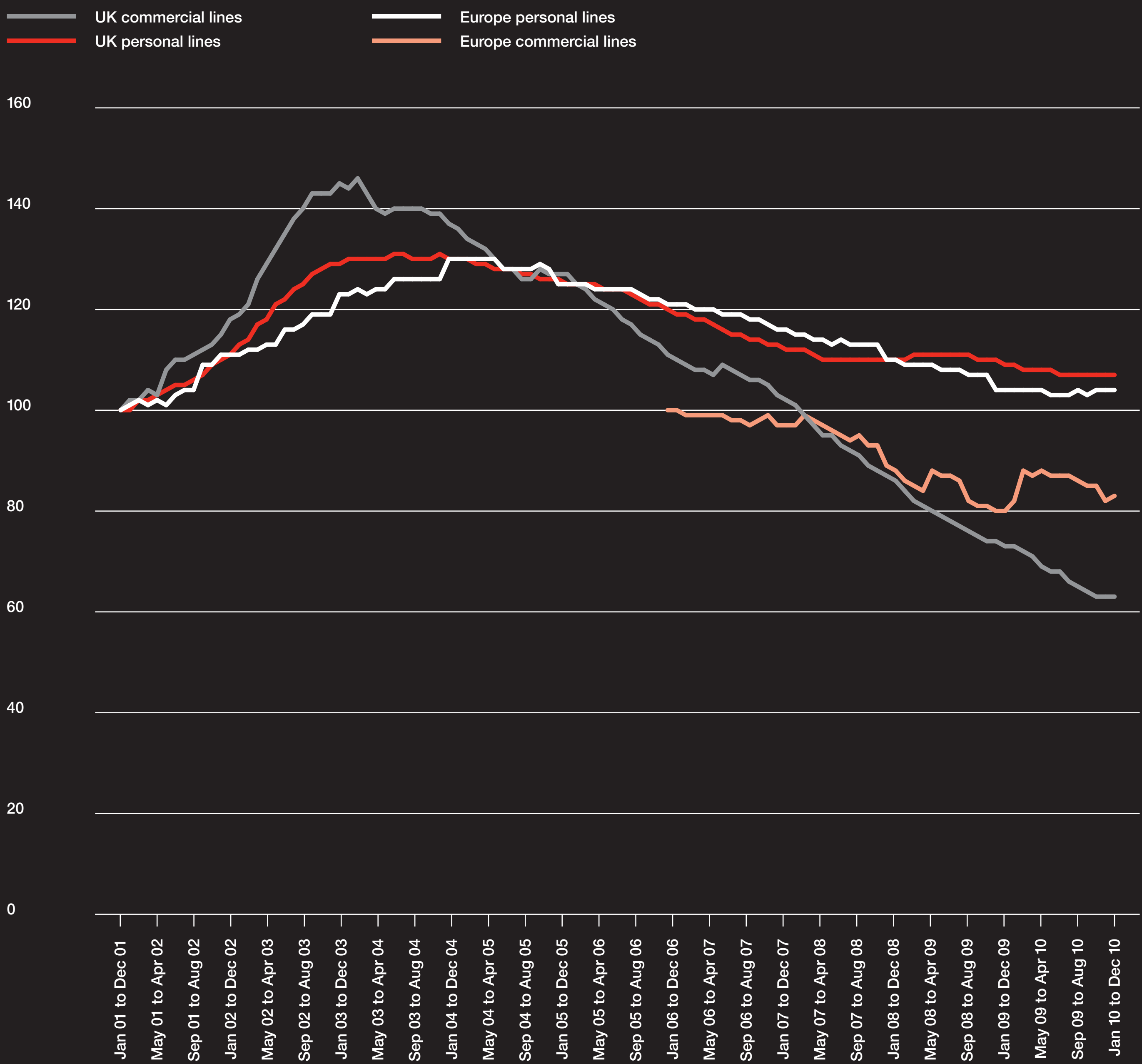
	2009 £m	2008 £m
Gross premiums written	**351.4**	244.4
Net premiums earned	**277.5**	197.0
Underwriting profit	**59.5**	34.8
Investment result	**57.7**	(8.4)
Foreign exchange	**7.0**	(22.1)
Profit before tax	**124.2**	4.3
Combined ratio	**76.3%**	93.1%
Combined ratio excluding foreign exchange	**78.6%**	82.5%

We have also worked hard to develop new products for both the surplus lines and the admitted market. In the surplus lines market there is great flexibility in pricing and wording. In the admitted market, advance approval of rates, forms and underwriting guidelines is required in each US state before launching a new product. Gaining approval has taken far longer than we had anticipated, but we are making steady progress.

Although Hiscox USA grew its top line to $162.1 million, up 24.6% (2008: $130.1 million), this growth was less than we had budgeted, as the anticipated upturn in the US domestic market did not occur. Our response has been to call a temporary halt to expanding our product range and to focus in 2010 on marketing those products we have already developed. We are confident this is the right way to improve the underlying financial performance of the business.

Investment returns
In 2009 we made a tremendous return on our investments. David Astor, our Chief Investment Officer, steered our portfolio very effectively through the financial crisis and kept his nerve when many others panicked. His courage was rewarded with an outstanding investment income result of £182.8 million, a return of 7.2% on invested assets (2008: -£27.6 million; -1.3%). This was achieved by maintaining a well spread portfolio, comprising corporate bonds, quality

Hiscox UK and Europe rating index
Index level (%). 12 month rolling period



Chief Executive's report continued

mortgage securities, an allocation to risk assets and a safe allocation to cash and Government bonds. Our caution towards complex products helped us to avoid the worst in 2008 and, as our portfolio recovered in 2009, we saw much better returns. We expect interest rates to remain low for at least the next year. With this in mind, we have reduced the duration of our Government bond portfolio but continue to retain a good allocation to credit, mostly through corporate bonds and to some exposure to mortgage and asset backed products. Whatever we do, we do not expect, in a world of 0.5% to 1.0% returns on short-term Government bonds, to see an investment return this year of the same level that we enjoyed in 2009.

Claims
In 2009 we handled a higher volume of claims than in 2008, reflecting our growing retail business. In addition to this everyday business, the team has also been working harder on recoveries, subrogating against third-parties and making a major contribution to Hiscox UK's 'Get Fit' efficiency programme. They have achieved all of this while maintaining very high levels of customer satisfaction. In 2010 we will make a significant investment in upgrading our claims handling systems for the London Market. Hiscox is a supporter of the move to electronic claims, but current systems require multiple data entry. We will be addressing this obvious inefficiency. A source of deep concern to us is the new Lloyd's Claims Transformation Project. We support the move to choice of service provider on more complex claims, but we believe strongly that Lloyd's customers expect a centralised, coordinated approach to enable their non-complex, standard claims to be paid speedily and efficiently. We fear the new scheme has the potential to create a damaging free-for-all in claims that threatens to tarnish the Lloyd's brand. We have objected to this aspect of the scheme from inception and we hope that sense will prevail before its final implementation.

Operations and IT
The future efficiency and competitiveness of this business depends on effective IT and efficient operations. Michael Gould, our Group COO, and his team have replaced our 15 year-old London Market system during 2009. During 2010 we will continue to invest in the new system, to make all of the post-implementation tweaks and improvements that our underwriters and operations people have requested. We are also designing and developing a new system for our retail businesses which will be first tested in Guernsey and then implemented across all our retail activities. This will make it easier to roll out new products and drive down our expense ratio. As part of the development process Michael will be driving us to adopt lean processes – applying manufacturing concepts to the operating approach of our business.

Capital management
The financial crisis has graphically illustrated how success in financial services depends on balancing expected return against perceived risk, while holding sufficient capital to protect against disaster. The challenge for outsiders is that while insurers' revenue and capital are very visible, the amount of risk they are taking is not. We have tried to make our risk profile clear to shareholders by publishing our expected losses using Realistic Disaster Scenarios promulgated by Lloyd's and by publishing a 'box plot and whisker' chart on our website. The 'box plot' chart gives the likely range of possible losses for Hiscox from major industry events.

The individual catastrophic losses are examined alongside an analysis of all the Group's expected losses, as well as our forecast investment returns and expenses, to arrive at a comprehensive view of our risk profile.

This picture of our risk profile enables us to have a debate on our risk appetite, which is then agreed by the Board. Everyone is aware that if our expected underwriting margins fall, or forecast investment returns decrease, we are confronted with a choice: either we are forced to take less risk or we need to have more capital.

In 2010 we expect our investment returns are likely to be much lower than in 2009. On the underwriting side we expect prices will remain at attractive levels. Therefore, in order to allow us to continue to take the same risk in 2010 as we did in 2009, we need to hold more capital in the business. This means that in 2010 the level of capital we will hold against our premium income will increase.

We look at this balance of expected return, risk and capital every quarter and make minor course adjustments accordingly. Once a year, ahead of the 1 January renewal season, we have a major review of our risk strategy and, if required, make our major course corrections then.

People
Insurance remains a business in which intellectual capital is as important as financial capital as a prerequisite for success. That we were able to reshuffle our senior management in 2009 without having to look outside to fill any of these roles is a testament to the growing strength of our management cadre. This greater strength is what gives me confidence that we will be able to continue to improve our performance as the Group grows and develops.

We have continued to invest in training and development and we are always on the lookout for high quality recruits. In 2009 we relaunched our graduate recruitment programme, and, as a result of the meltdown in other parts of the financial sector, we recruited slightly more graduates than we had expected. The programme is continuing in 2010.

Conclusion and outlook

We are optimistic for the year ahead. 2009 was a great year, combining excellent underwriting profits and investment returns. 2010 may not be as memorable a harvest but has good prospects, despite the continuing fallout from the financial markets crisis and the deepest global recession in living memory. We expect to see modest growth thanks to the expansion of our retail activities in Europe, the UK and the US and, provided major losses fall within our expectations, we expect to continue to deliver good returns for our shareholders and staff.

Bronek Masojada
Chief Executive
1 March 2010

Hiscox locations

Bermuda	Europe	Guernsey	UK	USA
Hamilton	Amsterdam	St Peter Port	Birmingham	Armonk (New York)
	Bordeaux		Colchester	Atlanta
	Brussels		Glasgow	Boston
	Cologne		Leeds	Chicago
	Dublin		London	Geneva (Illinois)
	Hamburg		Maidenhead	Kansas City (Missouri)
	Lisbon		Manchester	Lexington (Kentucky)
	Lyon			Los Angeles
	Madrid			Miami
	Munich			New York City
	Paris			San Francisco
	Stockholm			

Hiscox at a glance

Hiscox Ltd

Hiscox London Market

Hiscox International

Hiscox UK and Europe

Hiscox London Market

Russell Merrett
Managing Director

- Reinsurance
- Property
- Marine and energy
- Specialty
- Kidnap and ransom
- Terrorism
- Political risks
- Errors and omissions
- Aerospace

Hiscox Bermuda

Charles Dupplin
Chief Executive Officer

- Global reinsurance
- Group capital support
- Healthcare insurance

Hiscox Guernsey

Steve Camm
Managing Director

- Fine art
- Kidnap and ransom
- Terrorism

Hiscox USA

Richard Watson
Chief Executive Officer

- Errors and omissions
- Directors and officers' liability
- Specialty
- Kidnap and ransom
- Terrorism
- Technology/media
- Property

Hiscox UK

Steve Langan
Managing Director

- Fine art
- High-value household
- Errors and omissions
- Directors and officers' liability
- Specialty commercial
- Technology/media
- Direct to customer household and commercial business

Hiscox Europe

Pierre-Olivier Desaulle
Managing Director

- Fine art
- High-value household
- Errors and omissions
- Directors and officers' liability
- Specialty commercial
- Technology/media
- Kidnap and ransom
- Terrorism

Hiscox London Market
Hiscox London Market underwrites insurance and reinsurance business around the world. It uses the Lloyd's of London broker network and licenses to participate on some of the world's largest and most complex risks, as well as the simpler and more traditional ones, that come to Lloyd's.

Gross premiums written (£m)	663.0
Profit before tax (£m)	179.9
Combined ratio (%)	78.8

Security
Hiscox Syndicate 33 has an A (Excellent) syndicate rating from A.M. Best. It also benefits from Lloyd's own ratings, A (Excellent) from A.M. Best, A+ (Strong) from Standard & Poor's and A+ (Strong) from Fitch.

Location
London.

Capacity
Hiscox increased the 2010 capacity for Syndicate 33 to £1 billion (2009: £750 million); Cougar Syndicate 6104 to £45 million (2009: £43 million); and Syndicate 3624, which is a wholly owned syndicate, to £150 million (2009: £80 million).

Hiscox International
Hiscox International consists of Hiscox Bermuda, Hiscox Guernsey and Hiscox USA.

Gross premiums written (£m)	351.4
Profit before tax (£m)	124.2
Combined ratio (%)	76.3

Security
Hiscox Insurance Company (Bermuda) Limited has an A (Excellent) rating from A.M. Best and an A (Strong) rating from Fitch. Hiscox Insurance Company (Guernsey) Limited has an A (Excellent) rating from A.M. Best and an A (Strong) rating from Fitch. Hiscox Insurance Company Inc. has an A (Excellent) rating from A.M. Best.

Hiscox Bermuda
Hiscox Bermuda underwrites a variety of reinsurance business including catastrophe, risk excess of loss, and healthcare insurance, as well as providing Group capital support.

Hiscox Guernsey
Hiscox Guernsey specialises in fine art, kidnap and ransom, terrorism and piracy insurance.

Hiscox USA
Hiscox USA opened in 2006 and underwrites a mix of specialty, casualty and property business.

Locations
Bermuda, Guernsey, USA – Armonk (New York), Atlanta, Boston, Chicago, Geneva (Illinois), Kansas City (Missouri), Lexington (Kentucky), Los Angeles, Miami, New York City, San Francisco.

Hiscox UK and Europe
Hiscox UK and Europe underwrite local specialty insurance from 20 different regional centres across Europe. Business is sourced mainly through brokers however some household and commercial products are offered directly to the customer via internet and telephone.

Gross premiums written (£m)	421.0
Profit before tax (£m)	20.5
Combined ratio (%)	105.1

Security
Hiscox Insurance Company Limited has an A (Excellent) rating from A.M. Best, an A (Strong) rating from Standard and Poor's, and an A (Strong) rating from Fitch.

Locations
UK – Birmingham, Colchester, Glasgow, Leeds, London, Maidenhead, Manchester. Europe – Amsterdam, Bordeaux, Brussels, Cologne, Dublin, Hamburg, Lisbon, Lyon, Madrid, Munich, Paris, Stockholm.

People

The quality of our people has been a key ingredient in our success in this highly competitive, cyclical market. Hiscox's reputation for innovation and dynamism has been built in large part on the energy, commitment and expertise of our employees.

A good reputation takes a long time to build, but can be lost very quickly. We place a great emphasis on recruiting the best people, developing their skills and careers and ensuring that they are motivated. Some of the specific actions we take to fulfil each of these principles are described below.

The unique personality of Hiscox is expressed through our employees to our clients. We want customers to find us intelligent but not intellectual, bold but not arrogant, thought provoking but not patronising, different while being straight-forward, positive but not pushy, contemporary not stuffy, sophisticated but not superior.

1. Recruit the best

Hiscox aims to fill posts by recruiting internally, where possible. Because we strive to attract and retain the best people, we believe we have the ideal candidates for many jobs already working in the firm. We also want to stretch our people so they can reach their full potential. In 2009, 118 new appointments were either internal promotions or recommendations from current employees. When we do recruit talent from outside, we ensure that they go through a thorough assessment. In 2009, we recruited ten graduate trainees into the UK. In 2010, we plan to extend this to Bermuda and continental Europe. This combined with our very successful internship scheme will provide us with another source of talent to fill senior roles in the future. The average number of candidates seen for each job we filled in 2009 was four.

2. Develop excellence

Hiscox has a unique underwriting training programme developed by some of our very experienced underwriters. The training, which aims to reinforce Hiscox's underwriting standards, includes how to underwrite profitably across the cycle and the importance of learning the lessons of history when assessing risks. We also want to instill in our underwriters a restless curiosity, to challenge convention and not simply to accept a practice because that is the way it has always been done in the past. A total of 338 delegates completed this training programme in 2009.

3. Motivate

Having attracted and trained the best people we can find, it is then essential that we keep them motivated and ensure they thrive in their roles.

The Hiscox Partnership

Senior staff members who have made an important contribution to the Group's success may be appointed as a Hiscox Partner. The Hiscox Partnership, which numbers up to 5% of the total number of staff, is informed of all the strategic decisions and facts and figures of the Group, which enables them to influence the direction and performance of the Group. They also act as mentors to talented young people and ensure that we are operating in a way which is consistent with our values everywhere in the Group. In 2009 five new Partners were appointed.

Employee engagement survey

In September, Hiscox conducted its second global employee engagement survey. The survey, which was open to all permanent members of staff, looked at how committed employees feel to Hiscox, their managers, their teams and their role.

The idea behind it is simple: if employees feel very engaged they are more likely to stay and deliver their very best for the company. Being able to measure levels of commitment enables Hiscox to identify areas where it can improve performance and boost staff retention.

The survey is based on four key measurements:
- emotional commitment – the extent to which employees value, enjoy and believe in their work, in their manager, team and Hiscox;
- rational commitment – the extent to which employees believe Hiscox, their managers, and their teams have their best professional and development interests at heart;
- discretionary effort – employees' willingness to go above and beyond what is expected of them; and
- intention to stay.

The survey shows Hiscox enjoys high employee engagement and we consistently outscore the global benchmark set against 113 organisations across 58 countries. Our intent to stay rating was better than 95% of other firms.

1,116

Total number of staff at December 2009

Hiscox Partners

Stephen Ashwell	Global Head, Terrorism
David Astor	Chief Investment Officer
Neil Bolton	Head of US Casualty, Hiscox USA
Stuart Bridges	Chief Financial Officer
Amanda Brown	Group Human Resources Director
David Bruce	Deputy Managing Director, Hiscox London Market Head of Specialty, Hiscox London Market
Steve Camm	Managing Director, Hiscox Guernsey
Glenn Caton	Director of Marketing, Hiscox UK Head of Direct, Hiscox UK
Robert Childs	Chief Underwriting Officer
Robert Davies	Global Head, Kidnap and Ransom
Pierre-Olivier Desaulle	Managing Director, Hiscox Europe
Ed Donnelly	President, Hiscox USA
Charles Dupplin	Chief Executive Officer, Hiscox Bermuda Group Company Secretary
Michael Gould	Chief Operating Officer
Gary Head	Chief Underwriter, Hiscox UK
David Henderson	Branch Manager, Birmingham, Hiscox UK
Robert Hiscox	Chairman
Jason Jones	Group Compliance and Audit Director
Suzanne Kemble	Global Head, Media and Entertainment
Kevin Kerridge	Head of Direct, Hiscox USA
Ian King	Reinsurance Underwriter, Hiscox London Market
Steve Langan	Managing Director, Hiscox UK, and Group Marketing Director
Paul Lawrence	Head of Property Division, Hiscox London Market
Ian Martin	Finance Director, Hiscox London Market
Bronek Masojada	Chief Executive
Russell Merrett	Managing Director, Hiscox London Market
Jeremy Pinchin	Group Claims Director
Steve Quick	Global Head, Broker Relations
Robert Read	Global Head, Fine Art
Bruno Ritchie	Head of Aerospace and Global Risks Europe, Hiscox London Market
Christopher Sharpe	Chief Underwriter, Hiscox Bermuda
Nicholas Thomson	Retired Chief Underwriting Officer
Gavin Watson	Chief Financial Officer, Hiscox USA
Richard Watson	Chief Executive Officer, Hiscox USA
Simon Williams	Head of Marine and Energy, Hiscox London Market

Group financial performance

Post-tax return on equity increased to 30.1% (2008: 9.2%). Robust underwriting profits combined with a strong investment result assisted in growing the net asset value per share by 15.9% to 299.2p (2008: 258.1p). Gross premiums written increased by 25.1% reflecting an increase in rates for reinsurance and aided by the strong US Dollar. Profit before tax increased to £320.6 million (2008: £105.2 million) resulting in an increase in earnings per share to 75.2p (2008: 18.8p). Total dividend per share for the year increased by 17.6% to 15p (2008: 12.75p).

A good underwriting result combined with a strong investment return due to the rally in the investment markets, contributed to the Group's record profits.

Included within the Group's profits are foreign exchange losses of £25.6 million reversing part of the £109.8 million gain recorded in the prior year. In addition, inherent within the underwriting result is the foreign exchange impact of the non retranslation of non monetary items. This resulted in a loss for the year of £53.2 million (2008: £36.1 million gain). Retranslation of non monetary items at year end rates of exchange

30.1%
Return on equity

Group financial performance

	2009					2008 Restated*				
	London Market	UK and Europe	International	Corporate Centre	Total	London Market	UK and Europe	International	Corporate Centre	Total
Gross premiums written (£m)	663.0	421.0	351.4	–	1,435.4	545.9	357.1	244.4	–	1,147.4
Net premiums written (£m)	483.6	391.5	281.9	–	1,157.0	363.1	329.1	206.2	–	898.4
Net premiums earned (£m)	453.3	367.3	277.5	–	1,098.1	427.8	303.3	197.0	–	928.1
Investment result – financial assets (£m)	80.9	34.9	57.8	9.2	182.8	(5.5)	(11.9)	(8.4)	(1.8)	(27.6)
Investment result – derivatives (£m)	(1.2)	2.0	(0.1)	(0.3)	0.4	–	(10.5)	–	(42.5)	(53.0)
Profit/(loss) before tax (£m)	179.9	20.5	124.2	(4.0)	320.6	137.0	31.8	4.3	(67.9)	105.2
Claims ratio (%)	38.8	53.4	33.0	–	41.8	61.2	42.2	44.6	–	52.7
Expense ratio (%)	32.2	49.9	45.6	–	40.4	33.3	50.1	37.9	–	38.9
Foreign exchange impact (%)	7.8	1.8	(2.3)	–	3.8	(28.7)	(10.7)	10.6	–	(16.3)
Combined ratio (%)	78.8	105.1	76.3	–	86.0	65.8	81.6	93.1	–	75.3

*During the year, following a new geographic management structure including new business written through Syndicate 3624, the Group has changed its segmental reporting to provide more effective financial reporting for the evaluation of business segments by the chief operating decision maker to make decisions about future allocation of resources. Accordingly, the 2008 segmental comparatives have been restated in order to enable comparison of results by the user.

	2009	2008
Financial assets and cash** (£m)	2,660.6	2,522.4
Other assets (£m)	1,156.8	1,236.9
Total assets (£m)	3,817.4	3,759.3
Net assets (£m)	1,121.3	951.0
Net asset value per share (p)	299.2	258.1
Net tangible asset value per share (p)	285.7	244.9
Adjusted number of shares in issue (m)	374.8	368.5

**excluding derivative assets and catastrophe bonds.

Group financial performance continued

would result in a 4.3% improvement in the combined ratio (2008: 4.7% decline). The Group also recorded a foreign exchange loss of £69.6 million recognised directly in equity as a result of the retranslation of investments in its US Dollar operations.

The underwriting performance for each reporting segment is detailed below.

Segmental performance

During the year, following a new geographic management structure, the Group changed the way it reports its segments. The comparative information has been adjusted accordingly.

Hiscox London Market

Hiscox London Market comprises the results of Syndicate 33, excluding the result of fine art, UK regional events coverage and non US household business which is included within the results of UK and Europe. In addition, it excludes the larger TMT business which is allocated to the International segment and an element of kidnap and ransom and terrorism included in UK and Europe.

- Gross premiums written increased by 21.5% to £663.0 million (2008: £545.9 million) reflecting the strength of the US Dollar exchange rate. In original currency, gross premiums written were comparable with the prior year as rates in reinsurance and marine and energy increased, offset by our deliberate reduction in certain areas where rates were less favourable including US property.
- The reinsurance outwards spend was comparable to the prior year and reinsurance contracts with commercial reinsurers were renewed during the year with similar terms. The quota share arrangement with the Cougar Syndicate remained in place.
- A positive investment return of £80.9 million (2008: £5.5 million negative) was recognised as the Group benefited from the rally in the markets.
- The claims ratio improved significantly to 38.8% compared with 61.2% in the prior year due to a benign year for catastrophe losses and favourable developments in some older years.
- The resulting combined ratio excluding the impact of foreign currency movements improved to 71.0% (2008: 94.5%).
- Profit before tax for the year increased by 31.3% to £179.9 million (2008: £137.0 million).

Hiscox UK and Europe

Hiscox UK and Europe comprises the results of Hiscox Insurance Company Limited, the results of Syndicate 33's fine art, UK regional events coverage and non US household business together with the income and expenses arising from the Group's retail agency activities in the UK and continental Europe. It excludes the results of the larger TMT business written by Hiscox Insurance Company Limited. It also includes an element of kidnap and ransom and terrorism written in Syndicate 33.

- Gross premiums written increased by 17.9% to £421.0 million (2008: £357.1 million) with growth coming from all core lines especially the direct business and the professional and commercial specialty area. It was aided by the strong Euro exchange rate.
- Again, the investment result for the year improved significantly and a total return of £34.9 million, excluding derivatives, was achieved (2008: £11.9 million negative).
- The claims ratio declined by 11.2% to 53.4% due to a number of large unrelated claims in Europe including the impact of Windstorm Klaus and the 'freeze' losses experienced early in the year. The combined ratio, before the impact of foreign exchange, also deteriorated by 11% to 103.3%.
- Profit before tax for the year decreased to £20.5 million (2008: £31.8 million).

Hiscox International

Hiscox International comprises the results of Hiscox Insurance Company (Guernsey) Limited, Hiscox Insurance Company (Bermuda) Limited, Syndicate 3624, Hiscox Inc. and Hiscox Insurance Company Inc.. It also includes the results of the larger TMT business written by Hiscox Insurance Company Limited and Syndicate 33.

- Gross premiums written increased by 43.8% to £351.4 million (2008: £244.4 million). Growth in original currency was 22.0% reflecting increased rates and levels of reinsurance written in Bermuda, increased demand for piracy products in Guernsey and our continued expansion in the US.
- The investment return increased significantly to £57.8 million profit (2008: £8.4 million loss) consistent with the overall increase in the total investment return for the Group.
- The claims ratio improved by 11.6% to 33.0% (2008: 44.6%) reflecting a quiet year for catastrophe losses in Bermuda and recognising good loss experience in Guernsey.

£320.6m

Profit before tax

- The expense ratio deteriorated by 7.7% to 45.6% as a result of continued expansion costs to take advantage of opportunities in the US.
- Profit before tax increased significantly to £124.2 million (2008: £4.3 million).

Hiscox Corporate Centre
Hiscox Corporate Centre comprises the investment return, finance costs and administration costs associated Group management activities. Corporate centre also includes the majority of foreign currency items on economic hedges and intragroup borrowings.

- The investment result improved significantly to £9.2 million profit (2008: £1.8 million loss), an improvement experienced across all segments.
- Total expenses including certain foreign exchange items have decreased by 54.7% to £8.7 million (2008: £19.2 million). Included within foreign exchange gains of £10.3 million (2008: £9.0 million loss) is the foreign currency impact on certain intragroup loan balances.
- The resulting loss before tax in Corporate Centre improved significantly to £4.0 million (2008: £67.9 million). In the prior year, the Group recorded a derivative loss of £42.5 million in protecting currency translation gains recognised directly in equity.

Cash and liquidity
The Group's primary source of liquidity is generated from premium income and income received on investments. Funds received are used predominantly to pay claims, expenses, reinsurance, increase investments and to pay dividends and taxes.

Total net cash outflows for the year were £150.1 million (2008: inflow £75.8 million).

The outflow for the year is driven mainly by the settlement of 2008 losses, payment of expenses, the payment of dividends and the settlement of the derivative contracts which were outstanding at the end of 2008. In addition, the decrease also represents the strategic decision by the Group to increase its returns by investing surplus cash balances into its fixed interest portfolio.

Net cash outflows from investing activities for the year were £11.7 million (2008: £16.7 million). The cash outflow is primarily as a result of the purchase of tangible and intangible assets. The Group did not acquire any new subsidiaries or associates during the year.

Net cash inflows from financing activities for the year were £1.6 million (2008: outflow £108.5 million). The inflow is due to an increase in the borrowing facility offset by the payment of dividends. The Group did not enter into any share buy-back programmes in the current year. In 2008 the Group spent £62.9 million for the purchase of shares held in treasury and £2.2 million for the purchase of shares held in trust.

The Group maintains relationships with a limited selection of banks who are monitored for their credit status and ability to meet the day-to-day banking requirements of the Group.

There were no impairments recorded against cash or cash equivalents and no recoverability issues have been identified on such assets.

The Group has a secured revolving credit facility for a total of £350 million which may be drawn by way of cash or Letter of Credit or a combination thereof providing that the cash portion does not exceed £200 million. The facility may be drawn in any foreign currency at the request of the Group. As at 31 December 2009, $225 million was drawn by way of Letter of Credit and £138 million by way of cash (2008: £137.5 million and $130.0 million respectively).

Solvency II
Solvency II is the new solvency regime for all EU insurers and reinsurer which is due to come into effect from 2012. The new regime aims to implement solvency requirements that are consistent across all member states and which better reflect the risks that insurers and reinsurers face.

The new regime is based on a three-pillar approach as follows:
Pillar 1 – Quantitative requirements
Pillar 2 – Government and risk management requirements
Pillar 3 – Disclosure and transparency requirements.

A working group has been established to lead the implementation of the new regime and a comprehensive implementation plan is in place with performance and execution ongoing. Many of the qualitative requirements already form an integral part of the Group's risk management framework and a gap analysis has been performed in order to identify those areas which may require small incremental changes.

The Group is seeking approval for its own internal models and is in a firm position to ensure that the Solvency II requirements will be implemented successfully, however uncertainty still exists as the full details of the regime are yet to be confirmed.

7.2%
Investment return

Group financial performance continued

£2.66bn
Invested assets

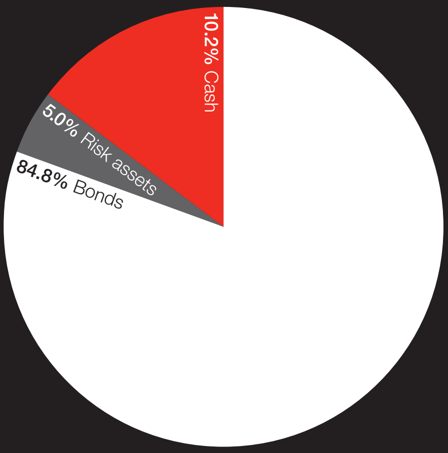
Group investment performance

		31 December 2009				31 December 2008	
		Asset allocation %	Return %	Return £000	Asset allocation %	Return %	Return £000
Bonds	£	19.1	3.5		11.6	5.3	
	US$	58.6	9.2		54.7	(2.5)	
	Other	7.1	6.8		10.2	3.1	
Bonds total		84.8	7.7	152,954	76.5	(0.3)	(4,027)
Equities		5.0	20.7	26,360	5.0	(28.4)	(38,267)
Deposits and cash equivalents		10.2	0.8	3,455	18.5	3.7	14,662
Actual return			7.2	182,769		(1.3)	(27,632)
Group invested assets*				£2,660.6m			£2,522.4m

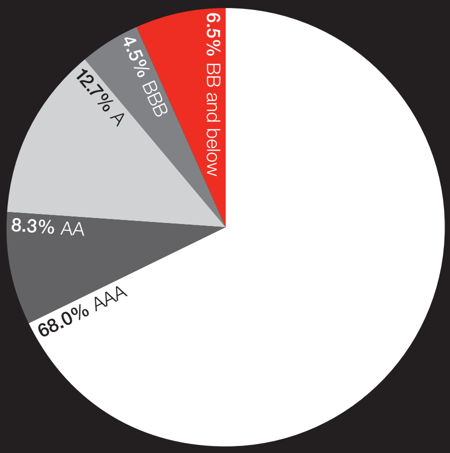
*excludes derivatives and investment in catastrophe bonds.

High quality and well diversified portfolio
Investment portfolio: £2,660.6m

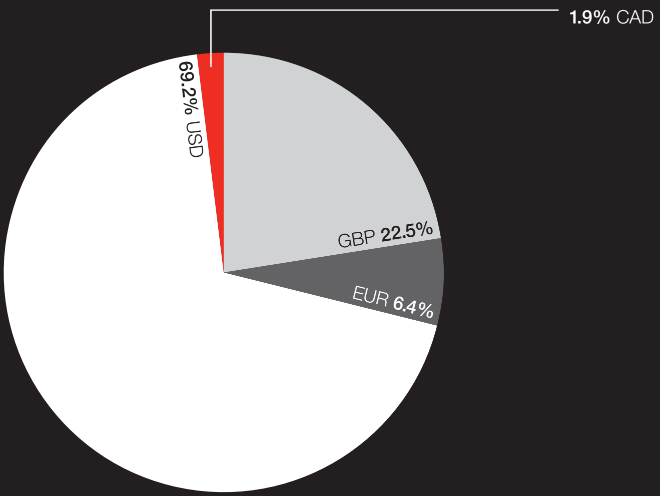
Asset allocation



Bond credit quality



Bond currency split



Group investments

The Group's invested assets increased slightly to £2.66 billion (2008: £2.52 billion) as positive cashflows offset the effect of the decline in the US Dollar against the Pound. The investment return, excluding derivative positions, amounted to £182.8 million (2008: £27.6 million negative).

The last two years have witnessed dramatic events in the investment world. Each one, in a very different way, has turned out to be extremely interesting and indeed challenging. Having survived 2008, there was no let up in early 2009, as volatility and uncertainty continued to grip markets. Whilst there was temptation to de-risk further during the periods of greatest uncertainty, the robustness of our balance sheet and the strength of cashflows from the bond portfolio meant that such a move was not required. Additionally, rigorous stress testing and monitoring of the underlying securities confirmed that the prices available in the market for many of our bonds bore little relevance to their fundamental value. Throughout the year payments of principal and interest were as expected. It is therefore pleasing to report that the Group has benefited from holding on to those securities that were heavily discounted in value at the end of 2008 and into the first quarter of 2009. What has been more of a surprise is the speed at which they have returned towards par, making up for most of last year's losses. This, of course, has been made possible by the extraordinary monetary conditions that have prevailed and the scale of Government measures deployed in order to restore liquidity and confidence in the various markets.

As a degree of calm and rationality has been restored, improved valuations for securitised bonds boosted our US Dollar portfolios. Similarly, financial bonds in our Sterling and Euro portfolios recovered once it became clear that the authorities were unlikely to let strategically important banks fail. This did not stop prices for subordinated paper being marked down, but our exposure to the lower parts of the capital structure was minimal.

With interest rates at low levels and liquidity improving, investors have had more confidence to seek yield. The portfolio, where we continued to increase our exposure to credit during the year, was well positioned for the resulting narrowing of credit spreads. Even modest allocations to high yield and other credit opportunities contributed significantly to our overall returns. Whilst the Group's allocation to corporate bonds has increased from 20% to 25% during the year, safety and liquidity have remained a high priority and the percentage of the portfolio held in cash and Government supported debt was maintained at around 60%. We are extremely focused on not jeopardising the Group's capacity to underwrite and pay claims.

Our risk assets performed well and added materially to the Group's investment return. Given the strength of equities since their lows last March we reduced our exposure in the third quarter, maintaining our allocation at 5% of assets. The pace of the recovery, and hence this year's strong returns, clearly has an impact on the prospects for our portfolio going into 2010. Whilst strong cashflows provided comfort during the crisis they will serve as a drag on yield as they are reinvested at the rates prevailing in the markets. These low rates in turn have a bearing on our risk appetite given our desire not to lose money in any one year. At current market levels any meaningful increase to equities is unlikely in the short-term. Whilst the best of the rally in risk markets may therefore be behind us, we continue to see value in the corporate bond market, but remain wary of the threat of higher interest rates. Government bonds in particular seem over priced, and there is unlikely to be a shortage of supply any time soon. We are keeping the duration of the main bond portfolios correspondingly short.

We anticipate that volatility will continue and that patience will be required as Governments remove their support and interest rates move to more normal levels. The price of this patience will be lower investment yields in the immediate future.

Risk management

The risk management framework extends to all aspects of risk including insurance, market, credit, operational, liquidity, environmental, ethical and strategic risks. The core business of Hiscox is dealing with risk. The understanding of risk is intrinsic to every level of decision-making in the Group.

The risks associated with the core business represent some of the greater exposures, however the Group is exposed to a number of other risks and has systems and procedures to identify and manage them. These procedures are regularly reviewed and improved in the light of the changing risk environment and best practices. Risk appetite is set by the main Board and cascaded down into the Group's global operations as part of the business planning cycle and through various risk and operational committees. These are:

- Risk Committees
- Underwriting Review Group
- Reinsurance Purchase Review Group
- Reinsurance Security Committee
- Cash Flow Review Group
- Broker Credit Committee
- Investment Committee
- Reserving Committees
- Business Continuity Committee.

These committees are all chaired by either the Chief Executive, Chief Financial Officer or Chief Underwriting Officer and have specific areas of focus, such as underwriting, reinsurance purchase and security, liquidity, broker credit risk, investments, claims reserving and business continuity. Senior management responsibilities are clearly defined together with their reporting lines and the execution of delegated responsibilities is closely monitored by reporting to the Board and its committees. This monitoring, supported by financial and non-financial management information, assesses performance against agreed targets and objectives, as well as the risks to achieving these objectives and the effectiveness of the measures in place to manage these risks. In parallel with these direct risk management processes, there is a dedicated risk management function which, in conjunction with Internal Audit and the Group risk committees, monitors and reviews the effectiveness of risk management activities throughout the organisation and reports to the Board. These functions are organised centrally to assist in the integration of best practice throughout the Group. A range of risk management tools is used to assess and manage risk both at business unit level and on a Group-wide basis.

Major risks

The major risks that the Group faces are presented below. Detailed information on the major risks and uncertainties impacting the Group's financial statements is set out in note 3 to the financial statements.

Insurance

Catastrophe and systemic insurance losses

The Group continues to underwrite significant risks in geographical regions that are prone to natural peril. This business remains a compelling proposition for the Group since it is capable of returning good margins over the medium to long-term as the occurrence of catastrophes averages out. As with similar insurers, the Group's earnings are affected by unpredictable external events such as natural and other catastrophes, legal developments, social and economic change and the emergence of latent risks. Such events can create significant levels of underwriting losses. The Group manages its exposure to these risks through having a clearly defined risk appetite which dictates the business plan and is realised through disciplined underwriting, close and continuous monitoring of exposures and aggregations, and a prudent and disciplined reinsurance purchase programme to cap losses from risk concentrations.

Of critical importance is the quality of our underwriting models and risk aggregation capability. Incentives ensure that underwriting staff make sound and objective judgements that are aligned with the Group's overall strategic objectives and risk appetite. Clear authority limits are also in place that are regularly reviewed and monitored. Policy wordings are reviewed regularly by specialists and legal experts in the light of legal developments to ensure that the Group's exposure is restricted, as far as possible, to those risks identified at the time of policy issuance. The modelling and monitoring tools are used both in the underwriting process and by independent risk specialists. They are used to design the insurance and reinsurance programmes and control the business underwritten to ensure that the risk profiles of contracts match the exposures for which the programmes were devised.

Incentives ensure that underwriting staff make sound and objective judgements that are aligned with the Group's overall strategic objectives.

Risk management
continued

Aggregation and modelling resources are shared across the Group. Subsidiaries and locations worldwide therefore employ the same sophisticated standard of modelling tools tailored to the characteristics of each specific market. We also run realistic disaster scenario projections on a subsidiary and consolidated basis in order to estimate the potential loss across all books of business following a range of specific events. We adjust our business plan, target products and reinsurance programme to deliver a well-diversified book. This enables us to maximise expected risk/return on the portfolio as a whole and offset potential losses on the more volatile accounts.

Competition and the insurance cycle
In our markets, Hiscox competes against major international groups with similar offerings. At times, a minority of these groups may choose to underwrite for cash flow or market share purposes at prices that sometimes fall short of the break even technical price. The Group is firm in its resolve to reject business that is unlikely to generate underwriting profits. Accepting insurance risk below the technical price is detrimental to the industry's prospects, since it drives the prevailing rates in the market lower to the point where business failures occur, insurers' capital is destroyed, customers receive sub-optimal service and the industry suffers from negative publicity. As capacity levels in the market fall, prices inevitably rise until the point where the cycle of irrational pricing may begin again. In common with all insurers, the Group is exposed to this price volatility. Prolonged periods of low premium rating levels or high levels of competition in the insurance markets are likely to have a negative impact on the Group's financial performance.

To manage this risk, Hiscox alters its appetite for the lines of business and the layers it writes in response to market conditions and the risk appetite of the Group. Pricing levels are monitored on a continuous basis with detailed monthly reports showing current prices relative to exposure, trends over the past 12 months, and projections to the year end. The Group's cycle management strategy and related modelling and monitoring are essential to ensure that it quickly identifies and controls any accumulating adverse effects of changes. As the Group frequently acts as the lead insurer in the complex co-insurance programmes required to cover significant high value assets, it has some ability to set market rates rather than follow them.

Mutualisation is a related risk arising from the phenomenon of pricing cycles in the industry. The Group is required to contribute towards the obligations of other financial institutions who fail. Syndicates 33 and 3624 contribute to the New Central Fund operated by the Council of Lloyd's, and in the UK certain Hiscox entities contribute to the Financial Services Compensation Scheme (FSCS). Insurance companies may be asked to contribute to the recent claims on the FSCS from the banking industry, currently funded by the Treasury. Any such requests depend on the final level of claims from deposit holders (net of asset recoveries), the period of repayment demanded by the Treasury and the ability of the banks to make such repayments. The Group participates in many industry bodies, associations and task-force initiatives in order to monitor developments and influence their strategic direction. In particular, the continued involvement of the Group's executives in the reshaping of the Lloyd's market underscores that commitment.

Reserving
The Group establishes provisions for unpaid claims, defence costs and related expenses to cover its ultimate liability in respect of both reported claims and incurred but not reported (IBNR) claims. These provisions take into account both the Group's and the industry's experience of similar business, historical trends in reserving patterns, loss payments and pending levels of unpaid claims and awards, as well as any potential changes in historic rates arising from market or economic conditions. Details of the actuarial and statistical methods and assumptions used to calculate reserves are set out in note 27 to the financial statements. The provision estimates are subject to rigorous review and challenge by senior management from all areas of the business and the final provision is approved by the reserving committees. The provision is set above the expected or mean reserve requirement to minimise the risk that actual claims exceed the amount provided.

Binding authorities
Hiscox writes a considerable amount of premium income through agents to whom binding authority is given to accept risks on behalf of Hiscox Group carriers. All binding authorities are strictly controlled through tight underwriting guidelines and limits and extensive vetting, monitoring, and auditing of compliance. Agents to whom binding authorities are granted are regularly examined to ensure they meet the Group's minimum standards. These checks are performed by staff independent of the underwriting function and the process is overseen by a committee comprising both underwriters and non-underwriters from the senior management team and the Group Head of Internal Audit.

We adjust our business plan, target products and reinsurance programme to deliver a well-diversified book.

Credit

Reinsurance counterparties

The Group purchases reinsurance protection to limit its exposure to single claims and the aggregation of claims from catastrophic events. The Group places reinsurance with companies that it believes are strong financially and operationally. Credit exposures to these companies are closely managed by the Reinsurance Security Committee (RSC), which is chaired by the Group Finance Director. All reinsurers used must be approved by the RSC following an internal assessment of the company's financial strength, trading record, payment history, outlook and organisational structure, in addition to credit ratings granted by external agents. Approved reinsurers are monitored continuously to identify potential deteriorations as early as possible. Monitoring procedures include consideration of public information produced by reinsurers; the Group's experience of the reinsurers and their behaviour in the marketplace; and analysis from external consultants and from rating agencies. Credit limits are set for approved reinsurers both at a Hiscox Group level and for each underwriting subsidiary based on a defined risk appetite. The Group's experience of bad debts arising from its reinsurance arrangements has been minimal.

Operational and other key risks

Business continuity

The Group has taken significant steps to minimise the impact of business interruption that could result from a major external event. A formal disaster recovery plan is in place for both workspace recovery and retrieval of communications, IT systems and data. In the event of a major event, these procedures will enable the Group to move the affected operations to alternative facilities within very short periods of time. The disaster recovery plan is tested regularly and includes disaster simulation tests. Staff are widely distributed throughout the UK, Europe, USA, Bermuda and Guernsey. This geographical dispersion reduces the Group's exposure to natural or terrorist events that could prevent access to premises or loss of staff. In the event of a loss of staff, for example as a result of a pandemic, a plan is in place to re-assign key responsibilities and transfer resources to ensure key business functions can continue to operate.

Hiscox credit rating

The external ratings granted to the Group and its subsidiaries are essential to maintaining profitability, particularly in relation to our reinsurance business and managing the costs of financing and access to capital. We have identified the key aspects of our business which are critical to maintaining our ratings and closely manage these to minimise the risk of an event which might jeopardise any rating and to ensure that we respond appropriately to unforeseen external events. We maintain regular and open communication with our rating agencies to ensure that we continue to meet their expectations and that careful consideration is given to the potential impact on a rating of any significant decision.

Emerging risks

Being able to identify and plan for unexpected events has become an increasingly important component of our business cycle management. Emerging risk identification and control is therefore a core part of risk management activity in relation to all aspects of our business, including underwriting, operations and strategy. Significant efforts are made, including obtaining external expertise, to try to identify any threats to the business either actual or potential. For example, a change in US legislation may result in unintended risks being underwritten, or may require us to cease business in certain US states. The identification of emerging risks is a core agenda item in each Risk Committee. We take all reasonable steps to minimise the likelihood and impact of such events and to be prepared for their occurrence.

Capital

The Group manages capital rigorously in order to maximise its return on capital whilst maintaining sufficient levels of financial resources to absorb unexpected losses and meet the requirements of regulators and rating agencies. Accurate measurement of potential losses under various scenarios is a critical aspect of our business planning and capital management cycle. Potential losses are calculated regularly using the most sophisticated modelling techniques available supported by stress and scenario assessments. We invest heavily in the most up-to-date risk management techniques and in expert staff to ensure our procedures and analyses remain second to none.

Investments and foreign exchange

Investment policy

The investment policy is designed to maximise returns within the overall risk appetite of the Group which stipulates a one in 100 year loss tolerance. The overriding philosophy with the Group's assets is not to lose money or to put at risk the Group's capacity to underwrite. Short-term interest rates are likely to remain at historically low levels throughout 2010. As a result the possibility of losing money with a portfolio consisting of any assets other than cash or short-term Government securities is statistically greater than normal. Consequently the Board has agreed, in current market conditions, to set aside extra capital to support the recommended asset allocation and to provide a buffer against possible investment losses during the year.

Technical funds, the investments held for the payment of future claims, are primarily invested in high quality bonds and cash.

Emerging risk identification and control is a core part of risk management activity in relation to all aspects of our business, including underwriting, operations and strategy.

The high quality and short duration of these funds allows the Group to meet its aim of paying valid claims quickly. These funds are maintained in the currency of the insurance policy to reduce foreign exchange risk.

Due to the short-tail nature of the Group's insurance liabilities, the aim is not to match the duration of the assets and liabilities precisely. Benchmarks are instead set for the fixed income fund managers which approximate the payment profile of the claims as well as providing the managers with some flexibility to enhance returns.

A proportion of the Group's assets is allocated to riskier assets, principally equities. Here, it is the Group's philosophy to take a long-term view in search of acceptable risk adjusted returns. The proportion of the Group's funds invested in risk assets will depend on the outlook for investment and underwriting markets. An allocation within the risk assets is made to less volatile, absolute return strategies. This balances the desire to enhance returns against the need to ensure capital is available to support underwriting throughout any downturn in financial markets.

Foreign exchange

The US Dollar is the Group's largest underwriting currency. The Group's policy is to match US Dollar insurance liabilities with investments held in the same currency in order to minimise the effect of currency fluctuations. Whilst the Group's functional and reporting currency is Sterling, a significant proportion of the Group's operational cost base is located in the US and Europe, and movements in foreign exchange rates may have a material adverse effect on its financial performance and position. In addition the capital base of the Bermuda, Guernsey and US insurance companies are in US Dollars. Where appropriate a percentage of the capital will be held in the currency matching that of the underlying business being written. Net currency positions are closely monitored and currency hedging transactions are entered into where this is considered advantageous in the light of anticipated movements in exchange rates. Further details of the Group's investment profile and its management of currency risks are provided in notes 3 and 20 to the financial statements.

Liquidity

Liquidity risk is the risk of being unable to meet liabilities to customers or other creditors as they fall due, or the risk of incurring excessive costs in selling assets or having to raise finance in a very short period.

The majority of the Group's cash inflows and outflows are routine and can be forecast well in advance. The primary source of inflows is insurance premiums whilst outflows are to policyholders for claims made. Cash flow is forecast on rolling weekly, monthly and quarterly basis depending on the source, and, in the event of a major catastrophe, such forecasting may be up to three years in advance. Free cash is invested according to the Group's investment policy and cash requirements can normally be met through regular income streams (i.e. premiums or investment income), existing cash balances or realising investments that have reached maturity.

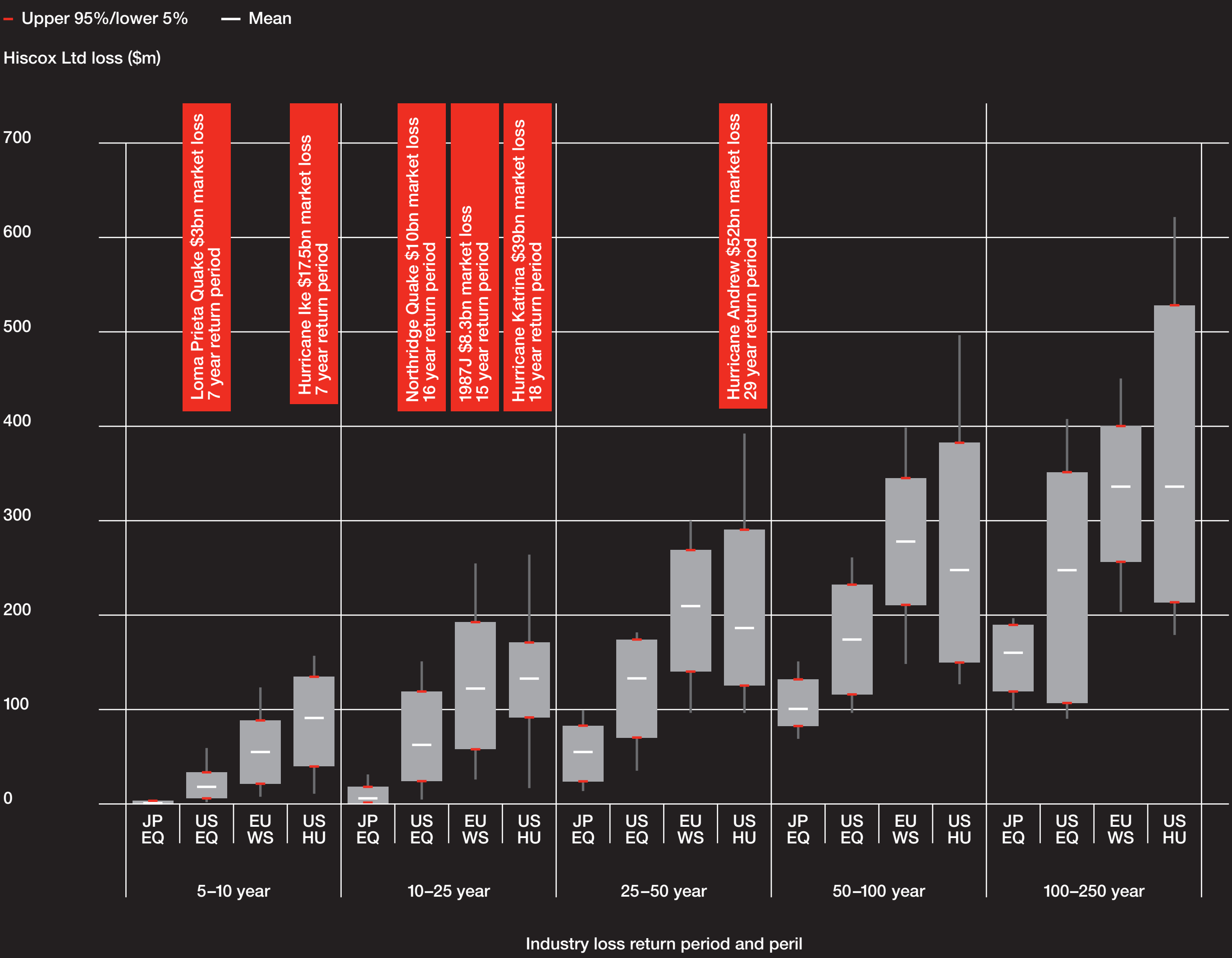
The Group's liquidity risk arises from large, unplanned cash demands and the principal source of risk is a major catastrophe resulting in a high value of claims. This could be exacerbated if we had to fund claims pending recovery from a reinsurance partner. We plan for this risk through a number of measures.

First, we run stress tests to estimate the size and timing of claims that might have to be paid in the event of a number of major catastrophes all occurring within a short period of time. We also run scenario analyses that consider the impact on liquidity of a range of adverse events happening simultaneously; for example, an economic downturn and declining investment returns combined with unusual levels of insurance losses.

Second, taking into account the stress and scenario analyses, we maintain extensive borrowing facilities. These are held with a diverse range of major international banks in order to minimise the risk of one or more being unable to honour their commitments.

Third, our investment policy recognises that some investments may need to be realised before maturity or at short notice and hence a high proportion of investments must be held in liquid assets. This minimises the risk of loss in the event of having to sell assets quickly. Using these measures we believe the likelihood of being unable to meet our liabilities, or of incurring excessive costs in doing so, to be extremely remote.

Boxplot and whisker diagram of Hiscox Ltd net loss (USD)



The chart above shows the variability in net loss the Group expects from individual losses of a given industry loss size.

The return period is the frequency at which an industry insured loss of a certain amount or greater is likely to occur. For example, an event with a return period of 20 years would be expected to occur on average five times in 100 years.

Corporate responsibility

"**Fundamental to corporate and social responsibility is honest and fair dealing in all activities of the Group. Hiscox has always been extremely conscious of its reputation. Management has always believed that a reputation for integrity and decent behaviour in all dealings, be they within the Group or with those from outside who come in contact with the Group, will be good for morale and for the results of the business.**"

Robert Hiscox

Hiscox's commitment to responsible business practices is reflected:

In the marketplace

Dealing with business partners
Insurance brokers are an important Hiscox stakeholder, and Hiscox endeavours to have good relationships with them to create a competitive advantage in the marketplace. Clear communication is key to good relations and Hiscox regularly sends partner brokers updates (electronically or in hard copy) to keep them informed of developments at Hiscox and in the industry.

Dealing with investors
In keeping with its policy of open and transparent communication, Hiscox reports both its half and full year results to its investors via a series of presentations as well as ensuring all relevant Group financial information is available on its website. In addition, senior management and key employees meet investors and analysts throughout the year to explain and take questions on the Group financial performance and business strategy.

Dealing with customers
Hiscox is dedicated to advising customers on risk management to prevent burglary and fire in the home and other distressing losses. Should a loss occur, the Hiscox UK philosophy is that insurance is a promise to pay, and the claims service aims to support customers and make them whole as soon as possible.

In the workplace

Hiscox wants to employ the best people and provide them with the means and the motivation to excel. This is achieved with fair rewards and by providing staff with an environment in which they can enjoy their work and reach their full potential. Hiscox recognises how important it is for employees to maintain a healthy work/life balance and gives staff the option of flexible and home working wherever possible.

Equal opportunities
Hiscox is committed to providing equal opportunities to all employees and potential employees in all aspects of employment regardless of disability, sex, race, religion, sexual inclination or background.

Rewards and benefits
Hiscox encourages employees to identify with the success of the Group through performance-related pay and bonus savings-related share option schemes and executive share option schemes. Competitive benefits packages contain health, fitness, flexible working and career break opportunities. Salary packages are benchmarked by Watson Wyatt against the financial services industry as a whole and against the Lloyd's market specifically, where applicable. Packages are also considered on a country-by-country basis.

Training and development
Hiscox is committed to training and developing its employees to help them maximise their potential. Each permanent member of staff is provided with a tailored personal development programme. Training and development needs are reviewed twice a year, along with performance, against clearly set objectives.

Communication and participation
Employees are kept informed of business developments through formal briefings, team meetings, intranet bulletins, video conferences and informal routes. Management takes these opportunities to listen to staff and involve them in taking the business forward. A monthly staff e-zine provides updates on issues and social events.

Culture
The Hiscox culture is underpinned by a set of core values that determine the standard of behaviour expected of employees. These core values – challenge convention, integrity, respect, courage, quality and excellence in execution – guide everything that Hiscox does in its business. With this conduct, the Group recognises that it is more likely to achieve business success and create value for its shareholders. Hiscox strives for the highest standards of corporate governance while being

in essence a non-bureaucratic organisation. An effective and firm system of internal controls ensures that risks are managed within acceptable limits, but not at the expense of innovation or speed of response.

The Group believes that it has got this balance right and that it is one of its greatest strengths. The Group's policies ensure that it continues to follow a best practice approach to managing its people and remains a fair and professional employer. In the unlikely event of an employee having a material concern relating to the operations of the business, a whistleblowing policy explains to staff how they can confidentially raise their misgivings. Hiscox also subscribes to Public Concern at Work, which provides free legal advice to any employee with a concern about possible danger or malpractice in the workplace.

In the community
Hiscox donated £1,171,000 to charities in 2009. As the Group expands internationally, it has been recruiting local staff wherever possible, developing a rapport with the local community and making a direct contribution to the local economy. The Group has maintained its involvement in its local communities with the strong support of its employees. In Bermuda, Hiscox supports the Bermuda Sunshine League which is a transitional living facility for children removed from unstable living environments and gives employees the opportunity to contribute their time and effort to children who require adult role models and a semblance of stability. Hiscox is a member of the Lloyd's Community Programme, which supports local initiatives concerning education, training, enterprise and regeneration. In London, the Reading Partners Scheme has continued, through which staff assist pupils at the Elizabeth Selby Infants School in Tower Hamlets. Employees also mentor students at Morpeth School in Tower Hamlets.

Supporting the arts
The Group continues to support the Bermuda Masterworks Foundation, which aims to repatriate artworks by Bermudian artists or featuring Bermuda landscapes/seascapes.

Hiscox has a two-year commitment to support the Whitechapel Art Gallery in London.

The Hiscox Foundation
The Hiscox Foundation, a charity funded by an annual donation from Hiscox, has been set up to give donations to deserving causes. It gives priority to any charity in which a member of staff is involved with the aim of encouraging and developing such activity. Hiscox staff continued their eight year long support of the Richard House Hospice, raising over £34,000 during 2009. The foundation has committed to support HART (Humanitarian Aid Relief Trust) over a three year period. The charity helps some of the poorest and most abused people in the world. More details of the charities Hiscox supports can be found on our website www.hiscox.com.

In the environment
The way customers conduct their business is of paramount importance to the Group. Hiscox's approach to underwriting their risks will take into account customers' attitudes to all aspects of their business, including care of the environment.

The Group's direct environmental impact is mainly from the energy it uses and the emissions and waste it generates from its premises. In accordance with the Group's environmental policy, consumables are recycled and reused wherever possible. The Group continues to take steps to reduce the amount of raw materials used in business processes and by staff, particularly through the extensive use of computerisation and communications technology. Programmes for recycling batteries, mobile phones, lamps and CDs continued during the year.

The Group's efforts were rewarded by a Clean City Award from the City of London Corporation, which aims to promote good waste management practices and encourage waste minimisation, reuse and recycling.

Hiscox is a member of Climatewise, an insurance industry initiative which aims to reduce the economy's and society's long-term risk from climate change. Hiscox supports the principles of Climatewise and is encouraged by the actions taken by Lloyd's to assist the market to meet the majority of the principles.

In 2009 Hiscox UK conducted an audit of its impact on the environment and, with Corporate Citizenship, calculated the carbon footprint of the UK business. Hiscox UK aims to be Carbon Neutral by the end of 2010 by reducing greenhouse gas emissions, engaging employees to modify their behaviours and seeking to offset unavoidable carbon emissions.

More detailed information relating to the actions Hiscox is taking to meet each of the Climatewise Principles will be published on www.hiscox.com in June 2010.

Hiscox strives for the highest standards of corporate governance while being in essence a non-bureaucratic organisation.

Insurance carriers

Syndicate 3624
Syndicate 3624 is a wholly owned syndicate which began underwriting for the 2009 year of account with an underwriting capacity of £80 million. Syndicate 3624 writes certain business lines including the US E&O account written through the Hiscox underwriting agency in Armonk, New York and a 50% quota share of Syndicate 33's TMT business written by Hiscox owned underwriting agencies. Syndicate 3624 has a capital requirement ratio of 69% of syndicate capacity. Total underwriting capacity of Syndicate 3624 has been increased to £150 million for the 2010 year of account.

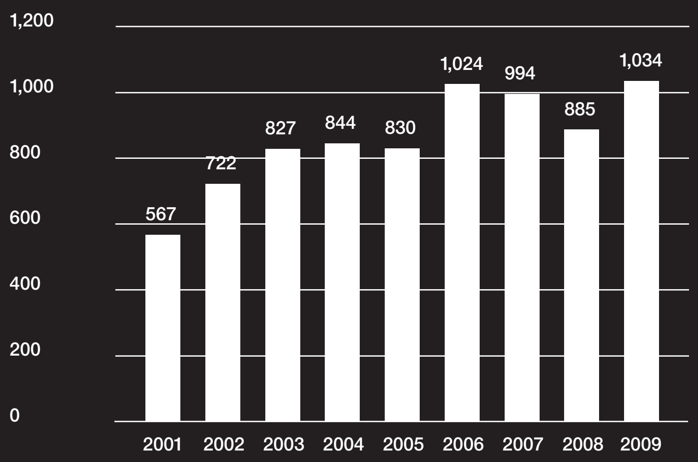
Syndicate 33
Hiscox can trace its origins in the Lloyd's Market to 1901. Today, Hiscox Syndicate 33 is one of the largest composite syndicates at Lloyd's, and has an A.M. Best syndicate rating of A (Excellent). Syndicate 33 underwrites a mixture of reinsurance, major property and energy business, as well as a range of specialty lines including contingency, technology and media risks among others. The business is mainly property-related short-tail business; there is little exposure to aviation or motor business. Syndicate 33 trades through the Lloyd's worldwide licences and ratings. It also benefits from the Lloyd's brand. Lloyd's has an A (Excellent) rating from A.M. Best, an A+ (Strong) from Standard & Poor's, and an A+ (Strong) rating from Fitch.

The geographical and currency splits are shown to the right. One of the main advantages of trading through Lloyd's is the considerably lower capital ratios that are available due to the diversification of business written in Syndicate 33 and in Lloyd's as a whole. For 2010 Syndicate 33 has a capital requirement ratio of approximately 43% of Syndicate capacity. The size of the Syndicate is increased or reduced according to the strength of the insurance environment in its main classes. At present, Hiscox owns approximately 72.5% of the Syndicate, with 27.5% being owned by third party Lloyd's Names. Hiscox receives a fee and a profit commission of approximately 17.5% of profit on the element it does not own.

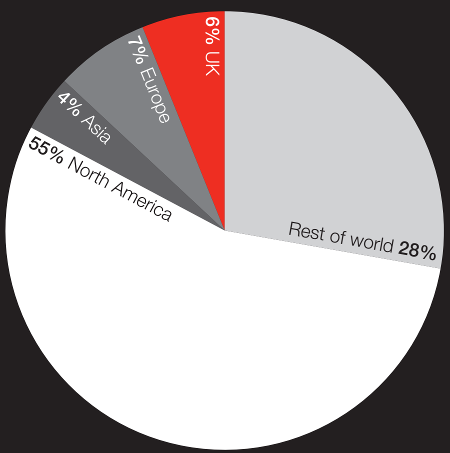
For the 2010 year of account, Syndicate 33's capacity has been increased from £750 million to £1 billion, primarily to reflect the strengthening US Dollar.

The chart to the right shows the gross premiums written of Syndicate 33 for the last nine years.

Syndicate 33
Gross premiums written (£m)



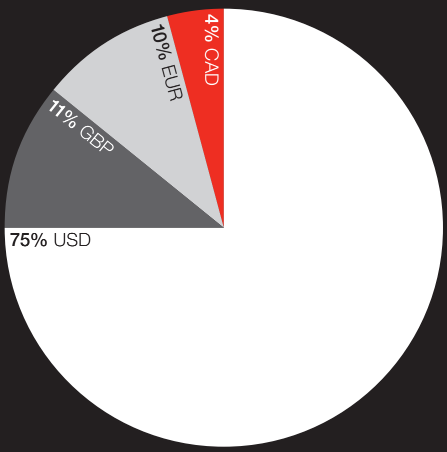
Syndicate 33
2009 Gross premiums written geographical split (%)



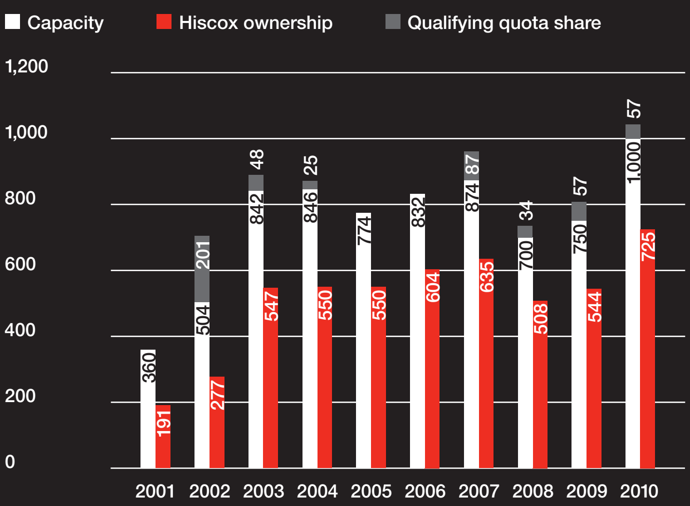
Cougar Syndicate 6104

Cougar Syndicate 6104 was set up under a limited tenancy agreement for the 2008 year of account with an initial capacity of £34 million. It is wholly backed by external Names and takes a pure year of account quota share of Syndicate 33's international property catastrophe reinsurance account. The arrangement was extended for the 2009 year of account and Cougar Syndicate 6104's capacity was increased to £43 million. The Syndicate will continue for the 2010 year of account and the underwriting capacity has been increased to £45 million.

Syndicate 33
2009 Gross premiums written currency split (%)



Syndicate 33
Capacity and Hiscox ownership (£m)



Insurance carriers
continued

Hiscox Insurance Company
Hiscox purchased Hiscox Insurance Company Limited in 1996, in keeping with its aim of diversifying its activities outside of Lloyd's and writing a focused book of regional specialist risks. The Group has reshaped the Company's original portfolio to concentrate on high value household and smaller premium professional indemnity business.

Hiscox Insurance Company has licences throughout Europe. It is the primary insurance vehicle used by the UK and mainland Europe offices for their business. The success of the reshaped portfolio can be seen in the chart below.

Hiscox Insurance Company Limited has achieved average compound growth in gross premiums written of 14.5% from 1997 to 2009, despite discontinuing almost all of its original business. It has also significantly improved its combined ratio.

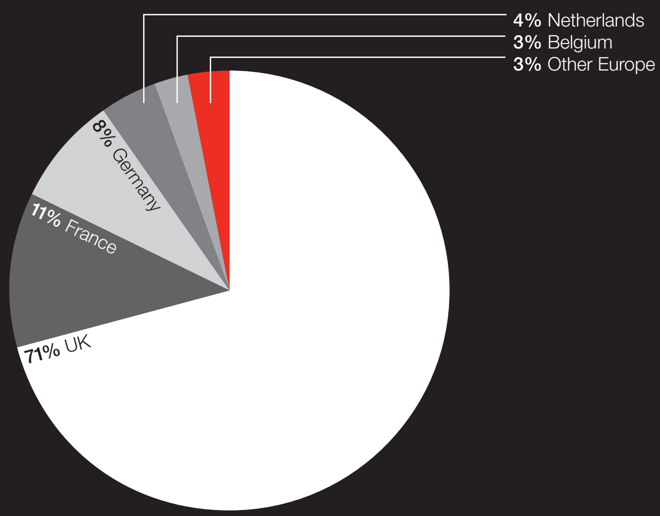
Hiscox Insurance Company Limited has an A.M. Best rating of A (Excellent) and a Standard & Poor's rating of A (Strong).

At the end of 2009, net assets exceeded £172 million (2008: £151 million).

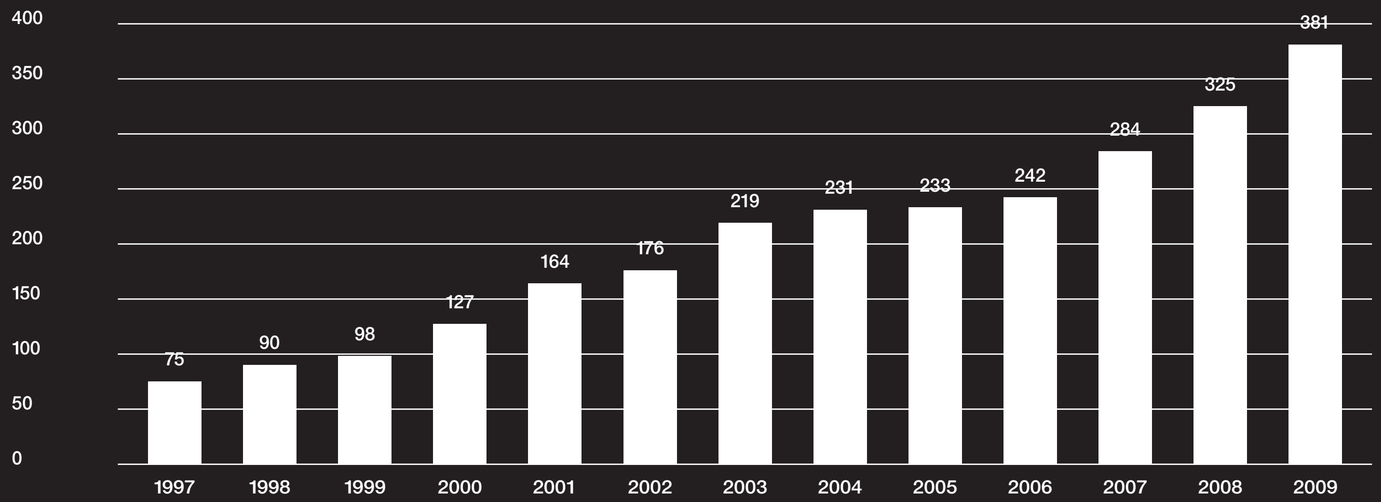
Hiscox Insurance Company (Guernsey)
Formed by Hiscox in 1998, Hiscox Insurance Company (Guernsey) Limited writes mainly kidnap and ransom and fine art insurance.

Hiscox Guernsey has an A.M. Best rating of A (Excellent). At the end of 2009, net assets exceeded $28 million (2008: $23 million).

Hiscox Insurance Company Limited
Gross premiums written geographical split by origin (%)



Hiscox Insurance Company Limited
Gross premiums written (£m)



Hiscox Insurance Company (Bermuda)
Formed by Hiscox in late 2005, Hiscox Insurance Company (Bermuda) Limited was set up as an expansion of the reinsurance operations of Hiscox and as an internal reinsurer of the Group. It recently employed a new team to underwrite healthcare insurance.

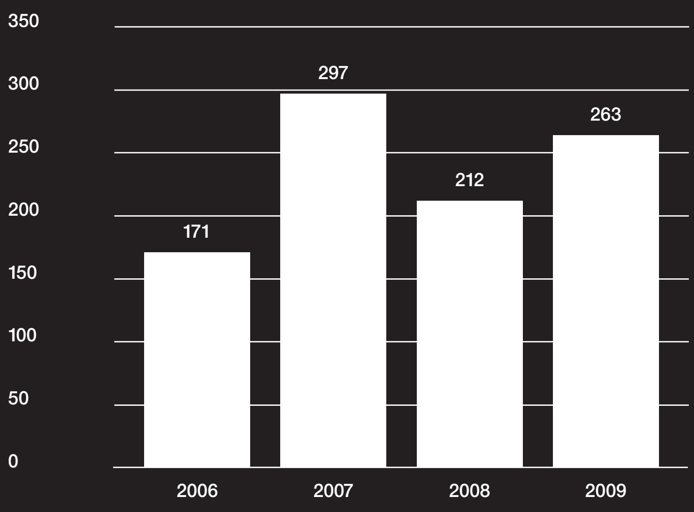
Hiscox Bermuda has an A.M. Best rating of A (Excellent). At the end of 2009, net assets were $807 million (2008: $804 million).

Hiscox Insurance Company Inc.
Hiscox Insurance Company Inc. was acquired by the Group in July 2007 through the purchase of the then parent holding company ALTOHA, Inc.

Hiscox Insurance Company Inc. is based in Geneva, Illinois and is an admitted insurance company with licences in all 50 US states. Its main business is animal mortality insurance for cattle and horses.

Hiscox Insurance Company Inc. is rated A (Excellent) by A.M. Best. At the end of 2009, net assets exceeded $56 million (2008: $52 million).

Hiscox Insurance Company (Bermuda) Limited
Gross premiums written ($m) External business



Board of Directors

Executive Directors

Robert Ralph Scrymgeour Hiscox
Chairman (Aged 67)
Robert Hiscox joined Hiscox in 1965 and has been Chairman of the main holding company of Hiscox since its incorporation in 1973. He was Deputy Chairman of Lloyd's between 1993 and 1995. He is a Non Executive Director of Grainger Trust plc, and AGICM Ltd.

Bronislaw Edmund Masojada
Chief Executive (Aged 48)
Bronek Masojada joined Hiscox in 1993. From 1989 to 1993 he was employed by McKinsey and Co. Bronek served as a Deputy Chairman of Lloyd's from 2001 to 2007. He was a Non Executive Director of Ins-sure Holdings Limited from 2002 to 2006 and is a past president of The Insurance Institute of London. He is Chairman of the Lloyd's Tercentenary Foundation, a charity which supports research in areas of interest to the insurance industry.

Stuart John Bridges
Group Finance Director (Aged 49)
Stuart Bridges joined Hiscox in 1999. He is a Chartered Accountant and has held posts in various financial service companies in the UK and US, including Henderson Global Investors. He is Chairman of the Business Advisory Board of the Institute of Chartered Accountants in England and Wales, a member of the Financial Regulation and Taxation Committee of the Association of British Insurers and Vice-chairman of the Lloyd's Market Association Finance Committee.

Robert Simon Childs
Chief Underwriting Officer and Chairman of Hiscox USA (Aged 58)
Robert Childs joined Hiscox in 1986, served as the Active Underwriter of the Hiscox Lloyd's Syndicate 33 between 1993 and 2005, and is the Group's Chief Underwriting Officer. Robert was Chairman of the Lloyd's Market Association from January 2003 to May 2005. He is Non Executive Director of HIM Capital Limited and HIM Capital Holdings Limited.

Independent Non Executive Directors

Daniel Maurice Healy ▲○□
Non Executive Director and Chairman of the Audit Committee (Aged 67)
Daniel Healy joined Hiscox in 2006. He was appointed Executive Vice President and Chief Financial Officer of North Fork Bancorporation in 1992 and a member of its Board of Directors in 2000. He was a partner with KPMG LLP before joining North Fork. He was the Managing Partner of the San José, California and Long Island, New York offices and held other positions in that firm during his tenure. He is Chairman of Herald National Bank and he holds Board positions with KBW, Inc. and Harlem RBI, a not-for-profit organisation. He is also a senior adviser to Permira Advisers LLC, an international private equity firm.

Ernst Robert Jansen △○□
Non Executive Director (Aged 61)
Ernst Jansen joined Hiscox in 2008. He held several Managing Director positions in the European chemical industry between 1980 and 1990. He was an Executive Director then Vice Chairman of Eureko B.V. between 1992 and 2007. Following retirement he became an adviser to the Executive Board and is a member of the Supervisory Board of a number of Eureko operating companies.

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Charles Dupplin

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22 Victoria Street
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Bankers
Bank of Bermuda – HSBC
6 Front Street
Hamilton HM 11
Bermuda

Stockbrokers
UBS Limited
1 Finsbury Avenue
London EC2M 2PP
United Kingdom

Registrars
Capita Registrars (Jersey) Limited
PO Box 532
St Helier
Jersey JE4 5UW

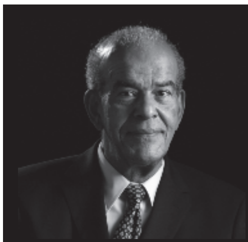
△
Member of the Audit Committee

○
Member of the Conflict Committee

□
Member of the Remuneration and Nomination Committee

Chairman of Committee is highlighted in solid

Independent Non Executive Directors
continued



Dr James Austin Charles King △●□
Non Executive Director and Chairman of the Conflict Committee (Aged 71)
Dr James King joined Hiscox in 2006. He chairs Keytech Limited, The Bermuda Telephone Company Ltd, the Argus Group of Companies, Grotto Bay Properties Ltd and the Establishment Investment Trust, a UK listed company. He was chairman of the Bank of N.T. Butterfield & Son Limited until 19 April 2007. He is a Trustee of the Bermuda Institute of Ocean Sciences and a Director of Castle Harbour Limited. Dr King is a fellow of the Royal College of Surgeons, Canada and the American College of Surgeons.

Sir Mervyn Pedelty ○■
Senior Independent Director and Chairman of the Remuneration and Nomination Committee (deceased)
Sir Mervyn Pedelty joined Hiscox in 2005. He was previously the Chief Executive and an Executive Director of The Co-operative Bank plc (from 1997 until his retirement in 2004) and also of Co-operative Financial Services Limited and the Co-operative Insurance Society Limited (from 2002 to 2004). He was a Director of the Association of British Insurers (from 2002 to 2004) and was a former Council Member of the British Bankers' Association. Sir Mervyn was a Chartered Accountant and a Chartered Banker. His other recent appointments included: Independent Director of Friends Provident plc, Chairman of the FTSE4 Good Policy Committee, a Director of Performances Birmingham Limited and a Senior Adviser to Permira Advisers LLP.

Andrea Sarah Rosen △○■
Acting Senior Independent Director and Acting Chairman of the Remuneration and Nomination Committee (Aged 55)
Andrea Rosen joined Hiscox in 2006. She was appointed as a Director of Alberta Investment Management Corporation in October 2007 and is a Director of Emera Inc. She was previously Vice Chair of TD Financial Group and President of TD Canada Trust from 2002 to 2005. Prior to this she held various positions within the TD Financial Group from 1994 to 2002, including Executive Vice President of TD Commercial Banking and Vice Chair of TD Securities. She was Vice President of Varity Corporation from 1991 to 1994 and held various positions with Wood Gundy Inc. from 1981 to 1990.

Gunnar Stokholm △○□
Non Executive Director (Aged 60)
Gunnar Stokholm joined Hiscox in 2008. He worked for Zurich Financial Services between 1995 and 2004, in a number of roles including CEO for Australia and Asian markets. He spent the majority of his career at Topdanmark Insurance and held the position of Managing Director of Topdanmark Holding from 1986 to 1995.

Dirk Arie Stuurop △○□
Non Executive Director (Aged 61)
Dirk Stuurop joined Hiscox in 2006. He is managing partner of Lighthouse Holdings LLC. From 2004 to 2009 he was Vice Chairman of the Board of RAM Holdings Limited, a Bermudian domiciled financial guaranty reinsurance operation. From 1999 to 2006, Dirk was President of Stuurop & Company, a privately-owned firm providing strategic advice to executive managements and boards of directors. In 1999 he retired as Chairman of Global Financial Institutions at Merrill Lynch where he worked from 1982. He served as Chairman of Worldinsure Ltd, from 2000 to 2002 and as Senior Executive Director to Banc of America Securities in 2003.

Corporate governance

Overview and basis of reporting
Hiscox Ltd ('the Company') is the Bermudian domiciled holding company for the Group. The Company is listed on the London Stock Exchange's main market for listed securities. The corporate governance framework for companies registered in Bermuda is established by the Company's constitution together with Companies Act legislation.

During 2009, and up to the date of this report and accounts, the Group has complied with the provisions of the Combined Code in all material respects.

The Board of Directors
The Board comprises four Executive Directors and seven independent Non Executive Directors, including a Senior Independent Director. Biographical details for each member of the Board are provided on pages 32 to 33.

The Board continues to believe in the need for an Executive Chairman. The roles and activities of the Chairman and Chief Executive are distinct and separate. The Chairman is responsible for running an effective Board including oversight of corporate governance and overall strategy. The Chief Executive has responsibility for running the Group's business.

In accordance with the Company's Bye-Laws all Directors are required to submit themselves for re-election at least every three years. The appointment and removal of the Company Secretary is a matter for the Board as a whole. All Directors are entitled to seek independent professional advice at the Company's expense. A copy of the advice is provided to the Company Secretary who will circulate it to all Directors. No such advice was sought during the year.

The Board meets at least four times a year and operates within established Terms of Reference. It is supplied with appropriate and timely information to enable it to review business strategy, trading performance, business risks and opportunities. The Board of Hiscox Ltd met four times during the year. The Board considers all the Non Executive Directors to be independent within the meaning of the Combined Code as there are no relationships or circumstances which would interfere with the exercise of their independent judgement.

The Board's Terms of Reference include a Schedule of Matters Reserved for Board Decision, a copy of which can be found on the Group's website: www.hiscox.com.

The Board retains ultimate authority for high level strategic and management decisions including: setting Group strategy, approving significant mergers or acquisitions, approving the financial statements, declaration of the interim dividends and recommendation of the final dividend, approving Group business plans and budgets, approving major new areas of business, approving capital raising, approving any bonus or rights issues of share capital, setting Group investment guidelines, approving the Directors' remuneration, approving significant expenditure or projects, and approving the issue of share options. The Board has, however, authorised the boards of the trading entities and business divisions to manage their respective operational affairs, to the extent that Company Board level approval is not required.

The Board's committees
The Board has appointed and authorised a number of committees to manage aspects of the Group's affairs. Each committee operates within established written terms of reference and each committee Chairman reports directly to the Board.

The Group Executive Committee
The Group Executive Committee, comprising the Executive Directors, meets monthly to raise and discuss topics such as Group strategy (subject always to Board approval), approval of senior appointments and remuneration (other than Board appointments), management of the Group's trading performance, mergers and acquisitions (which are not significant to the Group), significant issues raised by the London, European and US executive groups and approval of exceptional spend within the limits established by the Board. The London, European and US executive groups provide strategic direction and are a forum for communicating important issues. Below these geographic executive groups, are the local management teams that drive the local businesses.

The Audit Committee
The Audit Committee of Hiscox Ltd is chaired by Daniel Healy and comprises Ernst Jansen, Dr James King, Andrea Rosen, Gunnar Stokholm and Dirk Stuurop. Daniel Healy and Dr James King are considered by the Board to have

recent and relevant financial experience.
The Audit Committee meets at least three times a year to assist the Board on matters of financial reporting, risk management and internal control. The Audit Committee monitors the scope, results and cost effectiveness of the internal and external audit functions, the independence and objectivity of the external auditors, and the nature and extent of non-audit work undertaken by the external auditors together with the level of related fees. The internal and external auditors have unrestricted access to the Audit Committee. All non-audit work undertaken by the Group's external auditors with fees greater than £50,000 must be pre-approved by the Audit Committee. KPMG has confirmed to the Audit Committee that in its opinion it remains independent.
The Committee is satisfied that this is the case.

The Remuneration and Nomination Committee
The Remuneration and Nomination Committee comprises Daniel Healy, Ernst Jansen, Dr James King, Andrea Rosen, Gunnar Stokholm, Dirk Stuurop and until his death Sir Mervyn Pedelty. It was chaired, until his death, by Sir Mervyn Pedelty, with Andrea Rosen as alternate, and is now chaired by Andrea Rosen. It meets a minimum of two times a year to deal with appointments to the Board and to recommend a framework of executive remuneration.

The Directors' remuneration report is presented on pages 37 to 44.

The Conflicts Committee
The Group has a Conflicts Committee which comprises of independent Non Executive Directors from within the Group, and chaired by Dr James King. It meets as and when required. Conflicts of interest may arise from time to time because Syndicate 33, Syndicate 3624 and Syndicate 6104 are managed by a Hiscox-owned Lloyd's Managing Agency. 27.5% of the Names on Syndicate 33 are third parties and 72.5% of Syndicate 33 is owned by a Hiscox Group company. 100% of Syndicate 3624 is owned by a Hiscox Group company. 100% of Syndicate 6104 is owned by third parties. The Conflicts Committee serves to protect the interests of the third-party Syndicate Names. Should such a potential conflict of interest arise, there is a formal procedure to refer the matter to this Committee.

Risk Committees
There are a number of committees within the Group which have been established to oversee specific risk areas, including underwriting, reserving, reinsurance credit, liquidity, broker credit, business continuity and investments.
A Group risk committee ensures risk management activities are effective and integrated. These committees comprise Directors of the Company and its subsidiaries and relevant senior employees.

Performance evaluation
Periodically the Chairman reviews the performance of the Board as a whole.
He meets with the Non Executive Directors separately and as a body to discuss a wide range of issues including the performance of the Executive Directors. In addition the Non Executives periodically meet without the Chairman and Executive Directors to discuss a similarly wide range of issues concerning the company including as appropriate the performance of the Chairman and the Executive Directors. No major issues concerning Board performance have been raised during the year.

The Chief Executive held one-to-one meetings with each of the Executive Directors to discuss their performance over the year and to set targets for the year ahead.

Meetings and attendance table

	Ltd Board	Audit Committee	Remuneration and Nomination Committee
Director	Attended	Attended	Attended
RRS Hiscox	4/4	n/a	n/a
BE Masojada	4/4	n/a	n/a
SJ Bridges	4/4	n/a	n/a
RS Childs	4/4	n/a	n/a
DM Healy	4/4	3/3	2/2
ER Jansen	4/4	3/3	2/2
Dr J King	3/4	3/3	2/2
Sir Mervyn Pedelty	3/4	n/a	1/2
AS Rosen	3/4	2/3	2/2
G Stokholm	4/4	3/3	2/2
DA Stuurop	3/4	2/3	2/2

Corporate governance
continued

Shareholder communications

The Executive Directors communicate and meet directly with shareholders and analysts throughout each year, and do not limit this to the period following the release of financial results or other significant announcements.

All Directors attended the Annual General Meeting in 2009.

The Company commissions independent research on feedback from shareholders and analysts on a regular basis following the Company's results announcements. This research together with the analysts' research notes are copied to the Non Executive Directors in full. The Chairman attends a number of meetings with shareholders as well as speaking at the analysts' presentations. In addition, any specific items covered in letters received from major shareholders are reported to the Board. Major shareholders are invited to request meetings with the Senior Independent Director and/or the other Non Executive Directors.

An alert service is available on www.hiscox.com to notify any stakeholder of new stock exchange announcements.

Accountability and internal control

The Directors are responsible for maintaining a sound system of internal control to safeguard the investment made by shareholders and the Company's assets, and for reviewing its effectiveness.

The risk management systems are set out in detail in the risk management report on pages 21 to 25.

The Board has reviewed the effectiveness of internal controls during 2009, including financial, operational and compliance controls. The Board confirms there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company, which has been in place throughout the year and up to the date of approval of the Annual Report and Accounts, and accords with the guidance in the document 'Internal Control: Guidance for Directors on the Combined Code'. The head of each business area is responsible for implementing the risk management programme in their area of operations. The Risk function collates risk management information and works with the risk committees to monitor significant risks and movements, and review the relevant internal controls.

The Group also has an internal audit function which has direct access to the Audit Committee and reports to each meeting.

The Board acknowledges that it is neither possible, nor desirable, to eliminate risk completely. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss. The constant aim is to be fully aware of the risks to which the business is exposed and to manage these risks to acceptable levels.

Directors' remuneration report

This report sets out the remuneration policy for the Group's senior executives. This policy is consistent with the overall reward approach across the Group. The sections in this report entitled 'Annual cash incentives', 'Share incentive schemes', 'Remuneration of Executive Directors' and 'Pensions' have been audited by KPMG. The remainder of the report is unaudited.

Remuneration and Nomination Committee
The Remuneration and Nomination Committee meets at least twice a year. The members of the Committee for 2009 were Sir Mervyn Pedelty (Chairman), Andrea Rosen (Acting Chairman), Daniel Healy, Dr James King, Dirk Stuurop, Ernst Jansen and Gunnar Stokholm.

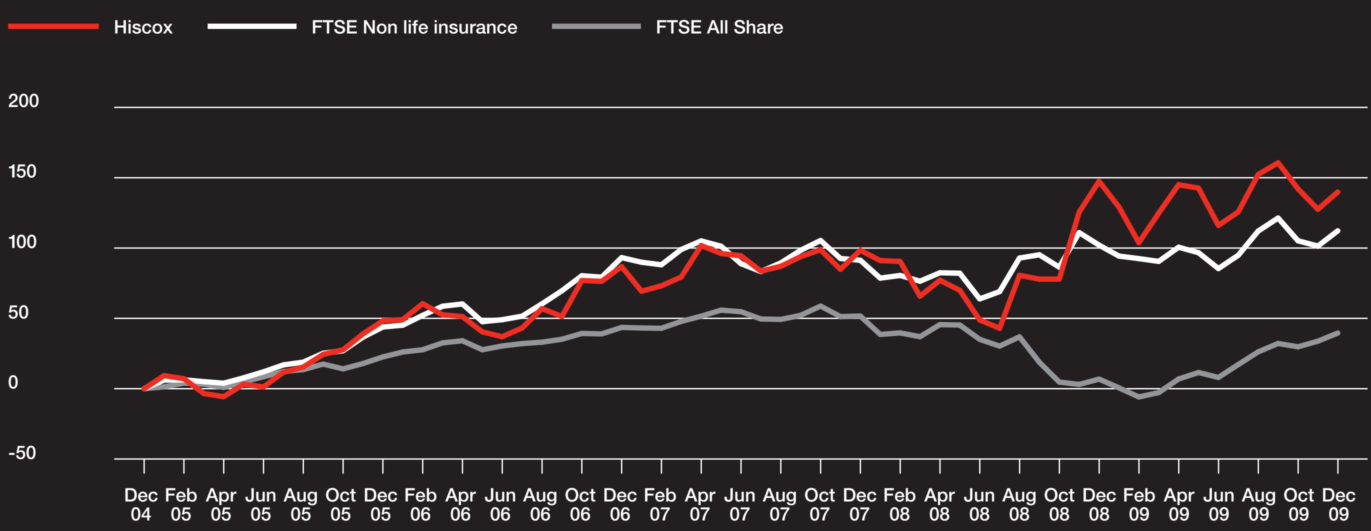
The Committee focuses on:
- the overall remuneration strategy, policy and cost for the Group;
- the determination of levels and make-up of remuneration for the four Executive Directors; and
- the award of sizable bonuses to individuals.

None of the committee has any personal financial interest (other than as a shareholder) or conflicts of interest arising from cross directorships or day-to-day involvement in running the business. No Director plays any part in any discussion about his or her own remuneration.

The Committee is provided with data and has access to advice from Towers Perrin, independent remuneration consultants. The Company also uses the Watson Wyatt compensation benchmarking reports. Towers Perrin and Watson Wyatt have now merged to form 'Towers Watson'. Towers Watson provide no other services to the Company.

Remuneration policy
The remuneration philosophy is to provide rewards that are competitive in every country in which Hiscox operates and that are consistent with our overall reward principles:
- competitive base pay;
- benefits which encourage health and security for the individual and his or her family but are not excessive and are consistent at all levels of the organisation;
- an annual bonus scheme which enables employees to earn attractive bonuses for generating good levels of return on equity;
- to encourage share ownership at all levels of the organisation and require it at senior levels; and
- contracts and notice periods that are in line with acceptable market practice but limit severance payments made on termination.

Total shareholder return (%)



Directors' remuneration report continued

As a business Hiscox is focused on generating strong pre-tax returns on equity and long-term shareholder returns, therefore our reward structure is aligned with this.

The Remuneration and Nomination Committee regularly reviews our remuneration approach and, particularly in the context of the current remuneration environment, will do so again this year.

Remuneration elements
The elements of remuneration at Hiscox are: fixed reward (base salary, benefits and retirement benefits), and variable reward (annual cash incentives (bonuses) and share incentive schemes).

Fixed reward
Fixed reward is made up of base salary, benefits and retirement benefits.

Base salary
Base salaries are reviewed annually. The Remuneration and Nomination Committee takes into account inflation rate movements by country, market data provided by its own consultants, Towers Perrin, and the competitive position of Hiscox salaries (based on the Watson Wyatt salary reports), in order to set the overall salary budget.

Individual salaries are set by taking into account all of the above as well as individual performance and skills.

When approving Executive Directors' salaries, the Remuneration and Nomination Committee takes into account rates of inflation, performance, and competitive positioning of salaries as informed by Watson Wyatt data and other publicly available reports.

In 2009, Executive Directors' salaries increased by 1.6% overall. Executive Directors did not receive a salary increase in the 2010 salary review.

Benefits
Benefits are set within agreed principles but reflect normal practice for each country. Hiscox benefits include health insurance, life insurance and long-term disability schemes.

Retirement benefits
These also vary by local country practice. With the exception of the Netherlands, all Hiscox retirement schemes are based on defined contributions. In the Netherlands, we closed the defined benefit scheme to new members from July 2008 and introduced a defined contribution scheme in 2009 into which all current employees will transition from the beginning of 2010.

Variable reward
Annual cash incentives (bonuses)
Hiscox's remuneration policy is underpinned by the belief that a significant portion of total remuneration should be attained through incentive awards, thereby linking rewards directly with performance. The expectation is that successful performance (company and individual) should enable employees to achieve upper quartile total remuneration.

Two bonus pools are operated: the Personal Performance Bonus (PPB) and the Profit Related Bonus (PRB). The PPB is only available to junior and mid-level staff and is based entirely on individual performance ratings. It is designed to ensure that employees in these roles continue to be motivated to perform and the benefit is up to 10% of relevant salaries.

All employees, including Executive Directors, are eligible for the Profit Related Bonus. The PRB scheme is triggered when the business profits of the Group, based on the year's pre-tax operating result, exceed a return on equity (ROE) linked to the longer-term rate of return ('Hurdle Rate'). The minimum Hurdle Rate is currently set at a 10% pre-tax return on allocated equity with the bonus pool comprising 15% of profits in excess of that. Bonus pools are then calculated for each major business division based on the performance of that division against the Hurdle Rate of return for the division's allocated equity.

The Hurdle Rate for the 2009 bonus was reviewed. On balance the conclusion was that the Hurdle Rate should remain unchanged for 2009 but should continue to be reviewed for subsequent years depending on changes in the longer-term rate of return.

Once the overall bonus pool has been established, individual bonuses, including those for Executive Directors, are calculated based on the results of each business area and individual performance. The Remuneration and Nomination Committee determines the bonuses to be paid to the Executive Directors based on the performance of the Group and an assessment of individual performance. In this way, the bonus scheme aligns the interests of Executive Directors and employees with shareholders.

Executive Directors' cash incentives and ROE

	Pre-tax return on equity %	Average bonus as a percentage of salary %
1998	16	73
1999	0	0
2000	3	0
2001	(24)	0
2002	13	90
2003	30	202
2004	28	173
2005	19	54
2006	35	274
2007	36	372
2008	14	53
2009	34	287

The payment of larger bonuses is normally deferred over a three-year period as follows.

Bonus of £50,000, €75,000, $100,000 and below	Entire bonus taken in cash in year one
Bonus above £50,000 and below £100,000 Bonus above €75,000 and below €150,000 Bonus above $100,000 and below $200,000	£50,000, €75,000, $100,000 taken in year one Balance of bonus split 50% in year two, and 50% in year three
Bonus above £100,000 Bonus above €150,000 Bonus above $200,000	50% of bonus taken in year one Balance of bonus split 50% in year two, and 50% in year three

Share ownership is encouraged amongst senior personnel by allowing the deferred element of the annual bonus to be used, without deferral for:
- payment of the exercise price on the exercise of share options;
- payment of tax on the exercise of performance shares;
- purchase of shares; and
- payment of debt due on share purchases.

The only exception to this is for US-based employees where, due to the implications of the US Internal Revenue Code, employees are not able to receive the deferred element of their bonuses early in order to purchase shares.

Early payment of deferred bonuses for reasons other than the above can only be made with the agreement of the Chief Executive (and the Remuneration and Nomination Committee in the case of Executive Directors).

The Remuneration and Nomination Committee has decided that bonuses earned in respect of performance in financial year 2009 need not be deferred. Employees will, however, be required to repay a proportion of their bonuses in the event that they leave in circumstances in which they would otherwise have forfeited them.

Share Incentive Schemes
The Remuneration and Nomination Committee believes that employees should be encouraged to own Hiscox shares so that they are aligned with the long-term success of the Company. Hiscox operates a Performance Share Plan for senior managers, a UK Save as You Earn scheme and an International Save as You Earn scheme.

Performance Share Plan
Restricted share awards or nil cost option awards (depending on the appropriate practice by country) are made to Executive Directors and other senior managers at the discretion of the Remuneration and Nomination Committee. Awards under this plan were made in 2009 and the Remuneration and Nomination Committee has also agreed to make awards under this plan in 2010. The maximum annual award to an individual under the Performance Share Plan is a value of 200% of basic salary. The highest actual grant awarded in 2009 was 193% of basic salary.

Dividend payments
In order to better align senior managers with Total Shareholder Return, the concept which is applied to the Performance Share Plan awards is that the recipient is provided with the equivalent of the dividend either in shares or cash. This specifically works as follows:
- dividends (or amounts equal to dividends) on shares granted under the Performance Share Plan roll up in the form of shares between the grant and vesting;
- at the end of the performance period the employee would have options over the proportion of the share grant which vests by reference to the satisfaction of the applicable performance target as well as over the number of shares representing the 'rolled up' dividends on those shares; and
- for UK-based employees only, after vesting but before exercise, the employee would then receive 'shadow dividends' (i.e. amounts equal to dividends paid) on the total number of shares remaining under option. Up to a maximum of 200,000 shares under option per individual, these amounts would be paid in cash, twice yearly, at the same time as dividends are paid to shareholders, until the option is exercised (which could be for up to a further seven years, when the option expires). Above 200,000 shares under option, the 'shadow dividends' would be re-invested into shares within the trust. Executive Directors, however, would have

Directors' remuneration report continued

the entire 'shadow dividend' re-invested in shares within an employee benefit trust.

Performance conditions

Performance conditions for the Performance Share Plan are as follows:
- 25% of the award vests if the Company achieves an average ROE of 10% post-tax for each of the three years;
- 100% vests if the average three-year return exceeds 17.5% post-tax; and
- vesting will occur on a straight-line basis between these points.

The Remuneration and Nomination Committee believes that using ROE as the long-term performance condition better aligns the interests of employees with shareholders as ROE best captures the efficiency with which the Company is using shareholder funds to generate earnings. The Remuneration and Nomination Committee believes that an average ROE performance requirement over the three-year period smoothes out any cyclical fluctuations in earnings and ensures that over any given period shareholders will receive a minimum return on equity before awards granted to employees will vest.

ROE has been calculated as profit after tax and goodwill amortisation divided by shareholders funds at the beginning of each year, excluding foreign currency items on economic hedges and intragroup borrowings.

Save as You Earn

The sharesave scheme and international sharesave scheme are offered to all employees and currently have a 60% participation.

Shareholding guidelines

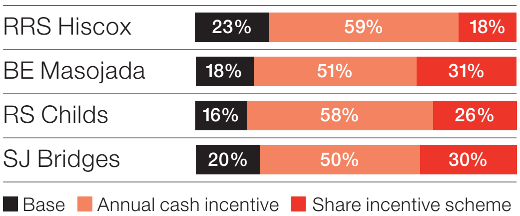
We strongly believe that senior managers within Hiscox should be aligned with Hiscox shareholders by owning a reasonable number of Hiscox shares.

Formal shareholding guidelines are in place which mean that within five years of becoming an Executive Director, Hiscox Partner (the top 5% of employees in the company) or a member of a subsidiary board, the employee will be expected to own Hiscox shares valued at 100% of salary for Hiscox Partners and members of subsidiary boards and 150% of salary for Executive Directors.

The table at the end of the remuneration report details Directors' interests in the long-term incentive plans.

Executive Director reward

Executive Directors' reward packages are consistent with the rest of the business. The actual compensation paid to the four Executive Directors in 2009 is outlined in the table below. Details of their contractual notice periods is contained in the table opposite.



'Base' refers to base salary for the year.
'Annual cash incentive' is the annual amount allocated from the profit bonus pool.
'Share incentive scheme' is the estimated value at award of the Performance Share Plan awards made during the year.

Remuneration of Executive Directors

	2009 Basic salary £000	2009 Benefits £000	2009 Bonus £000	2009 Total £000	2008 Basic salary £000	2008 Benefits £000	2008 Bonus £000	2008 Total £000
RRS Hiscox	**310**	**2**	**800**	**1,112**	308	2	175	485
BE Masojada	**436**	**2**	**1,250**	**1,688**	428	2	200	630
RS Childs	**356**	**73**	**1,250**	**1,679**	348	221	200	769
SJ Bridges	**326**	**2**	**800**	**1,128**	318	2	175	495

External Non Executive Directorships

No external appointments may be accepted by an Executive Director where such appointment may give rise to a conflict of interest. The consent of the Chairman is required in any event. During the year, RRS Hiscox has been a Non Executive Director of Grainger Trust plc and was paid £35,000 for his services and AGICM Ltd and was paid £10,000. During the year, RS Childs has been a Non Executive Director of HIM Capital Limited and HIM Capital Holdings Limited and did not receive any payment for his services. SJ Bridges and BE Masojada did not hold any Non Executive Director positions during the year.

Service contract table

Director	Effective date of Hiscox Ltd contract	Unexpired term and notice period
RRS Hiscox	12 Dec 2006	12 months
BE Masojada	12 Dec 2006	6 months
RS Childs	12 Dec 2006	6 months
SJ Bridges	12 Dec 2006	6 months
DM Healy	11 Oct 2006	3 months
ER Jansen	20 Nov 2008	3 months
Dr J King	11 Oct 2006	3 months
Sir Mervyn Pedelty	11 Oct 2006	3 months
AS Rosen	11 Oct 2006	3 months
G Stockholm	20 Nov 2008	3 months
DA Stuurop	11 Oct 2006	3 months

Remuneration of Non Executive Directors

Non Executive Directors receive an annual fee in respect of their Board appointments together with additional compensation for their further duties in relation to Board committees. All amounts are denominated in US Dollars. The structure of the fees paid are detailed below:

The fees in relation to Hiscox Ltd for the year were:

	Hiscox Ltd Board $000	Committees $000	**Total 2009 $000**	Total 2008 $000
DM Healy	83	37	**120**	115
ER Jansen	83	27	**110**	12
Dr J King	83	32	**115**	110
Sir Mervyn Pedelty	83	34	**117**	130
AS Rosen	83	34	**117**	113
G Stokholm	83	27	**110**	12
DA Stuurop	83	27	**110**	105

Pensions

	Increase in accrued pension during the year £000	Total accrued annual pension at 31 Dec 09 £000	Transfer value of increase in accrued pension £000	Transfer value of accrued pension at 1 Jan 09 £000	Transfer value of accrued pension at 31 Dec 09 £000	Increase/ (decrease) in transfer value of accrued benefit during the year £000
RRS Hiscox	26	231	26	4,772	4,701	(71)
BE Masojada	2	39	2	681	646	(35)
RS Childs	20	240	24	5,127	5,387	260
SJ Bridges	–	29	1	459	452	(7)

Share options

	Number of options at 1 January 2009	Number of options granted	Number of options lapsed	Number of options exercised	**Number of options at 31 December 2009**	Exercise price £	Market price at date of exercise £	Date from which exercisable	Expiry date
SJ Bridges	62,038	–	–	(62,038)	**–**	1.281	2.943-3.451	13 Oct 02	12 Oct 09
	56,398	–	–	–	**56,398**	1.755	–	03 May 04	02 May 11
	180,341	–	–	–	**180,341**	1.252	–	19 Nov 05	18 Nov 12
	154,578	–	–	–	**154,578**	1.465	–	02 Apr 06	01 Apr 13
	154,578	–	–	–	**154,578**	1.514	–	13 Jul 07	12 Jul 14
	154,578	–	–	–	**154,578**	1.499	–	06 Apr 08	05 Apr 15
	762,511	–	–	(62,038)	**700,473**				
RS Childs	112,797	–	–	(112,797)	**–**	1.281	3.437	13 Oct 02	12 Oct 09
	78,958	–	–	–	**78,958**	1.755	–	03 May 04	02 May 11
	206,104	–	–	–	**206,104**	1.252	–	19 Nov 05	18 Nov 12
	206,104	–	–	–	**206,104**	1.465	–	02 Apr 06	01 Apr 13
	206,103	–	–	–	**206,103**	1.514	–	13 Jul 07	12 Jul 14
	206,104	–	–	–	**206,104**	1.499	–	06 Apr 08	05 Apr 15
	1,016,170	–	–	(112,797)	**903,373**				
RRS Hiscox	56,398	–	–	–	**56,398**	1.755	–	03 May 04	02 May 11
	51,526	–	–	(51,526)	**–**	1.465	2.990	02 Apr 06	01 Apr 13
	51,526	–	–	(51,526)	**–**	1.514	3.028	13 Jul 07	12 Jul 14
	51,526	–	–	(51,526)	**–**	1.499	3.068	06 Apr 08	05 Apr 15
	210,976	–	–	(154,578)	**56,398**				
BE Masojada	112,797	–	–	(112,797)	**–**	1.281	3.465	13 Oct 02	12 Oct 09
	169,195	–	–	–	**169,195**	1.020	–	15 Jun 03	14 Jun 10
	78,958	–	–	–	**78,958**	1.755	–	03 May 04	02 May 11
	206,104	–	–	–	**206,104**	1.252	–	19 Nov 05	18 Nov 12
	206,104	–	–	–	**206,104**	1.465	–	02 Apr 06	01 Apr 13
	206,104	–	–	–	**206,104**	1.514	–	13 Jul 07	12 Jul 14
	206,104	–	–	–	**206,104**	1.499	–	06 Apr 08	05 Apr 15
	1,185,366	–	–	(112,797)	**1,072,569**				
Other employees	100,385	–	–	(100,385)	**–**	1.281	2.910-3.615	13 Oct 02	12 Oct 09
	326,297	–	–	(174,618)	**151,679**	1.020	2.895-3.502	15 Jun 03	14 Jun 10
	292,128	–	–	(47,386)	**244,742**	1.755	3.110-3.607	03 May 04	02 May 11
	435,322	–	–	(74,375)	**360,947**	0.806	2.948-3.368	27 Sep 04	26 Sep 11
	754,623	–	–	(133,190)	**621,433**	1.252	3.110-3.388	19 Nov 05	18 Nov 12
	843,325	–	–	(212,836)	**630,489**	1.465	3.138-3.527	02 Apr 06	01 Apr 13
	1,303,596	–	–	(165,186)	**1,138,410**	1.514	3.030-3.388	13 Jul 07	12 Jul 14
	1,576,674	–	–	(473,956)	**1,102,718**	1.499	2.935-3.502	06 Apr 08	05 Apr 15
	5,632,350	–	–	(1,381,932)	**4,250,418**				
Total	8,807,373	–	–	(1,824,142)	**6,983,231**				

Share options

The interests of the Directors and employees under the UK and International Sharesave Schemes of the Group are set out below:

	Number of options at 1 January 2009	Number of options granted	Number of options lapsed	Number of options exercised	**Number of options at 31 December 2009**	Exercise price £	Market price at date of exercise £	Date from which exercisable	Expiry date
UK Sharesave Scheme									
SJ Bridges	4,256	–	–	–	**4,256**	2.220	–	01 May 10	31 Oct 10
RRS Hiscox	4,907	–	–	–	**4,907**	1.956	–	01 Dec 11	31 May 12
BE Masojada	4,343	–	–	–	**4,343**	2.210	–	01 Dec 10	31 May 11
Other employees	218,193	–	(13,837)	–	**204,356**	2.220	–	01 May 10	31 Oct 10
	143,557	–	(6,624)	(2,234)	**134,699**	2.210	3.169	01 Dec 10	31 May 11
	540,640	–	(17,388)	(1,303)	**521,949**	1.982	2.948-3.352	01 May 11	31 Oct 11
	387,234	–	(36,998)	(2,452)	**347,784**	1.956	2.975-3.169	01 Dec 11	31 May 12
	–	122,827	(3,934)	–	**118,893**	2.418	–	01 May 12	01 Nov 12
	–	90,241	–	–	**90,241**	2.752	–	01 Dec 12	31 May 13
Total	1,303,130	213,068	(78,781)	(5,989)	**1,431,428**				
International Sharesave Scheme									
RS Childs	4,147	–	–	–	**4,147**	2.220	–	01 May 10	31 Oct 10
Other employees	1,613	–	–	(1,613)	**–**	1.576	3.367	01 Dec 08	31 May 09
	95,616	–	(5,925)	–	**89,691**	2.220	–	01 May 10	31 Oct 10
	7,363	–	–	–	**7,363**	2.220	–	01 Jul 10	31 Dec 10
	23,709	–	–	(671)	**23,038**	2.210	3.375	01 Dec 10	31 May 11
	198,056	–	(36,926)	–	**161,130**	1.982	–	01 May 11	31 Oct 11
	62,464	–	(12,713)	–	**49,751**	1.956	–	01 Dec 11	31 May 12
	–	54,987	(549)	–	**54,438**	2.418	–	01 May 12	01 Nov 12
	–	73,180	–	–	**73,180**	2.752	–	01 Dec 12	31 May 13
Total	392,968	128,167	(56,113)	(2,284)	**462,738**				

Performance Share Plan

	Number of awards at 1 January 2009	Number of awards granted	Number of awards lapsed	Number of awards exercised	**Number of awards at 31 December 2009**	Market price at date of exercise £	Date from which released
SJ Bridges	215,000	22,625	–	(237,625)	**–**	3.007	12 Jan 09
	120,000	–	–	–	**120,000**	–	26 Mar 10
	110,000	–	–	–	**110,000**	–	07 Apr 11
	–	200,000	–	–	**200,000**	–	02 Apr 12
RS Childs	250,000	26,309	–	(276,309)	**–**	2.948	12 Jan 09
	150,000	–	–	–	**150,000**	–	26 Mar 10
	140,000	–	–	–	**140,000**	–	07 Apr 11
	–	225,000	–	–	**225,000**	–	02 Apr 12
RRS Hiscox	100,000	10,523	–	(110,523)	**–**	2.890	12 Jan 09
	80,000	–	–	–	**80,000**	–	26 Mar 10
	75,000	–	–	–	**75,000**	–	07 Apr 11
	–	50,000	–	–	**50,000**	–	02 Apr 12
BE Masojada	260,000	27,361	–	(287,361)	**–**	2.898	12 Jan 09
	200,000	–	–	–	**200,000**	–	26 Mar 10
	175,000	–	–	–	**175,000**	–	07 Apr 11
	–	275,000	–	–	**275,000**	–	02 Apr 12
Other employees	3,090,000	322,541	(10,000)	(2,492,961)	**909,580**	2.890-3.617	12 Jan 09
	25,000	2,631	–	(27,631)	**–**	2.948	13 Mar 09
	170,000	17,100	(7,500)	(124,338)	**55,262**	2.916-2.948	05 Oct 09
	2,101,500	–	(75,000)	–	**2,026,500**	–	26 Mar 10
	52,000	–	–	–	**52,000**	–	02 Oct 10
	1,606,500	–	(53,500)	–	**1,553,000**	–	07 Apr 11
	–	2,991,000	(85,000)	–	**2,906,000**	–	02 Apr 12
Total	8,920,000	4,170,090	(231,000)	(3,556,748)	**9,302,342**		

Directors' report

The Directors have pleasure in submitting their Annual Report and financial statements for the year ended 31 December 2009.

Principal activity and business review
The Company is a holding company for subsidiaries involved in the business of insurance in Bermuda, the US, the UK, Guernsey and Europe. An analysis of the development and performance of the business can be found within the Chief Executive's report on pages 5 to 11. A description of the major risks can be found in the risk management section on pages 21 to 25.

Financial results
The Group achieved a pre-tax profit for the year of £320.6 million (2008: £105.2 million). Detailed results for the year are shown in the consolidated income statement on page 48, and also within the Group financial performance section on pages 15 to 19.

Going concern
A review of the financial performance of the Group is set out on pages 15 to 19. The financial position of the Group, its cash flows and borrowing facilities are included therein. In addition, note 3 to the financial statements provides a detailed discussion on the risks which are inherent to the Group's business and how those risks are managed.

The Group has considerable financial resources and a well balanced book of business.

After making enquiries, the Directors have an expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.

Dividends
An interim dividend of 4.5p (net) per share (2008: 4.25p (net)) was paid on 6 October 2009 by Hiscox Ltd in respect of the year ended 31 December 2009. A second interim dividend of 10.5p (net) per share (2008: final dividend 8.5p (net)) will be paid on 29 March 2010 in respect of the year ended 31 December 2009.

Share capital
Details of the structure of the Company's share capital and changes in the share capital during the year are disclosed in note 25 to the consolidated financial statements.

Directors
The names and details of the individuals who served as Directors of the Company during the year are set out on pages 32 to 33.

Stuart Bridges and Robert Childs retire by rotation in accordance with the Bye-Laws of the Company and they have each submitted themselves for re-election at the Annual General Meeting of the Company.

One of our Directors, Sir Mervyn Pedelty, died in January 2010. Sir Mervyn had been the Chairman of the Remuneration and Nomination Committee and Senior Independent Director of Hiscox Ltd since redomicile.

Political and charitable contributions
The Group made no political contributions during the year (2008: £nil). Charitable donations totalled £1,171,000 (2008: £717,000) of which £1,000,000 (2008: £500,000) was donated to the Hiscox Foundation, a UK-registered charity. The policy of the Hiscox Foundation is to assist and improve education, the arts and independent living for disabled and disadvantaged members of society. Further information concerning the Group's charitable activities is contained in the report on Corporate responsibility on page 27.

Major interests in shares
The Company has been notified of the following shareholdings of 5% or more in the ordinary shares of the Company as at 1 March 2010:

	Number of shares	% of total
Invesco Limited	48,909,615	13.04
Jupiter Asset Management	25,210,566	6.4
Standard Life Investments	21,943,914	5.852
Legal & General	18,591,533	5.05
Massachusettes Financial Services Company	23,175,509	5.23

A copy of the Company's Bye-Laws is available for inspection at the Company's registered office.

Directors' report
continued

Annual General Meeting

The notice of Annual General Meeting, to be held at the Elbow Beach Hotel, 60 South Shore Road, Paget PG04, Bermuda on 9 June 2010 at 10.00am (2.00pm (BST)), is contained in a separate circular to shareholders enclosed with this report.

By order of the Board
Charles Dupplin, Secretary
Wessex House, 45 Reid Street,
Hamilton HM12, Bermuda
1 March 2010

Directors' interests

	31 December 2009 5p Ordinary Shares number of shares beneficial	31 December 2009 5p Ordinary Shares number of shares non-beneficial	31 December 2008 5p Ordinary Shares number of shares beneficial	31 December 2008 5p Ordinary Shares number of shares non-beneficial
Executive Directors				
RRS Hiscox	**6,600,196**	**550,000**	6,327,050	550,000
BE Masojada	**3,229,465**	**10,081,500**	2,941,304	10,081,500
RS Childs	**1,906,840**	**–**	1,794,043	–
SJ Bridges	**1,009,399**	**–**	744,774	–
Non Executive Directors				
DM Healy	**55,000**	**–**	55,000	–
ER Jansen	**–**	**–**	–	–
Dr J King	**–**	**–**	–	–
Sir Mervyn Pedelty	**18,000**	**–**	18,000	–
AS Rosen	**–**	**–**	–	–
G Stokholm	**–**	**–**	–	–
DA Stuurop	**50,000**	**–**	50,000	–

Directors' responsibilities statement

The Board is responsible for ensuring the maintenance of proper accounting records which disclose with reasonable accuracy the financial position of the Company. It is required to ensure that the financial statements present a fair view for each financial period.

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Directors' report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The Directors responsible for authorising the responsibility statement on behalf of the Board are the Chairman, RRS Hiscox, and the Group Finance Director, SJ Bridges. The statements were approved for issue on 1 March 2010.

Report of the independent registered public accounting firm to the Board of Directors and the shareholders of Hiscox Ltd

We have audited the accompanying consolidated financial statements of Hiscox Ltd ('the Company') on pages 48 to 99 which comprise the consolidated balance sheet as at 31 December 2009, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

In addition to our audit of the consolidated financial statements, the Directors have engaged us to audit the information in the Directors' remuneration report that is described as having been audited, which the Directors have decided to prepare (in addition to that required to be prepared) as if the Company were required to comply with the requirements of Section 421 of the UK Companies Act 2006.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and, under the terms of our engagement letter, to audit the part of the Directors' remuneration report that is described as having been audited.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements and the part of the Directors' remuneration report to be audited are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements and the part of the Directors' remuneration report to be audited. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements and the part of the Directors' remuneration report to be audited, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the entity's preparation and fair presentation of the consolidated financial statements and the part of the Directors' remuneration report to be audited in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and the part of the Directors' remuneration report to be audited.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

In addition to our audit of the consolidated financial statements, the Directors have engaged us to review their Corporate governance statement as if the Company were required to comply with the Listing Rules of the Financial Services Authority in relation to those matters. We review whether the Corporate governance statement reflects the Company's compliance with the nine provisions of the 2006 Combined Code specified for our review by those rules, and we report if it does not. We are not required by the terms of our engagement to consider whether the Board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

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

Opinion

In our opinion:

- the consolidated financial statements give a true and fair view of the consolidated financial position of the Company as at 31 December 2009, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU; and
- the part of the Directors' remuneration report which we were engaged to audit has been properly prepared in accordance with Schedule 7A to the UK Companies Act 1985, as if those requirements were to apply to the Company.

KPMG
Hamilton, Bermuda
1 March 2010

Consolidated income statement
For the year ended 31 December 2009

	Note	2009 Total £000	2008 Results excluding foreign currency items on economic hedges and intragroup borrowings £000	2008 Foreign currency items on economic hedges and intragroup borrowings (note 14) £000	2008 Total £000
Income					
Gross premiums written	4	**1,435,401**	1,147,364	–	1,147,364
Outward reinsurance premiums		**(278,378)**	(248,970)	–	(248,970)
Net premiums written	4	**1,157,023**	898,394	–	898,394
Gross premiums earned		**1,363,698**	1,171,511	–	1,171,511
Premiums ceded to reinsurers		**(265,596)**	(243,416)	–	(243,416)
Net premiums earned	4	**1,098,102**	928,095	–	928,095
Investment result – financial assets	7	**182,769**	(27,632)	–	(27,632)
Investment result – derivatives	7	**396**	(10,438)	(42,540)	(52,978)
Other revenues	9	**19,498**	19,858	–	19,858
Revenue		**1,300,765**	909,883	(42,540)	867,343
Expenses					
Claims and claim adjustment expenses, net of reinsurance	27.2	**(463,218)**	(479,380)	–	(479,380)
Expenses for the acquisition of insurance contracts	18	**(256,634)**	(227,943)	–	(227,943)
Administration expenses		**(112,627)**	(83,198)	–	(83,198)
Other expenses	9	**(116,939)**	(76,499)	–	(76,499)
Foreign exchange (losses)/gains		**(25,554)**	118,218	(8,463)	109,755
Total expenses		**(974,972)**	(748,802)	(8,463)	(757,265)
Results of operating activities		**325,793**	161,081	(51,003)	110,078
Finance costs	11	**(5,293)**	(5,158)	–	(5,158)
Share of profit of associates after tax	17	**118**	260	–	260
Profit before tax		**320,618**	156,183	(51,003)	105,180
Tax expense	29	**(40,121)**	(30,255)	(4,117)	(34,372)
Profit for the year (all attributable to owners of the Company)		**280,497**	125,928	(55,120)	70,808
Earnings per share on profit attributable to owners of the Company					
Basic	32	**75.2p**			18.8p
Diluted	32	**72.3p**			18.1p

Consolidated statement of comprehensive income
For the year ended 31 December 2009, after tax

	Note	2009 Total £000	2008 Results excluding foreign currency items on economic hedges and intragroup borrowings £000	2008 Foreign currency items on economic hedges and intragroup borrowings (note 14) £000	2008 Total £000
Profit for the year		**280,497**	125,928	(55,120)	70,808
Other comprehensive income					
Currency translation differences (net of tax of £nil (2008: £nil))		**(69,589)**	71,008	80,171	151,179
Net investment hedge (net of tax of £nil (2008: £(238,000)))		**–**	(597)	–	(597)
Total other comprehensive (loss)/income	13	**(69,589)**	70,411	80,171	150,582
Total comprehensive income recognised for the year (all attributable to owners of the Company)		**210,908**	196,339	25,051	221,390

The presentation of the consolidated income statement for the year ended 31 December 2008 has not been adopted in the current year as the current year amounts are insignificant both to the prior year amounts and overall result of the Group.

The notes on pages 52 to 99 are an integral part of these consolidated financial statements.

Consolidated balance sheet
At 31 December 2009

	Note	2009 £000	2008 £000
Assets			
Intangible assets	15	**50,413**	48,557
Property, plant and equipment	16	**22,244**	19,668
Investments in associates	17	**7,318**	7,200
Deferred tax	30	**14,077**	5,996
Deferred acquisition costs	18	**141,505**	131,130
Financial assets carried at fair value	20	**2,413,300**	2,081,772
Reinsurance assets	19, 27	**420,126**	503,794
Loans and receivables including insurance receivables	21	**488,782**	494,315
Current tax		**–**	26,289
Cash and cash equivalents	24	**259,647**	440,622
Total assets		**3,817,412**	3,759,343
Equity and liabilities			
Shareholders' equity			
Share capital	25	**20,158**	20,067
Share premium	25	**11,831**	9,418
Contributed surplus	25	**303,465**	352,078
Currency translation reserve	26	**37,728**	107,317
Retained earnings	26	**748,104**	462,146
Total equity (all attributable to owners of the Company)		**1,121,286**	951,026
Employee retirement benefit obligations	31	**–**	–
Deferred tax	30	**69,673**	74,645
Insurance liabilities	27	**2,122,351**	2,277,416
Financial liabilities	20	**138,539**	143,350
Current tax		**26,080**	–
Trade and other payables	28	**339,483**	312,906
Total liabilities		**2,696,126**	2,808,317
Total equity and liabilities		**3,817,412**	3,759,343

The notes on pages 52 to 99 are an integral part of these consolidated financial statements.

The consolidated Group financial statements were approved by the Board of Directors on 1 March 2010 and signed on its behalf by:

RRS Hiscox
Chairman

SJ Bridges
Group Finance Director

Consolidated statement of changes in equity

	Note	Share capital £000	Share premium £000	Contributed surplus £000	Currency translation reserve £000	Retained earnings £000	Total £000
Balance at 1 January 2008		19,898	4,955	398,834	(43,265)	443,882	824,304
Total recognised comprehensive income/(expense) for the year (all attributable to owners of the Company)		–	–	–	150,582	70,808	221,390
Employee share options:							
Equity settled share based payments	25	–	–	–	–	5,269	5,269
Excess tax benefit on share based payments		–	–	–	–	883	883
Proceeds from shares issued	25	169	4,463	–	–	–	4,632
Purchase of own shares held in treasury		–	–	–	–	(62,866)	(62,866)
Purchase of own shares held in trust		–	–	–	–	(2,200)	(2,200)
Deferred tax		–	–	–	–	6,370	6,370
Dividends paid to owners of the Company	33	–	–	(46,756)	–	–	(46,756)
Balance at 31 December 2008		20,067	9,418	352,078	107,317	462,146	951,026
Total recognised comprehensive income/(expense) for the year (all attributable to owners of the Company)		**–**	**–**	**–**	**(69,589)**	**280,497**	**210,908**
Employee share options:							
Equity settled share based payments	25	**–**	**–**	**–**	**–**	**5,260**	**5,260**
Excess tax benefit on share based payments		**–**	**–**	**–**	**–**	**–**	**–**
Proceeds from shares issued	25	**91**	**2,413**	**–**	**–**	**–**	**2,504**
Purchase of own shares held in treasury		**–**	**–**	**–**	**–**	**–**	**–**
Purchase of own shares held in trust		**–**	**–**	**–**	**–**	**–**	**–**
Deferred tax	30	**–**	**–**	**–**	**–**	**201**	**201**
Dividends paid to owners of the Company	33	**–**	**–**	**(48,613)**	**–**	**–**	**(48,613)**
Balance at 31 December 2009		**20,158**	**11,831**	**303,465**	**37,728**	**748,104**	**1,121,286**

The notes on pages 52 to 99 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows
For the year ended 31 December 2009

	Note	2009 £000	2008 £000
Profit before tax		**320,618**	105,180
Adjustments for:			
Interest and equity dividend income		**(78,298)**	(92,227)
Interest expense		**5,293**	5,158
Net fair value (gains)/losses on financial investments and derivatives		**(87,692)**	180,085
Depreciation and amortisation	15, 16	**6,046**	5,323
Charges in respect of share based payments	10	**5,260**	5,269
Other non-cash movements		**(975)**	(766)
Effect of exchange rate fluctuations on cash presented separately		**30,844**	(62,086)
Changes in operational assets and liabilities:			
Insurance and reinsurance contracts		**(58,366)**	281,633
Financial assets carried at fair value		**(338,556)**	(284,069)
Financial liabilities carried at fair value		**(52,533)**	–
Other assets and liabilities		**36,560**	(10,474)
Cash flows from operations		**(211,799)**	133,026
Interest received		**74,584**	89,608
Equity dividends received		**3,714**	2,619
Interest paid		**(5,066)**	(5,327)
Current tax paid		**(1,463)**	(18,982)
Net cash flows from operating activities		**(140,030)**	200,944
Cash outflow from the acquisition of subsidiary	34	**–**	(3,137)
Cash outflow from the sale of subsidiaries	35	**–**	(42)
Cash outflow from the acquisition of associates	17	**–**	(5,438)
Cash flows from the purchase of property, plant and equipment		**(8,802)**	(4,521)
Cash flows from the purchase of intangible assets		**(2,911)**	(3,530)
Net cash flows from investing activities		**(11,713)**	(16,668)
Proceeds from the issue of ordinary shares	25	**2,504**	4,632
Cash flows from the purchase of own shares including those arising on share buy-back programme	26	**–**	(65,066)
Dividends paid to owners of the Company	33	**(48,613)**	(46,756)
Net receipts/(repayments) of borrowings		**47,721**	(1,292)
Net cash flows from financing activities		**1,612**	(108,482)
Net (decrease)/increase in cash and cash equivalents		**(150,131)**	75,794
Cash and cash equivalents at 1 January		**440,622**	302,742
Net increase in cash and cash equivalents		**(150,131)**	75,794
Effect of exchange rate fluctuations on cash and cash equivalents		**(30,844)**	62,086
Cash and cash equivalents at 31 December	24	**259,647**	440,622

The purchase, maturity and disposal of financial assets is part of the Group's insurance activities and is therefore classified as an operating cash flow. The purchase, maturity and disposal of derivative contracts is also classified as an operating cash flow.

Included within cash and cash equivalents held by the Group are balances totalling £31,607,000 (2008: £47,094,000) not available for immediate use by the Group outside of the Lloyd's syndicate within which they are held.

The notes on pages 52 to 99 are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements

1 General information
The Hiscox Group, which is headquartered in Hamilton, Bermuda, comprises Hiscox Ltd (the parent Company, referred to herein as the 'Company') and its subsidiaries (collectively, the 'Hiscox Group' or the 'Group'). For the period under review the Group provided insurance and reinsurance services to its clients worldwide. It has operations in Bermuda, the UK, Europe, and the US and employs over 1,000 people.

The Company is registered and domiciled in Bermuda and on 12 December 2006 its ordinary shares were listed on the London Stock Exchange. As such it is required to prepare its annual audited financial information in accordance with Section 4.1 of the Disclosure and Transparency Rules and the Listing Rules, both issued by the Financial Services Authority (FSA), in addition to the Bermuda Companies Act 1981. The first two pronouncements issued by the FSA require the Group to prepare financial statements which comprise the consolidated income statement, the consolidated statement of comprehensive income, the consolidated balance sheet, the consolidated statement of changes in equity, the consolidated cash flow statement and the related notes 1 to 39 in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

The consolidated financial statements for the year ended 31 December 2009 include all of the Group's subsidiary companies and the Group's interest in associates. All amounts relate to continuing operations.

The financial statements were approved for issue by the Board of Directors on 1 March 2010.

2 Significant accounting policies
The principal accounting policies applied in the preparation of these consolidated Group financial statements are set out below. The most critical individual components of these financial statements that involve the highest degree of judgement or significant assumptions and estimations are identified at note 2.22.

2.1 Statement of compliance
The consolidated financial statements have been prepared in accordance with IFRS as adopted by the European Union and in accordance with the provisions of the Bermuda Companies Act 1981.

Since 2002, the standards adopted by the International Accounting Standards Board (IASB) have been referred to as IFRS. The standards from prior years continue to bear the title 'International Accounting Standards' (IAS). Insofar as a particular standard is not explicitly referred to, the two terms are used in these financial statements synonymously. Compliance with IFRS includes the adoption of interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC).

In March 2004, the IASB issued IFRS 4 Insurance Contracts which specifies the financial reporting for insurance contracts by an insurer. The standard is only the first phase in the IASB's insurance contract project and as such is only a stepping stone to phase II, introducing limited improvements to accounting for insurance contracts. Accordingly, to the extent that IFRS 4 does not specify the recognition or measurement of insurance contracts, transactions reported in these consolidated financial statements have been prepared in accordance with another comprehensive body of accounting principles for insurance contracts, namely accounting principles generally accepted in the UK.

During 2009, the IASB intensified its efforts to complete Phase II of its Insurance Contracts project. There were a number of key decisions made regarding the measurement approaches to be considered for inclusion within the new standard and the IASB is currently deciding on the detailed attributes of each approach. The aim of the IASB is to publish an Exposure Draft in the first half of 2010 and the final standard in 2011. The Group continues to monitor the progress of the project in order to assess any potential impact of the new standard on its results.

2.2 Basis of preparation
The financial statements are presented in Pounds Sterling and are rounded to the nearest thousand unless otherwise stated. They are compiled on a going concern basis and prepared on the historical cost basis except that pension scheme assets included in the measurement of the employee retirement benefit obligation, and certain financial instruments including derivative instruments are measured at fair value. Employee retirement benefit obligations are determined using actuarial analysis. The balance sheet of the Group is presented in order of increasing liquidity.

The accounting policies have been applied consistently by all Group entities, to all periods presented, solely for the purpose of producing the consolidated Group financial statements.

The comparative amounts reported herein for the year ended 31 December 2008, are as per those previously reported for that period, but have been adjusted for the reclassification of acquisition costs on the purchase of reinsurance contracts from 'Outward reinsurance premiums' to 'Expenses for the acquisition of insurance contracts'. The effect of the reclassification for the year ended 31 December 2008 is an increase to 'Outward reinsurance premiums' of £32,070,000, a decrease in 'Net premiums earned' of £24,925,000 and a decrease in 'Expenses for the acquisition of insurance contracts' of £24,925,000. The effect on the balance sheet for 31 December 2008 is an increase to 'Reinsurance assets' and an increase to 'Trade and other payables' of £16,074,000. The presentational adjustment has no impact on the Group's previously reported profit before tax, shareholders' equity or result from operating activities. The Directors' believe that the amended classification of the expense and commissions provides a more appropriate presentation of their operating nature.

The Group also reclassified the prior year comparative for deferred tax assets arising from overseas tax jurisdictions from net deferred tax liabilities to deferred tax assets. The reclassification provides a more appropriate presentation due to the increase of the asset. The effect of the reclassification is an increase to deferred tax assets and deferred tax liabilities of £5,996,000. The presentational adjustment has no impact on the Group's previously reported profit after tax, shareholders' equity or results from operating activities.

During the year, following a new geographic management structure including new business written through Syndicate 3624, the Group has changed its segmental reporting to provide more effective financial

2 Significant accounting policies continued
2.2 Basis of preparation continued

reporting for the evaluation of business segments by the chief operating decision maker to make decisions about future allocation of resources. The prior year segmental results have been restated accordingly.

The Group elected to apply the transitional arrangements contained in IFRS 4 that permitted the disclosure of only five years of data in claims development tables, in the year ended 31 December 2005 which was the year of adoption. The number of years of data presented was increased from eight in the prior year, to nine in the current financial year, and will be increased in 2010 up to a maximum of ten years if material outstanding claims exist for such periods.

The Group has financial assets and cash of over £2.6 billion. The portfolio is predominantly invested in liquid short-dated bonds and cash to ensure significant liquidity to the Group and to reduce risk from the financial markets. In addition the Group has significant borrowing facilities in place.

The Group writes a balanced book of insurance and reinsurance business spread by product and geography. The Directors believe that the current reinsurance and insurance markets are favourable and that the Group is well placed to trade in these markets whilst successfully managing its business risks.

A review of the financial performance of the Group is set out on pages 15 to 19. The financial position of the Group, its cash flows and borrowing facilities are included therein. In addition, note 3 to the financial statements provides a detailed discussion on the risks which are inherent to the Group's business and how those risks are managed.

The Group has considerable financial resources and a well balanced book of business.

The Directors have an expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

The Group early adopted IFRS8 Operating Segments from 1 January 2010.

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted, for the first time, the following new and amended Standards and Interpretations issued by the IASB and endorsed by the EU as of 1 January 2009.

- Amendments to IAS 39 Financial Instruments: Recognition and Measurement and IFRS 7 Financial Instruments: Disclosures (Amendment)
- Amendments to IFRS 7 Financial Instruments: Disclosure
- Amendments to IAS 32 Financial Instrument: Presentation and IAS 1 Presentation of Financial Statements - Puttable Financial Instruments and Obligations Arising on Liquidation
- Amendments to IAS 23 Borrowing Costs
- Improvements to IFRS

Adoption of the above had no impact on the financial performance or position of the Group.

Amendments to IAS 39 Financial Instruments: Recognition and measurement and IFRS 7 Financial Instruments: Disclosures (Amendment)
The amendments to IAS 39 and IFRS 7 were issued in response to the global market credit crisis in October 2008. The standard was effective retrospectively from 1 July 2008 to 1 November 2008. Thereafter, retrospective application was not permitted.

The amended standard permitted an entity to reclassify certain financial assets out of 'Held-for-Trading' if they were no longer held for the purpose of being sold, or repurchased, in the near term. The standard also allowed for those financial assets which are not eligible for classification as loans and receivables to be transferred from 'Held-for-Trading' to 'Available-for-Sale' or 'Held-to-Maturity' only in exceptional circumstances. IFRS 7 was amended to require disclosure of information for any reclassifications of assets described above to include amounts and any gains or losses.

The amendment had no impact on the Group's results.

Amendments to IFRS 7 Financial Instruments: Disclosure
The amendments to the standard enhance the disclosure requirements over fair value measurement and liquidity risk. The standard requires disclosure of those instruments measured at fair value by reference to the source of input used in determining fair value. The instruments are to be categorised using a three-level fair value hierarchy with those instruments with the most reliable method of determining fair value being classified as Level 1. For those instruments which have significant unobservable inputs, Level 3, the amendment requires a reconciliation of the opening and closing balance. In addition, transfers between each level of the hierarchy are to be disclosed. The standard also amends the previous liquidity risk disclosures for non derivative and derivative financial liabilities.

The standard is applicable prospectively and no comparatives are required on transition. However, the Group has voluntarily provided comparatives.

Amendments to IAS 32 Financial Instrument: Presentation and IAS 1 Presentation of Financial Statements- Puttable Financial Instruments and Obligations Arising on Liquidation
The amendments were issued in February 2008 and provide a limited scope exception for puttable financial instruments to be classified as equity if certain specified features are fulfilled. The amendments are effective for financial periods beginning on or after 1 January 2009. There is no impact on the Group's financial performance as it has not issued such instruments.

Amendment to IAS 23 Borrowing Cost
The amendment makes it compulsory to capitalise borrowing costs relating to qualifying assets and removes the option to expense such costs. The amendment excludes eligible assets measured at fair value from the revised standard's scope of application. The amendment had no impact on the Group's results.

Improvements to IFRSs
Improvements to IFRSs is an annual process which has been undertaken by the IASB with the view of removing inconsistencies and clarifying wording within the standards. In May 2008, the IASB issued the first in the series of these amendments with separate transitional arrangements for each standard. The following lists the main applicable improvements which have been adopted by the Group from 1 January 2009:

IFRS 7 Financial Instruments: Disclosures: removes the reference to 'total interest income' as a component of finance costs. This had no impact on the Group's accounting policy or financial position as this was already applied.

IAS 8 Accounting Policies: clarifies that only implementation guidance that is an integral part of an IFRS is mandatory when selecting accounting policies. This had no impact on the Group's accounting policy or financial position as this was already applied.

Notes to the consolidated financial statements continued

2 Significant accounting policies continued
2.2 Basis of preparation continued

IAS 10 Events After the Reporting Period: clarifies that dividends declared after the end of the reporting period are not obligations. This had no impact on the Group's accounting policy or financial position as this was already applied.

IAS 16 Property, Plant and Equipment: replaces the term 'net selling price' with 'fair value less costs to sell'. The Group has amended its accounting policy accordingly which did not result in any change in the financial position.

IAS 19 Employee Benefits: revised the definition of 'past service costs' to include reductions in benefits related to past services and to exclude the deduction in benefits related to future services that arise from plan amendments. The term 'return on plan assets' was revised to exclude plan administration costs if they have already been included in the actuarial assumptions. In addition, the definition of 'short-term' and 'other long-term' employee benefits was amended to focus on the point in time at which a liability is due to be settled. Finally, the reference to the recognition of contingent liabilities has been deleted. The amendment had no impact on the accounting policy and financial position of the Group as the definitions were consistent with the amendment.

Standards and interpretations issued but not yet effective or not yet endorsed by the EU
IFRS 9 – Financial Instruments (not endorsed)
Part I of the three-part project of the new standard for financial instruments was issued by the IASB in November 2009 and is applicable for accounting periods commencing 1 January 2013 although early adoption is permitted. The two remaining parts of the standard are Part II, Amortised Cost and Impairment and Part III, Hedge Accounting, both of which are expected to be issued in 2010.

IFRS 9, Part I reduces the classification and measurement categories of financial instruments to two, being fair value or amortised cost. To classify financial assets as amortised cost they must have basic loan features and be managed on a contractual yield basis. In addition, the classification must also be based on the business model as 'determined by key management personnel'. The new standard currently does not address how to measure financial liabilities and the IASB are currently considering including credit risk in measuring financial liabilities. It is expected to issue final requirements for this in 2010.

IFRS 3 (Revised) Business Combinations and IAS 27 (Amended) Consolidated and Separate Financial Statements (endorsed)
The revised standards were issued in January 2008 and are applicable for accounting periods commencing on or after 1 July 2009. IFRS 3 incorporates a number of changes in accounting for business combinations which will impact the amount of goodwill recognised and the results reported in the period of the combination and future reporting periods. IAS 27 requires that a change in the ownership interest of a subsidiary, provided that control is maintained, to be accounted for as an equity transaction. As such, a transaction of this nature will no longer give rise to goodwill nor gain or loss.

The Group has not early adopted these standards.

2.3 Basis of consolidation
(a) Subsidiaries
Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Generally this occurs when the Group obtains a shareholding of more than half of the voting rights of an entity. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account. Management also exercise significant judgement about any actual or perceived control acquired indirectly, through normal commercial dealings with entities of a special purpose nature. The Group does not undertake any such arrangements with such entities where control of that entity would be acquired. The consolidated financial statements include the assets, liabilities and results of the Group up to 31 December each year. The financial statements of subsidiaries are included in the consolidated financial statements only from the date that control commences until the date that control ceases.

Hiscox Dedicated Corporate Member Limited underwrites as a corporate member of Lloyd's on the main Syndicates managed by Hiscox Syndicates Limited (the 'main managed Syndicates' numbered 33 and, commencing 1 January 2009, 3624).
In view of the several but not joint liability of underwriting members at Lloyd's for the transactions of syndicates in which they participate, the Group's attributable share of the transactions, assets and liabilities of these Syndicates has been included in the financial statements. The Group manages the underwriting of, but does not participate as a member of, Syndicate 6104 at Lloyd's which provides reinsurance to Syndicate 33 on a normal commercial basis. Consequently, aside from the receipt of managing agency fees and defined profit commissions as appropriate, the Group has no share in the assets, liabilities or transactions of Syndicate 6104, nor is it controlled. The position and performance of that Syndicate is therefore not included in the Group's financial statements.

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

(b) Associates
Associates are those entities in which the Group has significant influence but not control over the financial and operating policies. Significant influence is generally identified with a shareholding of between 20% and 50% of an entity's voting rights. The consolidated financial statements include the Group's share of the total recognised gains and losses of associates on an equity accounted basis from the date that significant influence commences until the date that significant influence ceases. The Group's share of its associates' post-acquisition profits or losses after tax is recognised in the income statement each period, and its share of the movement in the associates' net assets is reflected in the investments' carrying values in the balance sheet. When the Group's share of losses equals or exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

2 Significant accounting policies continued
2.3 Basis of consolidation continued

(c) Transactions eliminated on consolidation
Intragroup balances, transactions and any unrealised gains arising from intragroup transactions are eliminated in preparing the consolidated financial statements. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. In accordance with IAS 21, foreign currency gains and losses on intragroup monetary assets and liabilities may not fully eliminate on consolidation when the intragroup monetary item concerned is transacted between two Group entities that have different functional currencies.

Unrealised gains arising from transactions with associates are eliminated to the extent of the Group's interest in the entity. Unrealised gains arising from transactions with associates are eliminated against the investment in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

2.4 Foreign currency translation
(a) Functional and presentational currency
Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The functional currency of all individual entities in the Group is deemed to be Sterling with the exception of the entities operating in France, Germany, the Netherlands and Belgium whose functional currency is Euros, those subsidiary entities operating from the US and Bermuda whose functional currency is US Dollars, Hiscox Insurance Company (Guernsey) Limited and Syndicate 3624 whose functional currency is also US Dollars.

(b) Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the retranslation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as IAS 39 effective net investment hedges or when the underlying balance is deemed to form part of the Group's net investment in a subsidiary operation and is unlikely to be settled in the forseeable future.

Non-monetary items carried at historical cost are translated in the balance sheet at the exchange rate prevailing on the original transaction date. Non-monetary items measured at fair value are translated using the exchange rate ruling when the fair value was determined.

(c) Group companies
The results and financial position of all the Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- (i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- (ii) income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the date of the transactions); and
- (iii) all resulting exchange differences are recognised as a separate component of equity.

When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as the foreign entity's assets and liabilities and are translated at the closing rate.

2.5 Property, plant and equipment
Property, plant and equipment are stated at historical cost less depreciation and any impairment loss. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance items are charged to the income statement during the financial period in which they are incurred.

Land and artwork assets are not depreciated as they are deemed to have indefinite useful economic lives. The cost of leasehold improvements is amortised over the unexpired term of the underlying lease or the estimated useful life of the asset, whichever is shorter. Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts, less their residual values, over their estimated useful lives. The rates applied are as follows:

— buildings	50 years
— vehicles	3 years
— leasehold improvements including fixtures and fittings	10–15 years
— furniture, fittings and equipment	3–15 years

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

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

2.6 Intangible assets
(a) Goodwill
Goodwill represents amounts arising on acquisition of subsidiaries and associates. In respect of acquisitions that have occurred since 1 January 2004, goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets and contingent liabilities assured of the acquired subsidiary or associate at the acquisition date.

In respect of acquisitions prior to this date, goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous generally accepted accounting principles.

Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates. Goodwill is not amortised but is tested annually for impairment and carried at cost less accumulated impairment losses. The impairment review process examines whether or not the carrying value of the goodwill attributable to individual cash generating units exceeds its implied value. Any excess of goodwill over the recoverable amount arising from the review process indicates impairment. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Notes to the consolidated financial statements continued

2 Significant accounting policies continued
2.6 Intangible assets continued

(b) Syndicate capacity
The cost of purchasing the Group's participation in the Lloyd's insurance syndicates is not amortised but is tested annually for impairment and is carried at cost less accumulated impairment losses. Having considered the future prospects of the London insurance market, the Board believe that the Group's ownership of syndicate capacity will provide economic benefits over an indefinite number of future periods.

(c) State authorisation licences
State authorisation licences acquired in business combinations are recognised initially at their fair value. The asset is not amortised, as the Board considers that economic benefits will accrue to the Group over an indefinite number of future periods, but is tested annually for impairment, and any accumulated impairment losses recognised are deducted from the historical cost amount to produce the net balance sheet carrying amount.

(d) Rights to customer contractual relationships
Costs directly attributable to securing the intangible rights to customer contract relationships are recognised as an intangible asset where they can be identified separately and measured reliably and it is probable that they will be recovered by directly related future profits. These costs are amortised on a straight-line basis over the useful economic life which is deemed to be 20 years and are carried at cost less accumulated amortisation and impairment losses.

(e) Computer software
Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring into use the specific software. These costs are amortised over the expected useful life of the software of between three and five years on a straight-line basis.

Internally developed computer software is only capitalised where the cost can be measured reliably, the Group intends to and has adequate resources to complete development, and where the computer software will yield future economic benefits in excess of the costs incurred.

2.7 Financial assets including loans and receivables
The Group has classified financial assets as a) financial assets designated at fair value through profit or loss, and b) loans and receivables. Management determines the classification of its financial investments at initial recognition. The decision by the Group to designate all financial investments, comprising debt and fixed income securities, equities and shares in unit trusts and deposits with credit institutions, at fair value through profit or loss reflects the fact that the investment portfolios are managed, and their performance evaluated, on a fair value basis. Regular way purchases and sales of investments are accounted for at the date of trade.

Financial assets are initially recognised at fair value. Subsequent to initial recognition financial assets are measured as described below.

Financial assets are de-recognised when the right to receive cash flows from them expires or where they have been transferred and the Group has also transferred substantially all risks and rewards of ownership.

Fair value for securities quoted in active markets is the bid price exclusive of transaction costs. For instruments where no active market exists, fair value is determined by referring to recent transactions and other valuation factors including the discounted value of expected future cash flows. Fair value changes are recognised immediately within the investment result line in the income statement. An analysis of fair values of financial instruments and further details as to how they are measured are provided in note 23.

(a) Financial assets at fair value through profit or loss
A financial asset is classified into this category at inception if it is managed and evaluated on a fair value basis in accordance with documented strategy, if acquired principally for the purpose of selling in the short-term, or if it forms part of a portfolio of financial assets in which there is evidence of short-term profit taking.

(b) Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. Receivables arising from insurance contracts are included in this category and are reviewed for impairment as part of the impairment review of loans and receivables. Loans and receivables are carried at amortised cost less any provision for impairment in value.

2.8 Cash and cash equivalents
The Group has classified cash deposits and short-term highly liquid investments as cash and cash equivalents. These assets are readily convertible into known amounts of cash and are subject to inconsequential changes in value. Cash equivalents are financial investments with less than three months to maturity at the date of acquisition.

2.9 Impairment of assets
Assets that have an indefinite useful life are not subject to amortisation and are tested annually or whenever there is an indication of impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

(a) Non-financial assets
Objective factors that are considered when determining whether a non-financial asset (such as goodwill, an intangible asset or item of property, plant and equipment) or group of non-financial assets may be impaired include, but are not limited to, the following:
- adverse economic, regulatory or environmental conditions that may restrict future cash flows and asset usage and/or recoverability;
- the likelihood of accelerated obsolescence arising from the development of new technologies and products; and
- the disintegration of the active market(s) to which the asset is related.

(b) Financial assets
Objective factors that are considered when determining whether a financial asset or group of financial assets may be impaired include, but are not limited to, the following:
- negative rating agency announcements in respect of investment issuers, reinsurers and debtors;
- significant reported financial difficulties of investment issuers, reinsurers and debtors;
- actual breaches of credit terms such as persistent late payments or actual default;
- the disintegration of the active market(s) in which a particular asset is traded or deployed;
- adverse economic or regulatory conditions that may restrict future cash flows and asset recoverability; and
- the withdrawal of any guarantee from statutory funds or sovereign agencies implicitly supporting the asset.

(c) Impairment loss
An impairment loss is recognised for the amount by which the asset's carrying

amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units).

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior periods. A reversal of an impairment loss is recognised as income immediately. Impairment losses recognised in respect of goodwill are not subsequently reversed.

2.10 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently valued at their fair value at each balance sheet date. Fair values are obtained from quoted market values and, if these are not available, valuation techniques including option pricing models as appropriate. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. For derivatives not formally designated as a hedging instrument, fair value changes are recognised immediately in the income statement. Changes in the value of derivatives and other financial instruments formally designated as hedges of net investments in foreign operations are recognised in the currency translation reserve to the extent they are effective; gains or losses relating to the ineffective portion of the hedging instruments are recognised immediately in the consolidated income statement.

The Group had no derivative instruments designated for hedge accounting during the current and prior financial year (see note 2.17).

2.11 Own shares

Where any Group company purchases the parent Company's equity share capital (own shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to the Company's owners on consolidation. Where such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity attributable to the Company's owners, net of any directly attributable incremental transaction costs and the related tax effects.

2.12 Revenue

Revenue comprises insurance and reinsurance premiums earned on the rendering of insurance protection, net of reinsurance, together with profit commission, investment returns, agency fees and other income inclusive of fair value movements on derivative instruments not formally designated for hedge accounting treatment. The Group's share of the results of associates is reported separately. The accounting policies for insurance premiums are outlined below. Profit commission, investment income and other sources of income are recognised on an accruals basis net of any discounts and amounts such as sales-based taxes collected on behalf of third-parties.

2.13 Insurance contracts

(a) Classification

The Group issues short-term casualty and property insurance contracts that transfer significant insurance risk. Such contracts may also transfer a limited level of financial risk.

(b) Recognition and measurement

Gross premiums written comprise premiums on business incepting in the financial year together with adjustments to estimates of premiums written in prior accounting periods. Estimates are included for pipeline premiums and an allowance is also made for cancellations. Premiums are stated before the deduction of brokerage and commission but net of taxes and duties levied. Premiums are recognised as revenue (premiums earned) proportionally over the period of coverage. The portion of premium received on in-force contracts that relates to unexpired risks at the balance sheet date is reported as the unearned premium liability.

Claims and associated expenses are charged to profit or loss as incurred based on the estimated liability for compensation owed to contract holders or third-parties damaged by the contract holders. They include direct and indirect claims settlement costs and arise from events that have occurred up to the balance sheet date even if they have not yet been reported to the Group. The Group does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are estimated using the input of assessments for individual cases reported to the Group and statistical analysis for the claims incurred but not reported, and an estimate of the expected ultimate cost of more complex claims that may be affected by external factors e.g. court decisions.

(c) Deferred acquisition costs (DAC)

Commissions and other direct and indirect costs that vary with and are related to securing new contracts and renewing existing contracts are capitalised as deferred acquisition costs. All other costs are recognised as expenses when incurred. DAC are amortised over the terms of the insurance contracts as the related premium is earned.

(d) Liability adequacy tests

At each balance sheet date, liability adequacy tests are performed by each segment of the Group to ensure the adequacy of the contract liabilities net of related DAC. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from assets backing such liabilities, are used. Any deficiency is immediately charged to profit or loss initially by writing-off DAC and by subsequently establishing a provision for losses arising from liability adequacy tests ('the unexpired risk provision'). Any DAC written-off as a result of this test cannot subsequently be reinstated.

(e) Outwards reinsurance contracts held

Contracts entered into by the Group, with reinsurers, under which the Group is compensated for losses on one or more insurance or reinsurance contracts and that meet the classification requirements for insurance contracts, are classified as insurance contracts held. Contracts that do not meet these classification requirements are classified as financial assets.

The benefits to which the Group is entitled under outwards reinsurance contracts are recognised as reinsurance assets. These assets consist of short-term balances due from reinsurers (classified within loans and receivables) as well as longer-term receivables (classified as reinsurance assets) that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts.

Reinsurance liabilities primarily comprise premiums payable for 'outwards' reinsurance contracts. These amounts are recognised in profit or loss proportionally over the period of the contract. Receivables and payables are recognised when due.

The Group assesses its reinsurance assets on a regular basis and, if there is objective evidence, after initial recognition, of an impairment in value, the Group reduces the

Notes to the consolidated financial statements continued

2 Significant accounting policies continued
2.13 Insurance contracts continued
(e) Outwards reinsurance contracts held *continued*

carrying amount of the reinsurance asset to its recoverable amount and recognises the impairment loss in the income statement.

(f) Receivables and payables related to insurance contracts
Receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders.

If there is objective evidence that the insurance receivable is impaired, the Group reduces the carrying amount of the insurance receivable accordingly and recognises the impairment loss in profit or loss.

(g) Salvage and subrogation reimbursements
Some insurance contracts permit the Group to sell property acquired in settling a claim (i.e. salvage). The Group may also have the right to pursue third-parties for payment of some or all costs (i.e. subrogation). Estimates of salvage recoveries are included as an allowance in the measurement of the insurance liability for claims and salvage property is recognised in other assets when the liability is settled. The allowance is the amount that can reasonably be recovered from the disposal of the property.

Subrogation reimbursements are also considered as an allowance in the measurement of the insurance liability for claims and are recognised in other assets when the liability is settled. The allowance is the assessment of the amount that can be recovered from the action against the liable third-party.

2.14 Deferred tax
Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not recognised. Deferred tax is determined using tax rates and laws that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled. Deferred tax assets are recognised to the extent that it is probable that the future taxable profit will be available against which the temporary differences can be utilised. Deferred tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

2.15 Employee benefits
(a) Pension obligations
The Group operated both defined contribution and defined benefit pension schemes during the year under review. The defined benefit scheme closed to future accrual with effect from 31 December 2006 and active members were offered membership of the defined contribution scheme from 1 January 2007.

A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity and has no further obligation beyond the agreed contribution rate. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation.

For defined contribution plans, the Group pays contributions to publicly or privately administered pension insurance plans on a contractual basis. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

The amount recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. Plan assets exclude any insurance contracts issued by the Group. To the extent that a surplus emerges on the defined benefit obligation, it is only recognisable on the asset side of the balance sheet when it is probable that future economic benefits will be recovered by the scheme sponsor in the form of refunds or reduced future contributions.

Actuarial gains and losses are only recognised when the net cumulative unrecognised actuarial gains and losses for each individual plan at the end of the previous accounting period exceeds 10% of the higher of the defined benefit obligation and the fair value of the plan assets at that date. Such actuarial gains or losses falling outside of this 10% corridor are charged or credited to income over the employees' expected average remaining working lives.

Past service costs are recognised immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortised on a straight-line basis over the vesting period.

(b) Other long-term employee benefits
The Group provides sabbatical leave to employees on completion of a minimum service period of ten years. The present value of the expected costs of these benefits is accrued over the period of employment. In determining this liability, consideration is given to future increases in salary levels, experience with employee departures and periods of service.

(c) Share based compensation
The Group operates a number of equity settled share based employee compensation plans. These include both the approved and unapproved share option schemes, and the Group's performance share plans, outlined in the Directors' remuneration report together with the Group's Save as You Earn (SAYE) schemes.

The fair value of the employee services received, measured at grant date, in exchange for the grant of the awards is recognised as an expense with the corresponding credit being recorded in retained earnings within equity. The total amount to be expensed over the vesting period is determined by reference to the fair value of the awards granted, excluding the impact of any non-market vesting conditions (e.g. profitability or net asset growth targets). Non-market vesting conditions are included in assumptions about the number of awards that are expected to become exercisable. At each balance sheet date, the Group revises its estimates of the number of awards that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity, over the remaining vesting period.

When the terms and conditions of an equity settled share based employee

2 Significant accounting policies continued
2.15 Employee benefits continued
(c) Share based compensation continued

compensation plan are modified, and the expense to be recognised increases as a result of the modification, then the increase is recognised evenly over the remaining vesting period. When a modification reduces the expense to be recognised, there is no adjustment recognised and the pre-modification expense continues to be applied. The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium when the options are exercised.

In accordance with the transitional arrangements of IFRS 2 only share based awards granted or modified after 7 November 2002, but not yet vested at the date of adoption of IFRS, are included in the calculations.

(d) Termination benefits
Termination benefits are payable when employment is terminated before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

(e) Profit sharing and bonus plans
The Group recognises a liability and an expense for bonuses and profit sharing, based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The Group recognises a provision where a contractual obligation to employees exists or where there is a past practice that has created a constructive obligation.

(f) Accumulating compensation benefits
The Group recognises a liability and an expense for accumulating compensation benefits (e.g. holiday entitlement), based on the additional amount that the Group expects to pay as a result of the unused entitlement accumulated at the balance sheet date.

2.16 Financial liabilities
All borrowings drawn after 6 May 2008 are now measured at amortised cost at each balance sheet date thereafter using the effective interest method. Any difference between the remeasured amortised cost carrying amount and the ultimate redemption amount is recognised in the income statement over the period of the borrowings.

Up to 6 May 2008 (when all existing borrowings were repaid in full), borrowings were measured at fair value at each balance sheet date using observable market interest rate data for similar instruments, with all changes in value from one accounting period to the next reflected in the income statement unless they formed part of a designated hedge accounting relationship in which case certain changes in value were recognised directly in equity, (see notes 2.17 and 20).

2.17 Net investment hedge accounting
In order to qualify for hedge accounting, the Group is required to document in advance the relationship between the item being hedged and the hedging instrument. The Group is also required to document and demonstrate an assessment of the relationship between the hedged item and the hedging instrument, which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is re-performed at each period end to ensure that the hedge remains highly effective.

The Group hedged elements of its net investment in certain foreign entities through foreign currency borrowings that qualified for hedge accounting from 3 January 2007 until their replacement on 6 May 2008; accordingly gains or losses on retranslation are recognised in equity to the extent that the hedge relationship was effective during this period. Accumulated gains or losses will be recycled to the income statement only when the foreign operation is disposed of. The ineffective portion of any hedge is recognised immediately in the income statement.

2.18 Finance costs
Finance costs consist of interest charges accruing on the Group's borrowings and bank overdrafts together with commission fees charged in respect of letters of credit. Arrangement fees in respect of financing arrangements are charged over the life of the related facilities.

2.19 Provisions
The Group is subject to various insurance-related assessments and guarantee fund levies. Provisions are recognised where there is a present obligation (legal or constructive) as a result of a past event that can be measured reliably and it is probable that an outflow of economic benefits will be required to settle that obligation.

2.20 Leases
(a) Hiscox as lessee
Leases in which significantly all of the risks and rewards of ownership are transferred to the Group are classified as finance leases. At the commencement of the lease term, finance leases are recognised as assets and liabilities at the lower of the fair value of the asset and the present value of the minimum lease payments. The minimum lease payments are apportioned between finance charges and repayments of the outstanding liability, finance charges being charged to each period of the lease term so as to produce a constant rate of interest on the outstanding balance of the liability. All other leases are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

(b) Hiscox as lessor
Rental income from operating leases is recognised on a straight-line basis over the term of the relevant contractual agreement.

2.21 Dividend distribution
Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved.

2.22 Use of critical estimates, judgements and assumptions
The preparation of financial statements requires the use of significant estimates, judgements and assumptions. The Directors consider the accounting policies for determining insurance liabilities, the valuation of investments, the valuation of retirement benefit scheme obligations and the determination of current and deferred tax assets and liabilities as being most critical to an understanding of the Group's result and position.

The inherent uncertainty of insurance risk requires the Group to make estimates, judgements and assumptions that affect the amounts of insurance and reinsurance assets and liabilities reported in the balance sheet date. This includes estimates for losses incurred but not reported. This is the most significant area of potential uncertainty in the Group's financial statements.

There are several sources of uncertainty that need to be considered in the estimation of the insurance liabilities that the Group will ultimately pay for valid claims. These include but are not restricted to: inflation; changes in legislation; changes in the Group's claims handling procedures; and judicial opinions which extend the Group's coverage

Notes to the consolidated financial statements continued

2 Significant accounting policies continued
2.22 Use of critical estimates, judgements and assumptions continued

of risk beyond that envisaged at the time of original policy issuance. The Group seeks to gather corroborative evidence from all relevant sources before making judgements as to the eventual outcome of claims, particularly those under litigation, which have occurred and been notified to the Group but remain unsettled at the balance sheet date.

Estimates of insurance liabilities are continually evaluated based on entity specific historical experience and contemporaneous developments observed in the wider industry when relevant, and are also updated for expectations of prospective future developments. Although the possibility exists for material changes in insurance liability estimates to have a critical impact on the Group's reported performance and financial position, it is anticipated that the scale and diversity of the Group's portfolio of insurance business considerably lessens the likelihood of this occurring. Note 27 to the consolidated financial statements provides a greater analysis of the main methods used by the Group when formulating estimates of the insurance claims liabilities at each balance sheet date.

The Group carries its financial investments at fair value through profit or loss with fair value determined using published price quotations in the most active financial markets in which the assets trade. During periods of economic distress and diminished liquidity, the ability to obtain quoted bid prices may be reduced and as such a greater degree of judgement is required in obtaining the most reliable source of valuation. Note 3.2 to the financial statements discusses the reliability of the Group's fair values.

With regard to employee retirement benefit scheme obligations, the amounts disclosed in these consolidated financial statements are sensitive to judgemental assumptions regarding mortality, inflation, investment returns and interest rates on corporate bonds, many of which have been subject to specific recent volatility. This complex set of economic variables may be expected to influence the liability obligation element of the reported net balance amount to a greater extent than the reported value of the scheme assets element. For example, if the recent cuts in official UK interest rates are replicated with lower yields emerging in UK corporate bond indices, a significant uplift may occur in the reported net scheme deficit through the reduced effect of discounting outweighing any expected appreciation in asset values. A sensitivity analysis is given at note 31.

Legislation concerning the determination of taxation assets and liabilities is complex and continually evolving. In preparing the Group's financial statements, the Directors estimate taxation assets and liabilities after taking appropriate professional advice. The determination and finalisation of agreed taxation assets and liabilities may not occur until several years after the balance sheet date and consequently the final amounts payable or receivable may differ from those presently recorded in these financial statements.

2.23 Reporting of additional performance measures
The Directors consider that the claims ratio, expense ratio and combined ratio measures reported in respect of operating segments and the Group overall at note 4 provide useful information regarding the underlying performance of the Group's businesses. These measures are widely recognised by the insurance industry and are consistent with internal performance measures reviewed by senior management including the chief operating decision maker. However, these three measures are not defined within the IFRS framework and body of standards and interpretations and therefore may not be directly comparable with similarly titled additional performance measures reported by other companies. Net asset value per share and return on equity measures, disclosed at notes 5 and 6, are likewise considered to be additional performance measures.

3 Management of risk
Overview of risk
The Group enters into contracts that directly accept and transfer insurance risk, which in turn necessarily creates exposure to financial and other classes of risk. Consequently, Hiscox is fundamentally concerned with the identification and management of all significant risks.

The Group's overall appetite for accepting and managing varying classes of risk is defined by the Group's Board. The Board has developed a governance framework and set Group-wide risk management policies and procedures which cover specific areas such as risk identification, risk management and mitigation, and risk reporting. The objective of these policies and procedures is to protect the Group's shareholders, policyholders and other stakeholders from negative events that could hinder the Group's delivery of its contractual obligations and its achievement of sustainable profitable economic and social performance.

The Board exercises oversight of the development and operational implementation of its risk management policies and procedures, and ongoing compliance therewith, partially through its own enquiries but primarily through a dedicated internal audit function, which has operational independence, clear terms of reference influenced by the Board's Non Executive Directors and a clear upwards reporting structure back into the Board.

The main sources of risk relevant to the Group's operations and its financial statements fall into two broad categories: insurance risk and financial risk. Note 3.1 details the Group's approach to managing insurance risk specifically whilst note 3.2 onwards outlines the Group's sensitivity to financial risk generally. Additional unaudited information is also provided in the corporate governance and risk management sections of this Report and Accounts.

The Group, in common with the non-life insurance industry generally, is fundamentally driven by a desire to originate, retain and service insurance contracts to maturity, rather than engaging in mass distribution of the risks assumed through large scale securitisation. The Group's business is therefore fundamentally different from other types of financial institutions in that its cash flows are funded mainly through advance premium collections rather than assuming cash deposits, and the timing of such premium inflows is reasonably predictable. In addition, the majority of material cash outflows are typically triggered by the occurrence of insured events non-correlated to financial markets, and not by the inclination or will of policyholders.

Consequently, as the Group therefore has the capacity to invest and hold a significant proportion of assets to maturity if required, it has the ability for many of its ultimate cash flows to remain relatively immune to short-term, technically driven accounting losses in fair value terms.

3.1 Insurance risk
Insurance risk is transferred to the Group by contract holders through the underwriting process. The Group's exposure to insurance risk arises from the possibility

3 Management of risk continued
3.1 Insurance risk continued

that an insured event occurs, and a claim is subsequently submitted by the insured for payment. Management of insurance risk on a day-to-day basis is the responsibility of the Chief Underwriting Officer, who receives assistance from the management information and risk modelling departments. The Board sets the Group's underwriting strategy for accepting and managing insurance risk prospectively, seeking to exploit identified opportunities and taking cognisance of other relevant anticipated market conditions. Specific underwriting objectives such as aggregation limits, reinsurance protection thresholds, geographical disaster event risk exposures and line of business diversification parameters are prepared and reviewed by the Chief Underwriting Officer in order to translate the Board's summarised underwriting strategy into specific measurable actions and targets. These actions and targets are reviewed and approved by the Board in advance of each underwriting year. The Board continually reviews its underwriting strategy throughout each underwriting year in light of the evolving market pricing and loss conditions and as opportunities present themselves.

The Board requires all underwriters to operate within an overall Group appetite for individual events. This defines the maximum exposure that the Group is prepared to retain on its own account for any one potential catastrophe event or disaster. The Group's underwriting risk appetite seeks to ensure that it should not lose more than one year's profit plus 15% of core capital as a result of a 1 in 250 year event.

Realistic disaster scenarios are extreme, hypothetical events selected to represent major events occurring in areas with large insured values. They also reflect the areas that represent significant exposures for Hiscox. The Group compiles estimates of losses arising from realistic disaster events using statistical models alongside input from its underwriters. The selection of realistic disaster scenario events is adjusted each year and they are not therefore necessarily directly comparable from one year to the next. The events are extreme and as yet untested, and as such these estimates may prove inadequate as a result of incorrect assumptions, model deficiencies, or losses from unmodelled risks. This means that should a realistic disaster actually eventuate, the Group's final ultimate losses could materially differ from those estimates modelled by management.

The Group's underwriters and management consider insurance risk at an individual contract level, and also from a portfolio perspective where the risks assumed in similar classes of policies are aggregated and the exposure evaluated in light of historical portfolio experience and prospective factors. To assist with the process of pricing and managing insurance risk the Group routinely performs a wide range of activities including the following:

- regularly updating the Group's risk models;
- documenting, monitoring and reporting on the Group's strategy to manage risk;
- developing systems that facilitate the identification of emerging issues promptly;
- utilising sophisticated computer modelling tools to simulate catastrophes and measure the resultant potential losses before and after reinsurance;
- monitoring legal developments and amending the wording of policies when necessary;
- regularly aggregating risk exposures across individual underwriting portfolios and known accumulations of risk;
- examining the aggregated exposures in advance of underwriting further large risks; and
- developing processes that continually factor market intelligence into the pricing process.

The delegation of underwriting authority to specific individuals, both internally and externally, is subject to regular review. All underwriting staff and binding agencies are set strict parameters in relation to the levels and types of business they can underwrite, based on individual levels of experience and competence. These parameters cover areas such as the maximum sums insured per insurance contract, maximum gross written premiums and maximum aggregated exposures per geographical zone and risk class. Monthly meetings are held between the Chief Underwriting Officer and a specialist central analysis and review team in order to monitor claim development patterns and discuss individual underwriting issues as they arise. The Chief Underwriting Officer also holds weekly video conference meetings with this team to discuss interim underwriting matters.

The Group's insurance contracts include provisions to contain losses such as the ability to impose deductibles and demand reinstatement premiums in certain cases. In addition, in order to manage the Group's exposure to repeated catastrophic events, relevant policies frequently contain payment limits to cap the maximum amount payable from these insured events over the contract period.

Another tool for managing insurance risk is reinsurance. Reinsurance protection such as excess of loss cover is purchased at an entity level and is also considered at an overall Group level to mitigate the effect of catastrophes and unexpected concentrations of risk. However, the scope and type of reinsurance protection purchased may change depending on the extent and competitiveness of cover available in the market.

Notes to the consolidated financial statements
continued

3 Management of risk continued
3.1 Insurance risk continued

Estimated concentration of gross and net insurance liabilities on balance sheet by territory coverage of premium written 31 December 2009

Types of insurance risk in the Group

		Reinsurance inwards £000	Property – Marine and major assets £000	Property – Other assets £000	Casualty – Professional indemnity £000	Casualty – Other risks £000	Other* £000	Total £000
UK and Ireland	Gross	**29,001**	**16,993**	**133,166**	**247,222**	**15,345**	**14,716**	**456,443**
	Net	**26,579**	**8,425**	**129,114**	**213,181**	**10,767**	**9,639**	**397,705**
Europe	Gross	**23,650**	**5,367**	**74,121**	**53,557**	**10,549**	**22,992**	**190,236**
	Net	**21,531**	**3,659**	**69,606**	**49,691**	**8,886**	**20,625**	**173,998**
United States	Gross	**188,593**	**26,143**	**146,842**	**249,942**	**20,828**	**15,819**	**648,167**
	Net	**139,688**	**22,506**	**82,919**	**233,294**	**13,689**	**11,294**	**503,390**
Other territories	Gross	**35,915**	**23,506**	**43,488**	**49,656**	**17,317**	**68,013**	**237,895**
	Net	**34,407**	**16,910**	**32,924**	**49,254**	**6,453**	**57,932**	**197,880**
Multiple territory coverage	Gross	**139,843**	**162,116**	**48,190**	**12,689**	**127,781**	**98,991**	**589,610**
	Net	**80,558**	**124,264**	**37,713**	**11,289**	**87,186**	**88,242**	**429,252**
Total	**Gross**	**417,002**	**234,125**	**445,807**	**613,066**	**191,820**	**220,531**	**2,122,351**
	Net	**302,763**	**175,764**	**352,276**	**556,709**	**126,981**	**187,732**	**1,702,225**

Types of insurance risk in the Group

31 December 2008		Reinsurance inwards £000	Property – Marine and major assets £000	Property – Other assets £000	Casualty – Professional indemnity £000	Casualty – Other risks £000	Other* £000	Total £000
UK and Ireland	Gross	51,386	8,900	141,470	223,181	3,100	13,887	441,924
	Net	43,742	8,163	139,043	177,272	2,610	11,807	382,637
Europe	Gross	27,922	5,370	75,624	44,932	9,219	11,447	174,514
	Net	22,546	4,097	70,241	41,082	7,478	9,615	155,059
United States	Gross	249,389	50,252	168,770	338,150	46,713	20,352	873,626
	Net	143,826	36,889	118,909	304,037	33,186	15,554	652,401
Other territories	Gross	81,258	15,736	28,459	37,062	7,118	62,779	232,412
	Net	69,152	13,490	19,598	34,746	5,829	48,970	191,785
Multiple territory coverage	Gross	124,552	183,410	38,615	3,990	154,195	50,178	554,940
	Net	88,940	130,329	25,670	3,756	105,584	37,461	391,740
Total	Gross	534,507	263,668	452,938	647,315	220,345	158,643	2,277,416
	Net	368,206	192,968	373,461	560,893	154,687	123,407	1,773,622

*Includes a diverse mix of certain specialty lines such as kidnap and ransom, terrorism, bloodstock and other risks which contain a mix of property and casualty exposures.

Frequency and severity of claims
The specific insurance risks accepted by the Group fall broadly into four main categories: reinsurance inwards, marine and major property risks, other property risks and casualty insurance risks including professional indemnity. These specific categories are defined for risk review purposes only and are not exclusively aligned to any specific reportable segment in the Group's operational structure or the primary internal reports reviewed by the chief operating decision maker. A discussion of the frequency and severity of claims for each of those categories is given below. The Group has no significant exposure to asbestos risks or life insurance business.

Reinsurance inwards
The Group's reinsurance inwards acceptances are primarily focused on large commercial property, homeowner and marine and crop exposures held by other insurance companies predominantly in North America and other developed economies. This business is characterised more by large claims arising from individual events or catastrophes than the high frequency, low severity attritional losses associated with certain other business written by the Group. Multiple insured losses can periodically arise out of a single natural or man-made occurrence. The main circumstances that result in claims against the reinsurance inwards book are conventional catastrophes, such as earthquakes or storms, and other events including fires and explosions. The occurrence and impact of these events are very difficult to model over the short-term which complicates attempts to anticipate loss frequencies on an annual basis. In those years where there is a low incidence of severe catastrophes, loss frequencies on the reinsurance inwards book can be relatively low.

A significant proportion of the reinsurance inwards business provides cover on an excess of loss basis for individual events. The Group agrees to reimburse the cedant once their losses exceed a minimum level.

Consequently the frequency and severity of reinsurance inwards claims is related not only to the number of significant insured events that occur but also to their individual magnitude. If numerous catastrophes occurred in any one year but the cedant's individual loss on each was below the minimum stated, then the Group would have no liability under such contracts. Maximum gross line sizes and aggregate exposures are set for each type of programme.

Property risks – marine and major assets
The Group directly underwrites a diverse range of property risks. The risk profile of the property covered under marine and major asset policies is different to that typically contained in the other classes of property (such as private households and contents insurance) covered by the Group.

Typical property covered by marine and other major property contracts include fixed and moveable assets such as ships and other vessels, cargo in transit, energy platforms and installations, pipelines, other subsea assets, satellites, commercial buildings and industrial plants and machinery. These assets are typically exposed to a blend of catastrophic and other large loss events and attritional claims arising from conventional hazards such as collision, flooding, fire and theft. Climatic changes may give rise to more frequent and severe extreme weather events (for example earthquakes, windstorms and river flooding etc.) and it may be expected that their frequency will increase over time.

For this reason the Group accepts major property insurance risks for periods of mainly one year so that each contract can be re-priced on renewal to reflect the continually evolving risk profile. The most significant risks covered for periods exceeding one year are certain specialist lines such as marine and offshore construction projects which can typically have building and assembling periods of between three and four years. These form a small proportion of the Group's overall portfolio.

Marine and major property contracts are normally underwritten by reference to the commercial replacement value of the property covered. The cost of repairing or rebuilding assets, of replacement or indemnity for contents and time taken to restart or resume operations to original levels for business interruption losses are the key factors that influence the level of claims under these policies. The Group's exposure to commodity price risk in relation to insurance contracts is very limited, given the controlled extent of business interruption cover offered in the areas prone to losses of asset production.

Other property risks
The Group provides home and contents insurance, together with cover for art work, antiques, classic cars, jewellery, collectables and other assets typically held by affluent individuals. The Group also extends cover to reimburse certain policyholders when named insureds or insured assets are seized for kidnap and a ransom demand is subsequently met. Events which can generate claims on these contracts include burglary, kidnap, seizure of assets, acts of vandalism, fires, flooding and storm damage. Losses on most classes can be predicted with a greater degree of certainty as there is a rich history of actual loss experience data and the locations of the assets covered, and the individual levels of security taken by owners are relatively static from one year to the next. The losses associated with these contracts tend to be of a higher frequency and lower severity than the marine and other major property assets covered above.

The Group's home and contents insurance contracts are exposed to weather and climatic risks such as floods and windstorms and their consequences. As outlined earlier the frequency and severity of these losses do not lend themselves to accurate prediction over the short-term. Contract periods are therefore not normally more than one year at a time to enable risks to be regularly re-priced.

Contracts are underwritten by reference to the commercial replacement value of the properties and contents insured, and claims payment limits are always included to cap the amount payable on occurrence of the insured event.

Casualty insurance risks
The casualty underwriting strategy attempts to ensure that the underwritten risks are well diversified in terms of type and amount of potential hazard, industry and geography. However, the Group's exposure is more focused towards marine and professional and technological liability risks rather than human bodily injury risks, which are only accepted under limited circumstances. Claims typically arise from incidents such as errors and omissions attributed to the insured, professional negligence and specific losses suffered as a result of electronic or technological failure of software products and websites.

The provision of insurance to cover allegations made against individuals acting in the course of fiduciary or managerial responsibilities, including directors' and officers' insurance, is one example of a casualty insurance risk. However the Group's specific exposure to this specific risk category is relatively limited. The Group's casualty insurance contracts mainly experience low severity attritional losses.

The Group's pricing strategy for casualty insurance policies is typically based upon historical claim frequencies and average claim severities, adjusted for inflation and extrapolated forwards to incorporate projected changes in claims patterns. In determining the price of each policy an allowance is also made for acquisition and administration expenses, reinsurance costs, investment returns and the Group's cost of capital.

Sources of uncertainty in the estimation of future claim payments
The Group's procedures for estimating the outstanding costs of settling insured losses at the balance sheet date, including those not yet notified by, or apparent to, the insured, are detailed in note 27.

The majority of the Group's insurance risks are short tail and, based on past history, significant claims are normally notified and settled within 12 to 24 months of the insured event occurring. Those claims taking the longest time to develop and settle typically relate to casualty risks where legal complexities occasionally develop regarding the insured's alleged omissions or negligence. The length of time required to obtain definitive legal judgements and make eventual settlements exposes the Group to a degree of reserving risk in an inflationary environment.

The majority of the Group's casualty exposures are written on a claims made basis. However the final quantum of these claims may not be established for a number of years after the event. Consequently a significant proportion of the casualty insurance amounts reserved on the balance sheet may not be expected to settle within 24 months of the balance sheet date.

Certain marine and property insurance contracts such as those relating to subsea and other energy assets, and the related business interruption risks, can also take longer than normal to settle. This is because of the length of time required for detailed subsea surveys to be carried out and damage assessments agreed together with difficulties in predicting when the assets can be brought back into full production.

Notes to the consolidated financial statements
continued

3 Management of risk continued
3.1 Insurance risk continued

For the reinsurance lines, there is often a time lag between the establishment and re-estimate of case reserves and reporting to the Group. The Group works closely with clients to ensure timely reporting and also centrally analyses industry loss data to verify the reported reserves.

3.2 Financial risk
Overview
The Group is exposed to financial risk through its ownership of financial assets including loans and receivables, financial liabilities and reinsurance assets. These items collectively represent a significant element of the Group's net shareholder funds.

The key financial risk for the Group is that the proceeds from its financial assets are not sufficient to fund the obligations arising from its insurance contracts and financial liabilities. The most important entity and economic variables that could result in such an outcome relate to risk factors such as equity price risk, interest rate risk, the reliability of fair value measures, credit risk, liquidity risk and currency risk. The Group's policies and procedures for managing exposure to these specific categories of risk are detailed below.

Reliability of fair values
The Group has elected to carry all financial investments at fair value through profit or loss as they are managed and evaluated on a fair value basis in accordance with a documented strategy. With the exception of unquoted equity investments, all of the financial investments held by the Group are available to trade in markets and the Group therefore seeks to determine fair value by reference to published prices or as derived by pricing vendors using observable quotations in the most active financial markets in which the assets trade. The Group seeks to determine the fair value of financial assets primarily with reference to their closing bid market prices at the balance sheet date. The ability to obtain quoted bid market prices may be reduced in periods of diminished liquidity, such as those prevailing for certain categories of fixed income instruments affected by the continued market dislocation that commenced during the second half of 2007. In addition, those quoted prices that may be available may represent an unrealistic proportion of market holdings or individual trade sizes that could not be readily available to the Group. In such instances fair values may be determined or partially supplemented using other observable market inputs such as prices provided by market makers such as dealers and brokers, and prices achieved in the most recent regular transaction of identical or closely related instruments occurring before the balance sheet date but updated for relevant perceived changes in market conditions. Throughout 2008 the Group witnessed substantial declines in observable market values for many fixed income assets such as corporate, municipal and asset backed bonds. In some cases the extent and duration of declines witnessed appeared to arise as a response to global macroeconomic and liquidity concerns and not as a result of specific issuer events or credit concerns. During 2009, the Group experienced a sharp recovery in those investments which were heavily marked down in 2008.

At 31 December 2009, the Group holds asset-backed and mortgage-backed fixed income instruments in its investment portfolio but has minimal direct exposure to sub-prime asset classes. Together with the Group's investment managers, management continues to monitor the potential for any adverse development associated with this investment exposure through the analysis of relevant factors such as credit ratings, collateral, subordination levels and default rates in relation to the securities held.

Valuation of these securities will continue to be impacted by external market factors including default rates, rating agency actions, and liquidity. The Group will make adjustments to the investment portfolio as appropriate as part of its overall portfolio strategy, but its ability to mitigate its risk by selling or hedging its exposures may be limited by the market environment. The Group's future results may be impacted, both positively and negatively, by the valuation adjustments applied to these securities.

Note 23 provides an analysis of the measurement attributes of the Group's financial instruments.

(a) Equity price risk
The Group is exposed to equity price risk through its holdings of equity and unit trust investments. This is limited to a small and controlled proportion of the overall investment portfolio and the equity and unit trust holdings involved are well diversified over a number of companies and industries. The fair value of equity assets in the Group's balance sheet at 31 December 2009 was £134 million (2008: £125 million). These may be analysed as follows:

Nature of equity and unit trust holdings	2009 % weighting	2008 % weighting
Directly held equity securities	**2**	–
Units held in funds – traditional long only	**68**	68
Units held in funds – long and short and special strategies	**30**	32
Geographic focus		
Specific UK mandates	**37**	29
Global mandates	**63**	71

The allocation of equity risk is not heavily confined to any one market index so as to reduce the Group's exposure to individual sensitivities. A 10% downward correction in equity prices at 31 December 2009 would have been expected to reduce Group equity and profit after tax for the year by approximately £11.4 million (2008: £10.0 million) assuming that the only area impacted was equity financial assets. A 10% upward movement is estimated to have an equal but opposite effect.

(b) Interest rate risk
Fixed income investments represent a significant proportion of the Group's assets and the Board continually monitors investment strategy to minimise the risk of a fall in the portfolio's market value which could affect the amount of business that the Group is able to underwrite or its ability to settle claims as they fall due. The fair value of the Group's investment portfolio of debt and fixed income securities is normally inversely correlated to movements in market interest rates. If market interest rates fall, the fair value of the Group's debt and fixed income investments would tend to rise and vice versa if credit spreads remained constant.

Debt and fixed income assets are predominantly invested in high quality corporate, government and asset backed bonds. The investments typically have relatively short durations and terms to maturity. The portfolio is managed to minimise the impact of interest rate risk on anticipated Group cash flows.

The Group may also from time to time, enter into interest rate future contracts in order to minimise the interest rate risk on specific longer duration portfolios.

The fair value of debt and fixed income assets in the Group's balance sheet at 31 December 2009 was £2,256 million (2008: £1,929 million). These may be analysed as follows:

Nature of debt and fixed income holdings	2009 % weighting	2008 % weighting
Government issued bonds and instruments	**28**	35
Agency and Government supported debt	**28**	17
Asset backed securities	**6**	10
Mortgage backed instruments – Agency	**4**	8
Mortgage backed instruments – Non-agency	**6**	8
Corporate bonds	**26**	20
Lloyd's and money market deposits	**2**	2

One method of assessing interest rate sensitivity is through the examination of duration-convexity factors in the underlying portfolio. Using a duration-convexity based sensitivity analysis, if market interest rates had risen by 100 basis points at the balance sheet date, the fair value might have been expected to decrease by £32 million (2008: decrease of £31 million) assuming that the only balance sheet area impacted was debt and fixed income financial assets.

Duration is the weighted average length of time required for an instrument's cash flow stream to be recovered, where the weightings involved are based on the discounted present values of each cash flow. A closely related concept, modified duration, measures the sensitivity of the instrument's price to a change in its yield to maturity. Convexity measures the sensitivity of modified duration to changes in the yield to maturity.

Using these three concepts, scenario modelling derives the above estimated impact on instruments' fair values for a 100 basis point change in the term structure of market interest rates.

Insurance contract liabilities are not directly sensitive to the level of market interest rates, as they are undiscounted and contractually non-interest-bearing. The Group's debt and fixed income assets are further detailed at note 20.

At 31 December 2009, £138 million was drawn on the Group's borrowing facility (2008: $130 million). The Group has no other significant borrowings or other assets or liabilities carrying interest rate risk, other than the facilities and Letters of Credit outlined in note 36.

(c) Credit risk

The Group has exposure to credit risk, which is the risk that a counterparty will suffer a deterioration in perceived financial strength or be unable to pay amounts in full when due.

The concentrations of credit risk exposures held by insurers may be expected to be greater than those associated with other industries, due to the specific nature of reinsurance markets and the extent of investments held in financial markets. In both markets, the Group interacts with a number of counterparties who are engaged in similar activities with similar customer profiles, and often in the same geographical areas and industry sectors. Consequently, as many of these counterparties are themselves exposed to similar economic characteristics, one single localised or macroeconomic change could severely disrupt the ability of a significant number of counterparties to meet the Group's agreed contractual terms and obligations.

Key areas of exposure to credit risk include:
- reinsurers' share of insurance liabilities;
- amounts due from reinsurers in respect of claims already paid;
- amounts due from insurance contract holders; and
- counterparty risk with respect to cash and cash equivalents, and investments including deposits, derivative transactions and catastrophe bonds.

The Group's maximum exposure to credit risk is represented by the carrying values of financial assets and reinsurance assets included in the consolidated balance sheet at any given point in time. The Group does not use credit derivatives or other products to mitigate maximum credit risk exposures on reinsurance assets. The Group structures the levels of credit risk accepted by placing limits on their exposure to a single counterparty, or groups of counterparties, and having regard to geographical locations. Such risks are subject to an annual or more frequent review. There is no significant concentration of credit risk with respect to loans and receivables, as the Group has a large number of internationally dispersed debtors with unrelated operations.

Reinsurance is used to contain insurance risk. This does not, however, discharge the Group's liability as primary insurer. If a reinsurer fails to pay a claim for any reason, the Group remains liable for the payment to the policyholder. The creditworthiness of reinsurers is therefore continually reviewed throughout the year.

The Group Reinsurance Security Committee assesses the creditworthiness of all reinsurers by reviewing credit grades provided by rating agencies and other publicly available financial information detailing their financial strength and performance. The financial analysis of reinsurers produces an assessment categorised by Standard & Poor's (S&P) rating (or equivalent when not available from S&P).

Despite the rigorous nature of this assessment exercise, and the resultant restricted range of reinsurance counterparties with acceptable strength and credit credentials that emerges therefrom, some degree of credit risk concentration remains inevitable.

The Committee considers the reputation of its reinsurance partners and also receives details of recent payment history and the status of any ongoing negotiations between Group companies and these third parties. This information is used to update the reinsurance purchasing strategy.

Individual operating units maintain records of the payment history for significant brokers and contract holders with whom they conduct regular business. The exposure to individual counterparties is also managed by other mechanisms, such as the right of offset where counterparties are both debtors and creditors of the Group. Management information reports detail provisions for impairment on loans and receivables and subsequent write-off. Exposures to individual intermediaries and groups of intermediaries are collected within the ongoing monitoring of the controls associated with regulatory solvency.

The Group also mitigates credit counterparty risk by concentrating debt and fixed income investments in high quality instruments, including a particular emphasis on Government bonds issued mainly by European Union and North American countries.

Notes to the consolidated financial statements
continued

3 Management of risk continued
3.2 Financial risk continued
(c) Credit risk *continued*

An analysis of the Group's major exposures to counterparty credit risk excluding loans and receivables, based on Standard & Poor's or equivalent rating, is presented below:

As at 31 December 2009	Note	AAA £000	AA £000	A £000	Other/ not rated £000	Total £000
Debt and fixed income securities	20	**1,555,636**	**198,001**	**256,120**	**245,980**	**2,255,737**
Deposits with credit institutions	20	**62**	**2,860**	**8,472**	**–**	**11,394**
Catastrophe bonds		**–**	**–**	**–**	**11,310**	**11,310**
Derivative financial instruments	20, 22	**–**	**–**	**–**	**1,018**	**1,018**
Reinsurance assets	19	**8,120**	**151,803**	**230,462**	**29,741**	**420,126**
Cash and cash equivalents	24	**27,456**	**136,214**	**93,999**	**1,978**	**259,647**
Total		**1,591,274**	**488,878**	**589,053**	**290,027**	**2,959,232**
Amounts attributable to largest single counterparty		**308,569**	**57,859**	**17,424**	**10,619**	

As at 31 December 2008	Note	AAA £000	AA £000	A £000	Other/ not rated £000	Total £000
Debt and fixed income securities	20	1,471,797	179,416	172,832	104,554	1,928,599
Deposits with credit institutions	20	4,146	11,800	12,323	–	28,269
Catastrophe bonds		–	–	–	–	–
Derivative financial instruments	20, 22	–	40	–	–	40
Reinsurance assets	19	6,926	281,041	189,444	26,383	503,794
Cash and cash equivalents	24	54,227	330,246	56,010	139	440,622
Total		1,537,096	802,543	430,609	131,076	2,901,324
Amounts attributable to largest single counterparty		415,429	271,991	15,508	8,103	

The largest counterparty exposure within AAA rating is with the US Treasury. Catastrophe bonds included within 'other/not rated' are rated BB or above. A significant proportion of 'other/not rated' reinsurance assets at 31 December 2009 and 31 December 2008 are supported by Letter of Credit guarantees issued by financial institutions with Standard & Poor's or equivalent credit or financial strength ratings of A or better.

At 31 December 2009 the Group held no material debt and fixed income assets that were past due or impaired beyond their reported fair values, either for the current period under review or on a cumulative basis (2008: £nil). For the current period under review, the Group did not experience any defaults on debt securities (2008: one financial instrument).

The available headroom of working capital is monitored through the use of a detailed Group cash flow forecast which is reviewed by management monthly or more frequently as required.

(d) Liquidity risk
The Group is exposed to daily calls on its available cash resources mainly from claims arising from insurance and reinsurance contracts. Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The Board sets limits on the minimum level of cash and maturing funds available to meet such calls and on the minimum level of borrowing facilities that should be in place to cover unexpected levels of claims and other cash demands.

A significant proportion of the Group's investments are in highly liquid assets which could be converted to cash in a prompt fashion and at minimal expense. The deposits with credit institutions largely comprise short-dated certificates for which an active market exists and which the Group can easily access. The Group's exposure to equities is concentrated on shares and funds that are traded on internationally recognised stock exchanges.

3 Management of risk continued
3.2 Financial risk continued
***(d) Liquidity risk** continued*

The main focus of the investment portfolio is on high quality short duration debt and fixed income securities, and cash. There are no significant holdings of investments with specific repricing dates. Notwithstanding the regular interest receipts and also the Group's ability to liquidate these securities and the majority of its other financial instrument assets for cash in a prompt and reasonable manner, the contractual maturity profile of the fair value of these securities at 31 December was as follows:

Fair values at balance sheet date analysed by contractual maturity	Debt and fixed income securities £000	Deposits with credit institutions £000	Catastrophe bonds £000	Derivative financial assets £000	Cash and cash equivalents £000	**2009 Total £000**	2008 Total £000
Less than one year	463,526	7,877	1,878	1,018	259,647	**733,946**	665,770
Between one and two years	710,347	3,517	5,836	–	–	**719,700**	593,371
Between two and five years	668,602	–	3,596	–	–	**672,198**	669,819
Over five years	359,094	–	–	–	–	**359,094**	407,273
Sub-total	2,201,569	11,394	11,310	1,018	259,647	**2,484,938**	2,336,233
Other non-dated instruments	54,168	–	–	–	–	**54,168**	61,297
Total	2,255,737	11,394	11,310	1,018	259,647	**2,539,106**	2,397,530

The Group's equities and shares in unit trusts and other non-dated instruments have no contractual maturity terms but could also be liquidated for cash in a prompt and reasonable timeframe within one year of the balance sheet date.

Average contractual maturity analysed by denominational currency of investments	**2009 Years**	2008 Years
Pound Sterling	**1.52**	4.85
US Dollar	**4.89**	6.95
Euro	**3.21**	5.10
Canadian Dollar	**1.38**	2.45

The following is an analysis by liability type of the estimated timing of net cash flows based on the net claims liabilities held. The Group does not discount claims liabilities. The estimated phasing of settlement is based on current estimates and historical trends and the actual timing of future settlement cash flows may differ materially from that disclosure below.

Liquidity requirements to settle estimated profile of net claim liabilities on balance sheet	Within one year £000	Between one and two years £000	Between two and five years £000	Over five years £000	**2009 Total £000**
Reinsurance inwards	86,533	61,120	52,478	13,529	**213,660**
Property – marine and major assets	54,426	33,557	34,163	10,194	**132,340**
Property – other assets	115,406	42,065	32,477	5,234	**195,182**
Casualty – professional indemnity	99,372	101,486	183,597	36,193	**420,648**
Casualty – other risks	55,636	37,247	34,243	8,301	**135,427**
Other*	56,342	30,266	27,088	9,480	**123,176**
Total	**467,715**	**305,741**	**364,046**	**82,931**	**1,220,433**

Liquidity requirements to settle estimated profile of net claim liabilities on balance sheet	Within one year £000	Between one and two years £000	Between two and five years £000	Over five years £000	2008 Total £000
Reinsurance inwards	136,718	75,744	53,762	8,859	275,083
Property – marine and major assets	71,590	41,561	39,787	6,630	159,568
Property – other assets	143,891	44,696	30,918	3,826	223,331
Casualty – professional indemnity	109,421	109,516	185,154	41,266	445,357
Casualty – other risks	60,526	47,281	49,774	11,912	169,493
Other*	34,985	15,742	14,220	3,646	68,593
Total	557,131	334,540	373,615	76,139	1,341,425

*Includes a diverse mix of certain specialty lines such as kidnap and ransom, terrorism, bloodstock and other risks which contain a mix of property and casualty exposures.

Details of the payment profile of the Group's borrowings, derivative instruments and other liabilities is given in notes 20 and 28.

3 Management of risk continued
3.2 Financial risk continued

(e) Currency risk
The Group operates internationally and its exposures to foreign exchange risk arise primarily with respect to the US Dollar, Pound Sterling and the Euro. These exposures may be classified in two main categories:
1) Structural foreign exchange risk through consolidation of net investments in subsidiaries with different functional currencies within the Group results; and
2) Operational foreign exchange risk through routinely entering into insurance, investment and operational contracts, as a Group of international insurance entities serving international communities, where rights and obligations are denominated in currencies other than each respective entity's functional currency.

The Group's exposure to structural foreign exchange risk primarily relates to the US Dollar net investments made in its domestic operation in Bermuda and its overseas operation in Guernsey and the US. Other structural exposures also arise on a smaller scale in relation to net investments made in European operations. The Group's risk appetite permits the acceptance of structural foreign exchange movements within defined aggregate limits and exchange rate parameters which are monitored centrally. Exchange rate derivatives are used when appropriate to shield the Group against significant movements outside of a defined range.

At a consolidated level, the Group is exposed to foreign exchange gains or losses on balances held between Group companies where one party to the transaction has a functional currency other than Pound Sterling. To the extent that such gains or losses are considered to relate to economic hedges and intragroup borrowings, they are disclosed separately in order for users of the financial statements to obtain a fuller understanding of the Group's financial performance (note 14).

Up to 6 May 2008 the Group financed a portion of its net investment in the Bermuda and Guernsey insurance operations using US Dollar borrowings to which hedge accounting was applied (see note 20). There were no items qualifying for hedge accounting in the current year.

The Group has the ability to draw on its current borrowing facility in any currency requested, enabling the Group to match its funding requirements with the relevant currency.

Operational foreign exchange risk is controlled within the Group's operations. The assets of the Group's overseas operations are generally invested in the same currencies as their underlying insurance and investment liabilities producing a natural hedge. Due attention is paid to local regulatory solvency and risk based capital requirements.

Details of all foreign currency derivative contracts entered into with external parties are given in note 22. All foreign currency derivative transactions with external parties are managed centrally. Included in the tables below are net non-monetary liabilities of £240 million (2008: £225 million) which are denominated in foreign currencies.

As a result of the accounting treatment for non monetary items, the Group may also experience volatility in its income statement during a period when movements in foreign exchange rates fluctuate significantly. In accordance with IFRS, non monetary items are recorded at original transaction rates and are not remeasured at the reporting date. These items include unearned premiums, deferred acquisition costs and reinsurers' share of unearned premiums. Consequently, a mismatch arises in the income statement between the amount of premium recognised at historical transaction rates, and the related claims which are retranslated using currency rates in force at the reporting date. The Group considers this to be a timing issue which can cause significant volatility in the income statements. Further details of the impact of the accounting treatment is provided in note 13.

The currency profile of the Group's assets and liabilities is as follows:

At 31 December 2009	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Intangible assets	44,105	6,308	–	–	50,413
Property, plant and equipment	13,678	7,893	673	–	22,244
Investments in associates	6,728	–	590	–	7,318
Deferred tax	–	14,077	–	–	14,077
Deferred acquisition costs	42,376	71,678	23,125	4,326	141,505
Financial assets carried at fair value	580,797	1,623,276	166,629	42,598	2,413,300
Reinsurance assets	54,976	320,424	27,375	17,351	420,126
Loans and receivables including insurance receivables	127,361	259,539	88,480	13,402	488,782
Current tax	–	–	–	–	–
Cash and cash equivalents	93,096	97,754	57,998	10,799	259,647
Total assets	963,117	2,400,949	364,870	88,476	3,817,412

3 Management of risk continued
3.2 Financial risk continued
(e) Currency risk *continued*

	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Employee retirement benefit obligations	**–**	**–**	**–**	**–**	**–**
Deferred tax	**69,673**	**–**	**–**	**–**	**69,673**
Insurance liabilities	**486,488**	**1,361,934**	**220,661**	**53,268**	**2,122,351**
Financial liabilities	**138,000**	**539**	**–**	**–**	**138,539**
Current tax	**26,080**	**–**	**–**	**–**	**26,080**
Trade and other payables	**142,659**	**149,005**	**42,766**	**5,053**	**339,483**
Total liabilities	**862,900**	**1,511,478**	**263,427**	**58,321**	**2,696,126**

At 31 December 2008	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Intangible assets	42,249	6,308	–	–	48,557
Property, plant and equipment	16,378	2,404	886	–	19,668
Investments in associates	6,504	–	696	–	7,200
Deferred tax assets	–	5,996	–	–	5,996
Deferred acquisition costs	40,263	66,462	20,094	4,311	131,130
Financial assets carried at fair value	370,043	1,430,712	236,066	44,951	2,081,772
Reinsurance assets	66,081	400,727	26,154	10,832	503,794
Loans and receivables including insurance receivables	127,702	290,523	64,748	11,342	494,315
Current tax	26,289	–	–	–	26,289
Cash and cash equivalents	127,881	229,165	75,109	8,467	440,622
Total assets	823,390	2,432,297	423,753	79,903	3,759,343

	Sterling £000	US Dollar £000	Euro £000	Other £000	Total £000
Employee retirement benefit obligations	–	–	–	–	–
Deferred tax	74,645	–	–	–	74,645
Insurance liabilities	455,606	1,570,090	206,228	45,492	2,277,416
Financial liabilities	–	132,818	10,532	–	143,350
Current tax	–	–	–	–	–
Trade and other payables	145,926	120,233	42,065	4,682	312,906
Total liabilities	676,177	1,823,141	258,825	50,174	2,808,317

Sensitivity analysis

As at 31 December 2009, the Group used closing rates of exchange of £1:€1.13 and £1:$1.61 (2008: £1:€1.03 and £1:$1.44). The Group performs sensitivity analysis based on a 10% strengthening or weakening of Pound Sterling against the Euro and US Dollar. This analysis assumes that all other variables, in particular interest rates, remain constant and that the underlying valuation of assets and liabilities in their base currency is unchanged. The process of deriving the undernoted estimates takes account of the linear retranslation movements of foreign currency monetary assets and liabilities together with the impact on the retranslation of those Group entities with non-sterling functional currency financial statements. During the year, the Group transacted in a number of over the counter forward currency derivative contracts. The impact of these contracts on the sensitivity analysis is negligible.

At 31 December 2009	Effect on equity after tax £m	Effect on profit before tax £m
Strengthening of US Dollar	**94.6**	**54.2**
Weakening of US Dollar	**(74.8)**	**(41.7)**
Strengthening of Euro	**10.0**	**13.9**
Weakening of Euro	**(8.2)**	**(11.4)**

Notes to the consolidated financial statements continued

3 Management of risk continued
3.2 Financial risk continued

(f) Limitations of sensitivity analysis
The sensitivity information given in notes (a) to (e) above demonstrates the estimated impact of a change in a major input assumption while other assumptions remain unchanged. In reality, there are normally significant levels of correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results. The same limitations exist in respect to the retirement benefit scheme sensitivities presented at note 31 to these financial statements. Furthermore, estimates of sensitivity may become less reliable in unusual market conditions such as instances when risk free interest rates fall towards zero.

The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs. For example, the Group's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action.

3.3 Capital risk management
The Group's primary objectives when managing its capital position are:
- to safeguard its ability to continue as a going concern, so that it can continue to provide long-term growth and progressive dividend returns for shareholders;
- to provide an adequate return to the Group's shareholders by pricing its insurance products and services commensurately with the level of risk;
- to maintain of an efficient cost of capital;
- to comply with all regulatory requirements by a significant margin; and
- to maintain financial strength ratings of A in each of its insurance entities.

The Group sets the amount of capital required in its funding structure in proportion to risk. The Group then manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to obtain or maintain an optimal capital structure the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, assume debt, or sell assets to reduce debt.

The Group's activities are funded by a mixture of capital sources including issued equity share capital, retained earnings, Letters of Credit, bank debt and other third-party insurance capital.

The Board ensures that the use and allocation of capital are given a primary focus in all significant operational actions. With that in mind, the Group has developed and embedded sophisticated capital modelling tools within its business. These join together short-term and long-term business plans and link divisional aspirations with the Group's overall strategy. The models provide the basis of the allocation of capital to different businesses and business lines, as well as the regulatory and rating agency capital processes.

During the year the Group was in compliance with capital requirements imposed by regulators in each jurisdiction where the Group operates.

There were no changes in the Group's approach to capital risk management during the current or prior year under review.

Gearing
The Group currently utilises short- to medium-term gearing as an additional source of funds to maximise the opportunities from strong markets and to reduce the risk profile of the business when the rating environment shows a weaker model for the more volatile business. The Group's gearing is obtained from a number of sources, including:
- Letter of Credit and revolving credit facility – the Group's main facility currently in place is for a total of £350 million which may be drawn as cash (under a revolving credit facility), Letter of Credit or a combination thereof, providing that the cash portion does not exceed £200 million. This facility was secured during 2008 by the Company's subsidiary Hiscox plc. The Letter of Credit availability period ends on 31 December 2009. This enables the Group to utilise the Letter of Credit as Funds at Lloyd's to support underwriting on both the 2009 and 2010 years of account. The revolving credit facility has a maximum five year contractual period for repayment.

  At 31 December 2009 US$225 million was drawn by way of Letter of Credit to support the Funds at Lloyd's requirement and a further £138 million by way of cash (2008: £137.5 million and US$130 million respectively) to support general trading activities;
- external Names – 27.5% of Syndicate 33's capacity is capitalised by third-parties paying a profit share of approximately 17.5%;
- Syndicate 6104 at Lloyd's – with an approximate capacity of £43 million for the 2009 year of account (2008 year of account: £34 million). This Syndicate is wholly backed by external members and takes a pure 2009 year of account quota share of Syndicate 33's international property catastrophe reinsurance account;
- gearing quota shares – historically the Group has used reinsurance capital to fund its capital requirement for short-term expansions in the volume of business underwritten by the Syndicate; and
- qualifying quota shares – these are reinsurance arrangements that allow the Group to increase the amount of premium it writes in hard markets.

The funds raised through Letters of Credit and loan facilities have been applied to support both the 2009 year of account for Syndicate 33 and the capital requirements of Hiscox Insurance Company (Bermuda) Limited.

Financial strength
The financial strength ratings of the Group's insurance company subsidiaries are outlined below:

	A.M. Best	Fitch	Standard & Poor's
Hiscox Insurance Company Limited	A (Excellent)	A	A (Strong)
Hiscox Insurance Company (Bermuda) Limited	A (Excellent)	A	–
Hiscox Insurance Company (Guernsey) Limited	A (Excellent)	A	–
Hiscox Insurance Company Inc.	A (Excellent)	–	–

Syndicate 33 benefits from an A.M. Best rating of A (Excellent). In addition, the Syndicate also benefits from the Lloyd's ratings of A (Excellent) from A.M. Best and A+ (Strong) from Standard & Poor's.

Capital performance
The Group's main capital performance measure is the achieved return on equity (ROE). This marker best aligns the aspirations of employees and shareholders.

As variable remuneration, the vesting of options and longer-term investment plans all relate directly to ROE, this concept is embedded in the workings and culture of

3 Management of risk continued
3.3 Capital risk management continued

the Group. The Group maintains its cost of capital levels and its debt to overall equity ratios in line with others in the non-life insurance industry.

Capital modelling and regulation
The capital requirements of an insurance group are determined by its exposure to risk and the solvency criteria established by management and statutory regulations.

In 2005, the UK Financial Services Authority (FSA) and Lloyd's introduced a new capital regime that requires insurance companies to calculate their own capital requirements through Individual Capital Assessments (ICA). Hiscox Insurance Company Limited and Syndicate 33 maintain ICA models in accordance with this regime. The models are concentrated specifically on the particular product lines, market conditions and risk appetite of each entity. If the FSA considers an ICA to be inadequate, it can require the entity to maintain an increased capital safeguard. The Directors are also required to certify that the Group has complied, in all material aspects, with the provisions of the Interim Prudential Sourcebook: Insurers (IPRU(INS)), the Integrated Prudential Sourcebook for Insurers (INSPRU) and General Prudential Sourcebook (GENPRU) when completing the ICA return. The Group used its own integrated modelling expertise to produce the ICA calculations. The results mirrored those driving the existing internal capital setting process.

The Group's capital requirements are managed both centrally and at a regulated entity level. The assessed capital requirement for the business placed through Hiscox Insurance Company Limited, Hiscox Insurance Company (Bermuda) Limited, Hiscox Insurance Company (Guernsey) Limited and Hiscox Insurance Company Inc., is driven by the level of resources necessary to maintain both regulatory requirements and the capital necessary to maintain financial strength of an A rating.

For Syndicate 33, the ICA process produces a result that is uplifted by Lloyd's to identify the capital required to hold the A rating. The strong control and risk management environment, together with the sophistication of the modelling, have produced a capital ratio below that suggested under the previous risk-based capital regime.

Another key area of capital modelling for Hiscox is to identify which insurance vehicle produces the best return on capital employed for the Group, given certain restraints from licences, reinsurance and the regulatory environment. This modelling takes into account transactional costs and tax, in addition to the necessary capital ratios. It proves the capital efficiency of Lloyd's, despite a tax disadvantage against offshore entities, and the cost advantage of processing smaller premium business outside of Lloyd's.

In addition to the ICA modelling process, the EU Insurance Group's Directive of 1998, as amended by the Financial Group's Directive (FGD), compels insurance companies that are members of a group to consider the solvency margin of their ultimate parent company. This consideration must refer to the surplus assets of the ultimate parent's related insurers, reinsurers, intermediate holding companies and other regulated entities.

The FGD has been applied in the UK through INSPRU and GENPRU. In accordance with these provisions, the parent company's solvency margin consideration became a minimum capital requirement for the Group from 31 December 2006 onwards. The Group complied with the requirement for the current and prior year.

In the Group's other geographical territories, including the US, its subsidiaries underwriting insurance business are required to operate within broadly similar risk-based externally imposed capital requirements when accepting business.

4 Operating segments
The Group's operating segments consist of four segments which recognise the differences between products and services, customer groupings and geographical areas. Financial information is used in this format by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The format is representative of the management structure of the segments.

During the year, following a new geographic management structure including new business written through Syndicate 3624, the Group has changed its segmental reporting to provide more effective financial reporting for the evaluation of business segments by the chief operating decision maker to make decisions about future allocation of resources. Accordingly the 2008 segmental comparatives have been restated in order to enable comparison of results by the user.

The Group's four operating segments are:
- **London Market** comprises the results of Syndicate 33, excluding the results of the fine art, UK regional events coverage and non US household business which is included within the results of UK and Europe. In addition, it excludes the larger TMT business which is allocated to the International segment and an element of kidnap and ransom and terrorism included in UK and Europe.
- **UK and Europe** comprises the results of Hiscox Insurance Company Limited, the results of Syndicate 33's fine art, UK regional events coverage and non US household business, together with the income and expenses arising from the Group's retail agency activities in the UK and in continental Europe. It excludes the results of the larger retail TMT business written by Hiscox Insurance Company Limited. It also includes an element of kidnap and ransom and terrorism written in Syndicate 33.
- **International** comprises the results of Hiscox Insurance Company (Guernsey) Limited, Hiscox Insurance Company (Bermuda) Limited, Syndicate 3624, Hiscox Inc. and Hiscox Insurance Company Inc.. It also includes the results of the larger TMT business written by Hiscox Insurance Company Limited and Syndicate 33.
- **Corporate Centre** comprises the investment return, finance costs and administrative costs associated with Group management activities. Corporate Centre also includes the majority of foreign currency items on economic hedges and intragroup borrowings. These relate to certain foreign currency items on economic hedges and intragroup borrowings, further details of which are given at note 14. Corporate Centre forms a reportable segment due to its investment activities which earn significant external coupon revenues.

Notes to the consolidated financial statements
continued

4 Operating segments continued

All amounts reported below represent transactions with external parties only, with all inter-segment amounts eliminated which is consistent with the information used by the chief operating decision maker when evaluating the results of the Group. Performance is measured based on each reportable segment's profit before tax.

(a) Profit before tax by segment

	Year to 31 December 2009					Year to 31 December 2008 Restated				
	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
Gross premiums written	**663,034**	**420,982**	**351,385**	**–**	**1,435,401**	545,930	357,095	244,339	–	1,147,364
Net premiums written	**483,611**	**391,461**	**281,951**	**–**	**1,157,023**	363,112	329,117	206,165	–	898,394
Net premiums earned	**453,281**	**367,326**	**277,495**	**–**	**1,098,102**	427,770	303,363	196,962	–	928,095
Investment result – financial assets*	**80,901**	**34,935**	**57,765**	**9,168**	**182,769**	(5,463)	(11,928)	(8,443)	(1,798)	(27,632)
Investment result – derivatives	**(1,192)**	**1,967**	**(83)**	**(296)**	**396**	–	(10,483)	–	(42,495)	(52,978)
Other revenues	**12,841**	**3,955**	**2,700**	**2**	**19,498**	15,606	2,929	1,323	–	19,858
Revenue	**545,831**	**408,183**	**337,877**	**8,874**	**1,300,765**	437,913	283,881	189,842	(44,293)	867,343
Claims and claim adjustment expenses, net of reinsurance	**(175,823)**	**(195,967)**	**(91,428)**	**–**	**(463,218)**	(261,875)	(130,723)	(86,782)	–	(479,380)
Expenses for the acquisition of insurance contracts	**(101,518)**	**(87,393)**	**(67,723)**	**–**	**(256,634)**	(108,346)	(74,582)	(45,015)	–	(227,943)
Administration expenses	**(25,794)**	**(56,057)**	**(29,531)**	**(1,245)**	**(112,627)**	(19,622)	(46,250)	(17,326)	–	(83,198)
Other expenses	**(26,384)**	**(41,136)**	**(31,597)**	**(17,822)**	**(116,939)**	(19,149)	(33,042)	(14,112)	(10,196)	(76,499)
Foreign exchange (losses)/gains	**(35,800)**	**(7,065)**	**6,989**	**10,322**	**(25,554)**	108,345	32,507	(22,100)	(8,997)	109,755
Total expenses	**(365,319)**	**(387,618)**	**(213,290)**	**(8,745)**	**(974,972)**	(300,647)	(252,090)	(185,335)	(19,193)	(757,265)
Results of operating activities	**180,512**	**20,565**	**124,587**	**129**	**325,793**	137,266	31,791	4,507	(63,486)	110,078
Finance costs	**(616)**	**(20)**	**(407)**	**(4,250)**	**(5,293)**	(273)	(35)	(186)	(4,664)	(5,158)
Share of profit of associates after tax	**–**	**–**	**–**	**118**	**118**	–	–	–	260	260
Profit before tax	**179,896**	**20,545**	**124,180**	**(4,003)**	**320,618**	136,993	31,756	4,321	(67,890)	105,180

*Interest revenues included total £74,584,000 (2008: £89,608,000).

The following charges are included within the consolidated income statement:

	Year to 31 December 2009					Year to 31 December 2008				
	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
Depreciation	**650**	**3,230**	**1,187**	**60**	**5,127**	1,348	3,007	921	47	5,323
Amortisation of intangible assets	**635**	**135**	**149**	**–**	**919**	–	135	123	1	259

The Group's wholly owned subsidiary, Hiscox Syndicates Limited, oversees the operation of Syndicate 33 at Lloyd's. The Group's percentage participation in Syndicate 33 can fluctuate from year to year and consequently, presentation of the results at the 100% level removes any distortions arising therefrom.

	Year to 31 December 2009					Year to 31 December 2008 Restated				
100% ratio analysis	London Market	UK and Europe	International	Corporate Centre	Total	London Market	UK and Europe	International	Corporate Centre	Total
Claims ratio (%)	**38.8**	**53.4**	**33.0**	**–**	**41.8**	61.2	42.2	44.6	–	52.7
Expense ratio (%)	**32.2**	**49.9**	**45.6**	**–**	**40.4**	33.3	50.1	37.9	–	38.9
Combined ratio excluding foreign exchange impact (%)	**71.0**	**103.3**	**78.6**	**–**	**82.2**	94.5	92.3	82.5	–	91.6
Foreign exchange impact (%)	**7.8**	**1.8**	**(2.3)**	**–**	**3.8**	(28.7)	(10.7)	10.6	–	(16.3)
Combined ratio (%)	**78.8**	**105.1**	**76.3**	**–**	**86.0**	65.8	81.6	93.1	–	75.3
Combined ratio excluding non monetary foreign exchange impact (%)	**71.5**	**103.9**	**76.3**	**–**	**81.7**	73.2	82.4	93.1	–	80.0

4 Operating segments continued

(a) Profit before tax by segment continued

The claims ratio is calculated as claims and claim adjustment expenses, net of reinsurance, as a proportion of net premiums earned. The expense ratio is calculated as the total of expenses for the acquisition of insurance contracts, administration expenses and other expenses as a proportion of net premiums earned. The foreign exchange impact ratio is calculated as the foreign exchange gains or losses as a proportion of net premiums earned. The combined ratio is the total of the claims, expense and foreign exchange impact ratios. The combined ratio excluding non monetary foreign exchange impact is calculated by adjusting the net premiums earned and the expenses for the acquisition of insurance contracts by the movement arising from retranslating net unearned premiums and net deferred acquisition costs at year end rates of exchange. All ratios are calculated using the 100% results.

Costs allocated to the Corporate Centre are non-underwriting related costs and are not included within the combined ratio. The impact on profit before tax of a 1% change in each component of the segmental combined ratios is:

	Year to 31 December 2009				Year to 31 December 2008 Restated			
	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	London Market £000	UK and Europe £000	International £000	Corporate Centre £000
At 100% level (note 4b)								
1% change in claims or expense ratio	6,248	3,824	2,875	–	5,894	3,179	2,076	–
At Group level								
1% change in claims or expense ratio	4,533	3,673	2,775	–	4,278	3,034	1,970	–

(b) 100% operating result by segment

	Year to 31 December 2009					Year to 31 December 2008 Restated				
	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
Gross premiums written	914,072	440,064	359,297	–	1,713,433	752,593	374,254	262,893	–	1,389,740
Net premiums written	666,692	408,037	287,589	–	1,362,318	500,585	344,342	219,560	–	1,064,487
Net premiums earned	624,755	382,417	287,524	–	1,294,696	589,446	317,868	207,552	–	1,114,866
Investment result – financial assets	111,446	36,428	59,297	9,168	216,339	(7,525)	(11,960)	(8,567)	(1,798)	(29,850)
Investment result – derivatives	(1,643)	1,967	(83)	(296)	(55)	–	(10,483)	–	(42,495)	(52,978)
Other revenues	–	2,716	677	2	3,395	23	2,929	35	–	2,987
Claims and claim adjustment expenses, net of reinsurance	(242,422)	(204,330)	(94,873)	–	(541,625)	(360,919)	(133,983)	(92,600)	–	(587,502)
Expenses for the acquisition of insurance contracts	(139,923)	(92,562)	(69,185)	–	(301,670)	(149,755)	(79,357)	(46,599)	–	(275,711)
Administration expenses	(34,196)	(56,812)	(30,427)	(1,245)	(122,680)	(26,905)	(46,964)	(18,391)	–	(92,260)
Other expenses	(26,858)	(41,136)	(31,613)	(17,822)	(117,429)	(19,531)	(33,042)	(13,589)	(10,196)	(76,358)
Foreign exchange (losses)/gains	(48,912)	(6,951)	6,678	10,322	(38,863)	169,393	34,152	(21,971)	(8,997)	172,577
Results of operating activities	242,247	21,737	127,995	129	392,108	194,227	39,160	5,870	(63,486)	175,771

Segment results at the 100% level presented above differ from those presented at the Group's share at note 4(a) solely as a result of the Group not owning 100% of the capacity of Syndicate 33 at Lloyd's.

(c) Segmental analysis of assets and liabilities

The segment assets and liabilities at 31 December and the capital expenditure for the year then ended are as follows:

	31 December 2009					
	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Intragroup items and eliminations £000	Total £000
Intangible assets	32,647	2,715	8,522	6,529	–	50,413
Deferred acquisition costs	59,741	44,735	36,453	–	576	141,505
Financial assets	1,161,612	365,268	604,927	75,118	213,693	2,420,618
Reinsurance assets	472,998	146,435	103,630	–	(302,937)	420,126
Other assets	369,751	235,075	294,113	925,940	(1,040,129)	784,750
Total assets	2,096,749	794,228	1,047,645	1,007,587	(1,128,797)	3,817,412
Insurance liabilities	1,326,719	482,577	384,186	–	(71,131)	2,122,351
Other liabilities	657,956	185,355	173,219	168,193	(610,948)	573,775
Total liabilities	1,984,675	667,932	557,405	168,193	(682,079)	2,696,126
Capital expenditure	1,539	2,245	6,962	275		11,021

Notes to the consolidated financial statements
continued

4 Operating segments continued
(c) Segmental analysis of assets and liabilities continued

	31 December 2008 Restated					
	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Intragroup items and eliminations £000	Total £000
Intangible assets	30,507	2,850	8,645	6,555	–	48,557
Deferred acquisition costs	52,609	41,102	37,901	–	(482)	131,130
Financial assets	1,175,492	320,776	471,676	121,028	–	2,088,972
Reinsurance assets	469,971	120,662	113,799	–	(200,638)	503,794
Other assets	482,204	231,224	536,702	742,713	(1,005,953)	986,890
Total assets	2,210,783	716,614	1,168,723	870,296	(1,207,073)	3,759,343
Insurance liabilities	1,541,644	436,949	498,964	–	(200,141)	2,277,416
Other liabilities	573,752	219,436	109,566	196,041	(567,894)	530,901
Total liabilities	2,115,396	656,385	608,530	196,041	(768,035)	2,808,317
Capital expenditure	8,622	337	934	220		10,113

Segment assets and liabilities primarily consist of operating assets and liabilities, which represent the majority of the balance sheet. Intragroup assets and liabilities that cross segments are presented under the separate category heading 'Intragroup items and eliminations'.

Capital expenditure comprises expenditure on intangible assets (note 15) other than goodwill, and additions to property, plant and equipment (note 16), but excluding assets acquired on business combinations.

(d) Geographical information
The Group's operational segments underwrite business domestically in Bermuda and from locations in the UK and Ireland, the US, Guernsey, France, Germany, Belgium, the Netherlands, Spain, Portugal, Sweden and Austria.

The following table provides an analysis of the Group's gross premium revenues earned by material geographical location from external parties:

	Year to 31 December 2009					Year to 31 December 2008 Restated				
Gross premium revenues earned from external parties	**London Market £000**	**UK and Europe £000**	**International £000**	**Corporate Centre £000**	**Total £000**	London Market £000	UK and Europe £000	International £000	Corporate Centre £000	Total £000
UK and Ireland	**33,028**	**257,873**	**24,298**	**–**	**315,199**	22,279	220,213	23,803	–	266,295
Europe	**47,271**	**111,552**	**30,513**	**–**	**189,336**	51,127	86,371	18,914	–	156,412
United States	**324,757**	**4,440**	**190,738**	**–**	**519,935**	285,796	4,567	147,472	–	437,835
Rest of World	**224,878**	**23,337**	**91,013**	**–**	**339,228**	232,044	23,535	55,390	–	310,969
	629,934	**397,202**	**336,562**	**–**	**1,363,698**	591,246	334,686	245,579	–	1,171,511

The Group's largest external policyholder contributed less than 2% of total gross Group premium revenues earned and the details thereof are not disclosed on the grounds of materiality.

The Group has not reported geographical segmental details of non-current assets excluding financial instruments and including loans and receivables, rights and obligations under insurance and reinsurance contracts, investments in associates and subsidiaries on the grounds of the relevance of these items to the Group's operations and the usefulness of such information to users.

5 Net asset value per share

	2009		2008	
	Net asset value (total equity) £000	NAV per share pence	Net asset value (total equity) £000	NAV per share pence
Net asset value	**1,121,286**	**299.2**	951,026	258.1
Net tangible asset value	**1,070,873**	**285.7**	902,469	244.9

The net asset value per share is based on 374,819,025 shares (2008: 368,477,595 shares), being the adjusted number of shares in issue at 31 December.

Net tangible assets comprise total equity excluding intangible assets.

6 Return on equity

	2009 £000	2008 £000
Profit for the year (all attributable to owners of the Company)	**280,497**	70,808
Opening shareholders' equity	**951,026**	824,304
Adjusted for the time weighted impact of capital distributions and issuance of shares	**(20,429)**	(55,700)
Adjusted opening shareholders' equity	**930,597**	768,604
Annualised return on equity (%)	**30.1**	9.2

7 Investment result

The total result for the Group before taxation comprises:

	Note	2009 £000	2008 £000
Investment income including interest receivable		**75,740**	94,678
Net realised gains on financial investments at fair value through profit or loss		**19,733**	4,743
Net fair value gains/(losses) on financial investments at fair value through profit or loss		**87,296**	(127,053)
Investment result – financial assets	8	**182,769**	(27,632)
Fair value gains/(losses) on derivative financial instruments	22	**396**	(52,978)
Total result		**183,165**	(80,610)

Investment expenses are presented within other expenses (note 9).

8 Analysis of return on financial investments

(a) The weighted average return on financial investments for the year by currency, based on monthly asset values, was:

	2009 %	2008 %
Sterling	**4.2**	(0.1)
US Dollar	**8.5**	(2.5)
Other	**6.5**	0.4

(b) Investment return

	London Market		UK and Europe		International		Corporate Centre		2009 Total	
	£000	%	£000	%	£000	%	£000	%	£000	%
Debt and fixed income securities	**80,616**	**8.0**	**19,212**	**5.9**	**48,887**	**9.2**	**4,239**	**3.8**	**152,954**	**7.7**
Equities and shares in unit trusts	**–**	**–**	**14,769**	**28.5**	**7,668**	**17.5**	**3,923**	**12.3**	**26,360**	**20.7**
Deposits with credit institutions/ cash and cash equivalents	**285**	**0.7**	**954**	**1.4**	**1,210**	**0.4**	**1,006**	**3.3**	**3,455**	**0.8**
	80,901	**7.7**	**34,935**	**7.8**	**57,765**	**6.8**	**9,168**	**5.2**	**182,769**	**7.2**

	London Market		UK and Europe		International		Corporate Centre		2008 Total Restated	
	£000	%	£000	%	£000	%	£000	%	£000	%
Debt and fixed income securities	(7,966)	(0.9)	7,374	3.4	(7,819)	(2.2)	4,384	5.4	(4,027)	(0.3)
Equities and shares in unit trusts	–	–	(25,529)	(41.9)	(5,552)	(16.2)	(7,186)	(18.0)	(38,267)	(28.4)
Deposits with credit institutions/ cash and cash equivalents	2,503	4.2	6,227	5.0	4,928	2.8	1,004	2.6	14,662	3.7
	(5,463)	(0.6)	(11,928)	(3.0)	(8,443)	(1.5)	(1,798)	(1.1)	(27,632)	(1.3)

9 Other revenues and expenses

	2009 £000	2008 £000
Agency related income	**6,651**	5,324
Profit commission	**12,248**	14,382
Other underwriting income, catastrophe bonds	**410**	–
Other income	**189**	152
Other revenues	**19,498**	19,858
Managing agency expenses	**33,051**	19,513
Overseas underwriting agency expenses	**47,943**	28,787
Connect agency expenses	**11,795**	13,343
Investment expenses	**2,690**	1,899
Other Group expenses including central overheads	**21,460**	12,957
Other expenses	**116,939**	76,499

10 Employee benefit expense

The aggregate remuneration and associated costs were:

	Note	2009 £000	2008 £000
Wages and salaries, including holiday pay and sabbatical leave charges		**108,626**	79,048
Social security costs		**12,391**	10,468
Share based payments cost of options granted to Directors and employees	25	**5,260**	5,269
Pension costs – defined contribution		**6,510**	5,794
Pension costs – net expense/(credit) arising on defined benefit schemes	31	**13,300**	–
		146,087	100,579

The average monthly number of staff employed by the Group was 1,061 (2008: 914) comprising 368 underwriting and 693 administrative staff (2008: 335 and 579 respectively). Of the total remuneration shown above, an amount of £21,555,000 (2008: £21,053,000) was recharged to Syndicate 33.

11 Finance costs

	Note	2009 £000	2008 £000
Interest and expenses associated with bank borrowings		**2,493**	3,201
Interest and charges associated with Letters of Credit	36	**2,780**	1,922
Interest charges arising on finance leases	37	**20**	35
		5,293	5,158

12 Auditors' remuneration

Fees payable to the Group's main external auditors, KPMG, its member firms and its associates (exclusive of VAT) include the following amounts recorded in the consolidated income statement:

Group	2009 £000	2008 £000
Fees payable to the Company's auditors for the audit of the Group's consolidated financial statements	**188**	262
Fees payable to the Company's auditors and its associates for other services:		
The audit of subsidiaries pursuant to legislation	**638**	519
Other services pursuant to legislation	**90**	75
All other services*	**185**	75
	1,101	931
Fees in respect of the defined benefit pension scheme:		
Audit	**11**	12
Total auditors' remuneration expense	**1,112**	943

*Other fees relate primarily to corporate advisory and financial reporting consulting services. Non-audit services with fees greater than £50,000 must be pre-approved by the Audit Committee which is composed solely of independent Non Executive Directors.

12 Auditors' remuneration continued

The full audit fee payable for the Syndicate audit has been included above, although an element of this is borne by the third-party participants in the Syndicate.

Fees payable to other external auditors in respect of the Company's subsidiaries in the US pursuant to legislation during 2009 were £52,000 (2008: £23,000).

13 Net foreign exchange (losses)/gains

The net foreign exchange (losses)/gains for the year include the following amounts:

	2009 £000	2008 £000
Exchange (losses)/gains recognised in the consolidated income statement	**(25,554)**	109,755
Exchange (losses)/gains classified as a separate component of equity	**(69,589)**	150,582
Overall impact of foreign exchange related items on net assets	**(95,143)**	260,337

The above excludes profit or losses on foreign exchange derivative financial instruments which are included within the investment result.

Net unearned premiums and deferred acquisition costs are treated as non monetary items in accordance with IFRS. As a result, a foreign exchange mismatch arises caused by these items being earned at historical rates of exchange prevailing at the original transaction date whereby resulting claims are retranslated at the end of each period. The impact of this mismatch on the income statement is shown below.

	2009 £000	2008 £000
Opening balance sheet impact of non retranslation of non monetary items	**50,525**	14,438
(Loss)/gain included within profit representing the non retranslation of non monetary items	**(53,732)**	36,087
Closing balance sheet impact of non retranslation of non monetary items	**(3,207)**	50,525

14 Foreign currency items on economic hedges and intragroup borrowings

In the prior year, the Group highlighted two separate charges on the consolidated income statement to enable readers to obtain a fuller understanding of their impact and that of related amounts recognised directly in other comprehensive income. The current year comparatives are not significant and as such this presentation has not been applied to the consolidated income statement for the year ended 31 December 2009. The current year comparatives are shown below:

Impact as at 31 December 2009	Consolidated income statement 2009 £000	Consolidated other comprehensive income 2009 £000	Total impact on equity 2009 £000
Realised gains on foreign currency derivative contracts used to manage retranslation risk associated with the net investment in Bermuda and Guernsey insurance operations	**314**	**–**	**314**
Retranslation loss on managed net investment in Bermuda and Guernsey insurance operations	**–**	**(5,207)**	**(5,207)**
Unrealised translation (losses)/gains on intragroup borrowings	**(4,362)**	**4,362**	**–**
Total losses recognised	**(4,048)**	**(845)**	**(4,893)**

Impact as at 31 December 2008	Consolidated income statement 2008 £000	Consolidated other comprehensive income 2008 £000	Total impact on equity 2008 £000
Unrealised losses on foreign currency derivative contracts used to manage retranslation risk associated with the net investment in Bermuda and Guernsey insurance operations	(42,540)	–	(42,540)
Retranslation gain on managed net investment in Bermuda and Guernsey insurance operations	–	67,591	67,591
Unrealised translation (losses)/gains on intragroup borrowings	(12,580)	12,580	–
Total (losses)/gains recognised	(55,120)	80,171	25,051

Foreign exchange losses of £6,058,000 before tax (£4,362,000 after tax) (2008: £8,463,000 and £12,580,000 respectively) have been recorded on certain loan arrangements, denominated in US Dollars, between Group companies. In most cases, as one party to each arrangement has a functional currency other than the US Dollar, foreign exchange losses arise which are not eliminated through the income statement on consolidation. Implicit offsetting gains are reflected instead on retranslation of the counterparty company's closing balance sheet through other comprehensive income and into the Group's currency translation reserve within equity.

In the prior year the Group entered into US Dollar currency option collar contracts which were contracted in September and October 2008 to serve as informal hedges of part of the Group's net investment in its Bermuda and Guernsey insurance operations (note 22).

14 Foreign currency items on economic hedges and intragroup borrowings continued

The contracts expired in January 2009 and a gain of £314,000 was recognised for the year ended 31 December 2009. Formal hedge accounting designation was not achievable due to the specific effectiveness requirements of IAS 39.

The Group did not enter into any new economic hedging derivative contracts during the current year.

15 Intangible assets

	Goodwill £000	Syndicate capacity £000	State authorisation licences £000	Other £000	Total £000
At 1 January 2008					
Cost	8,496	24,505	5,083	5,361	43,445
Accumulated amortisation and impairment	(2,430)	–	–	(563)	(2,993)
Net book amount	6,066	24,505	5,083	4,798	40,452
Year ended 31 December 2008					
Opening net book amount	6,066	24,505	5,083	4,798	40,452
Additions in year on business combinations	1,909	–	1,225	–	3,134
Other additions	–	–	–	5,230	5,230
Amortisation charges	–	–	–	(259)	(259)
Closing net book amount	7,975	24,505	6,308	9,769	48,557
At 31 December 2008					
Cost	10,405	24,505	6,308	10,591	51,809
Accumulated amortisation and impairment	(2,430)	–	–	(822)	(3,252)
Net book amount	7,975	24,505	6,308	9,769	48,557
Year ended 31 December 2009					
Opening net book amount	**7,975**	**24,505**	**6,308**	**9,769**	**48,557**
Other additions	**–**	**–**	**–**	**2,775**	**2,775**
Amortisation charges	**–**	**–**	**–**	**(919)**	**(919)**
Closing net book amount	**7,975**	**24,505**	**6,308**	**11,625**	**50,413**
At 31 December 2009					
Cost	**10,405**	**24,505**	**6,308**	**13,366**	**54,584**
Accumulated amortisation and impairment	**(2,430)**	**–**	**–**	**(1,741)**	**(4,171)**
Net book amount	**7,975**	**24,505**	**6,308**	**11,625**	**50,413**

Goodwill is allocated to the Group’s cash generating units (CGUs) identified according to country of operation and business segment. Goodwill is considered to have an indefinite life and as such is tested for impairment annually on a value in use basis similar to that described below for the Group's intangible asset relating to Syndicate capacity. Accumulated amortisation and impairment of goodwill relates to the amortisation charged prior to the Group’s adoption of IFRS.

The Group’s intangible asset relating to Syndicate capacity has been allocated, for impairment testing purposes, to one individual CGU being the active Lloyd’s corporate member entity. The Group has considered the recoverable amount from the active Lloyd’s corporate member entity on a value in use basis. This calculation uses cash flow projections based on financial forecasts approved by management covering a five-year period. Cash flows beyond the five-year period are extrapolated based on an average level of return and annual growth estimated at 2.5% (2008: 2%) consistent with the industry long-term average. A pre-tax discount factor of 1.8% (2008: 7%) has been applied to projected cash flows as part of the exercise. The results of this exercise indicate that the recoverable amount significantly exceeds the intangible’s carrying value and would not be sensitive to reasonably possible changes in assumptions. The Group’s weighted average cost recognised on the balance sheet is significantly below the average open market price witnessed in the recent Lloyd’s of London Syndicate 33 capacity auctions in Autumn 2009.

The Group has previously recognised intangible assets totalling £6,308,000 relating to insurance authorisation licences for 50 US states acquired in the business combination of ALTOHA Inc. (note 34). This intangible asset has been allocated for impairment testing purposes to one individual CGU being the Group’s North American underwriting businesses. The Group has considered the recoverable amount of this CGU on a consistent basis to the active Lloyd’s corporate member entity outlined above.

15 Intangible assets continued

Other intangible assets relate to the costs of acquiring rights to customer contractual relationships from AON Limited in 2007, and the additions during 2008 and 2009 relate to software licence and development costs.

The amortisation charge for the year includes £660,000 (2008: £nil) relating to capitalised software costs and is included in other expenses in the income statement. The net book value of capitalised software costs at 31 December 2009 was £7,368,000 (2008: £5,230,000). There are no charges for impairment during the current or prior financial year.

At 31 December 2009 there were no assets under development on which no amortisation has been charged (2008: £5,230,000).

16 Property, plant and equipment

	Land and buildings £000	Leasehold improvements £000	Vehicles £000	Furniture, fittings and equipment and art £000	Total £000
At 1 January 2008					
Cost	2,985	1,044	896	34,978	39,903
Accumulated depreciation	(160)	(379)	(300)	(19,686)	(20,525)
Net book amount	2,825	665	596	15,292	19,378
Year ended 31 December 2008					
Opening net book amount	2,825	665	596	15,292	19,378
Additions	–	257	145	4,450	4,852
Disposals	–	–	(47)	(23)	(70)
Depreciation charge	(40)	(222)	(144)	(4,917)	(5,323)
Foreign exchange movements	–	254	–	577	831
Closing net book amount	2,785	954	550	15,379	19,668
At 31 December 2008					
Cost	2,985	1,700	968	40,413	46,066
Accumulated depreciation	(200)	(746)	(418)	(25,034)	(26,398)
Net book amount	2,785	954	550	15,379	19,668
Year ended 31 December 2009					
Opening net book amount	**2,785**	**954**	**550**	**15,379**	**19,668**
Additions	**3,022**	**2,286**	**–**	**2,938**	**8,246**
Disposals	**–**	**(214)**	**(13)**	**(69)**	**(296)**
Depreciation charge	**(59)**	**(330)**	**(94)**	**(4,644)**	**(5,127)**
Foreign exchange movements	**–**	**(95)**	**(1)**	**(151)**	**(247)**
Closing net book amount	**5,748**	**2,601**	**442**	**13,453**	**22,244**
At 31 December 2009					
Cost	**6,007**	**3,807**	**940**	**42,732**	**53,486**
Accumulated depreciation	**(259)**	**(1,206)**	**(498)**	**(29,279)**	**(31,242)**
Net book amount	**5,748**	**2,601**	**442**	**13,453**	**22,244**

The Group's land and buildings assets relate to freehold property in the UK and US.

Assets with a net book value of £398,000 were held under finance leases (2008: £582,000). The total depreciation charge for the year in respect of assets held under finance leases was £56,000 (2008: £116,000) and is included in other expenses.

At 31 December 2009 there were £1,906,000 of assets under development upon which no depreciation has yet been charged (2008: £3,106,000).

17 Investments in associates

Movement in carrying value	2009 £000	2008 £000
Year ended 31 December		
At beginning of year	**7,200**	1,502
Additions during the year	**–**	5,438
Share of post-tax profit recognised for the period	**118**	260
At end of year	**7,318**	7,200

The Group's interests in its principal associates, all of which are unlisted, were as follows:

	% interest held at 31 December	Assets £000	Liabilities £000	Revenues £000	Profit after tax £000
		100% results			
2009					
Associates incorporated in the UK	**From 25% to 49%**	**11,100**	**7,800**	**8,743**	**234**
Associates incorporated in Europe	**up to 25%**	**943**	**436**	**1,379**	**30**
Total at the end of 2009		**12,043**	**8,236**	**10,122**	**264**

	% interest held at 31 December	Assets £000	Liabilities £000	Revenues £000	Profit after tax £000
		100% results			
2008					
Associates incorporated in the UK	From 25% to 49%	11,981	8,809	6,214	877
Associates incorporated in Europe	up to 25%	2,066	1,289	1,483	268
Total at the end of 2008		14,047	10,098	7,697	1,145

There were no additional investments in associates made during 2009.

The equity interests held by the Group in respect of associates do not have quoted market prices and are not traded regularly in any active recognised market. The associates concerned have no material impact on the results or assets of the Group. No impairments were identified during the current or prior financial year under review.

During the prior year the Group made equity investments in Senior Wright Indemnity Ltd and Media Insurance Brokers. Cash consideration of £5,438,000 was paid.

18 Deferred acquisition costs

	2009			2008		
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Balance deferred at 1 January	**131,130**	**(21,068)**	**110,062**	123,081	(14,568)	108,513
Acquisition costs incurred in relation to insurance contracts written	**312,705**	**(42,212)**	**270,493**	270,126	(40,634)	229,492
Acquisition costs expensed to the income statement	**(302,330)**	**45,696**	**(256,634)**	(262,077)	34,134	(227,943)
Balance deferred at 31 December	**141,505**	**(17,584)**	**123,921**	131,130	(21,068)	110,062

The deferred amount of insurance contract acquisition costs attributable to reinsurers of £17,584,000 (2008: £21,068,000) is not eligible for offset against the gross balance sheet asset and is included separately within trade and other payables (note 28).

The amounts expected to be recovered before and after one year are estimated as follows:

	2009 £000	2008 £000
Within one year	**123,921**	110,062
After one year	**–**	–
	123,921	110,062

19 Reinsurance assets

	Note	2009 £000	2008 £000
Reinsurers' share of insurance liabilities		**425,572**	511,325
Provision for non-recovery and impairment		**(5,446)**	(7,531)
Reinsurance assets	27	**420,126**	503,794

The amounts expected to be recovered before and after one year, based on historical experience, are estimated as follows:

Within one year	**217,278**	254,546
After one year	**202,848**	249,248
	420,126	503,794

Amounts due from reinsurers in respect of outstanding premiums and claims already paid by the Group are included in loans and receivables (note 21). The Group recognised a gain during the year of £2,085,000 (2008: loss of £4,205,000) in respect of impaired balances.

20 Financial assets and liabilities

Financial assets are measured at their bid price values, with all changes from one accounting period to the next being recorded through the income statement, except in the case of unlisted equity investments, and borrowing instruments that formed part of a designated hedge accounting relationship from 3 January 2007 to 6 May 2008 as provided for by IAS 39.

	Note	2009 Fair value £000	2008 Fair value £000
Debt and fixed income securities		**2,255,737**	1,928,599
Equities and shares in unit trusts		**133,841**	124,864
Deposits with credit institutions		**11,394**	28,269
Total investments		**2,400,972**	2,081,732
Catastrophe bonds		**11,310**	–
Derivative financial instruments	22	**1,018**	40
Total financial assets carried at fair value		**2,413,300**	2,081,772

	Note	2009 Fair value £000	2008 Fair value £000
Borrowings from credit institutions carried at amortised cost*		**138,000**	90,278
Derivative financial instruments	22	**539**	53,072
Total financial liabilities		**138,539**	143,350

*The fair value of borrowings from credit institutions is not considered to be significantly different from the amortised cost.

An analysis of the credit risk and contractual maturity profiles of the Group's financial instruments is given in notes 3.2(c) and 3.2(d).

The Group's investment in catastrophe bonds consists of £11.3 million, comprising of 12 catastrophe bonds with credit ratings of BB or above. The issuers of these securities have used the proceeds to collateralise certain catastrophe reinsurance obligations mainly in US and European wind and earthquake risks. The investment in these contracts is therefore at risk of loss, in whole or in part if a covered catastrophe occurs.

The Group's borrowings from credit institutions at 31 December 2009 are denominated in Pound Sterling (2008: US Dollars). The entire amount from December 2008 was repaid during the year and the amount outstanding at 31 December 2009 is expected to be repaid in full within one year from the balance sheet date. The movement in fair value of derivative instrument liabilities includes settlements totalling £49,838,000, realised gains of £3,234,000 and unrealised losses of £539,000.

From 3 January 2007 until 6 May 2008, the Group designated US$182 million of foreign currency borrowings as hedging instruments in a net investment hedge relationship. The hedging relationship was effective throughout the entire period.

20 Financial assets and liabilities continued

Investments at 31 December are denominated in the following currencies at their fair value:

	2009 £000	2008 £000
Debt and fixed income securities		
Sterling	**508,292**	293,697
US Dollars	**1,559,673**	1,378,167
Euro and other currencies	**187,772**	256,735
	2,255,737	1,928,599
Equities and shares in unit trusts		
Sterling	**60,549**	55,011
US Dollars	**51,914**	45,611
Euro and other currencies	**21,378**	24,242
	133,841	124,864
Deposits with credit institutions		
Sterling	**11,223**	21,335
US Dollars	**171**	6,934
Euro and other currencies	**–**	–
	11,394	28,269
Total investments	**2,400,972**	2,081,732

21 Loans and receivables including insurance receivables

	2009 £000	2008 £000
Gross receivables arising from insurance and reinsurance contracts	**413,449**	441,752
Provision for impairment	**(955)**	(560)
Net receivables arising from insurance and reinsurance contracts	**412,494**	441,192
Due from contract holders, brokers, agents and intermediaries	**270,593**	274,470
Due from reinsurance operations	**141,901**	166,722
	412,494	441,192
Prepayments and accrued income	**10,020**	7,948
Other loans and receivables:		
Net profit commission receivable	**17,758**	11,959
Accrued interest	**12,227**	9,480
Share of Syndicate's other debtors' balances	**20,273**	13,546
Other debtors including related party amounts	**16,010**	10,190
Total loans and receivables including insurance receivables	**488,782**	494,315

The amounts expected to be recovered before and after one year are estimated as follows:		
Within one year	**482,194**	491,529
After one year	**6,588**	2,786
	488,782	494,315

There is no significant concentration of credit risk with respect to loans and receivables as the Group has a large number of internationally dispersed debtors. The Group has recognised a loss of £395,000 (2008: gain of £832,000) for the impairment of receivables during the year ended 31 December 2009.

22 Derivative financial instruments

The Group entered into both exchange-traded and over the counter derivative contracts for a number of purposes during 2009. The Group had the right and intention to settle each contract on a net basis. The assets and liabilities of these contracts at 31 December 2009 all mature within one year of the balance sheet date and are detailed below:

31 December 2009

Derivative financial instrument assets included on balance sheet	Gross contract notional amount £000	Fair value of assets £000	Fair value of liabilities £000	Net balance sheet position £000
Foreign exchange forward contracts	50,105	180	7	173
Interest rate futures contracts	21,288	906	61	845
	71,393	1,086	68	1,018

Derivative financial instrument liabilities included on balance sheet	Gross contract notional amount US$000	Fair value of assets £000	Fair value of liabilities £000	Net balance sheet position £000
Event linked futures contracts	2,400	18	557	539

31 December 2008

Derivative financial instrument assets included on balance sheet	Gross contract notional amount US$000	Fair value of assets £000	Fair value of liabilities £000	Net balance sheet position £000
Event linked futures contracts	80	474	434	40

Derivative financial instrument liabilities included on balance sheet	Gross contract notional amount 000	Fair value of assets £000	Fair value of liabilities £000	Net balance sheet position £000
Foreign exchange option collar contracts	US$600,000	–	42,540	42,540
Foreign exchange forward contracts	€68,680	–	10,532	10,532
		–	53,072	53,072

Foreign exchange forward contracts

During the current and prior year the Group entered into a series of conventional over the counter forward contracts in order to secure translation gains made on Euro, US Dollar and other non Pound Sterling denominated monetary assets. The contracts require the Group to forward sell a fixed amount of the relevant currency for Pound Sterling at pre-agreed future exchange rates. The Group made a gain on these forward contracts of £769,000 (2008: loss of £10,123,000) as included in note 7. The opposite exchange loss is included within financial investments.

There was no initial purchase cost associated with these instruments.

Interest rate futures contracts

During the year the Group continued short selling a number of Government bond futures and sovereign futures denominated in a range of currencies to informally hedge substantially all of the interest rate risk on specific long portfolios of the matching currencies denominated corporate bonds. All contracts are exchange traded and the Group made a loss on these futures contracts of £78,000 (2008: £360,000) as included in note 7.

Event linked future contracts

In June 2008 the Group commenced trading event linked future contracts which are transacted on the Chicago Climate Futures Exchange. The contracts have fixed maturity dates and are structured such that cash inflows are binary in nature and are triggered by the occurrence of specific natural events in specific geographical zones which cause pre-determined losses to the insurance industry in excess of a specified amount. The Group itself does not have to suffer losses to receive a payment once the industry loss strike amount on each contract has been reached. Consequently the contracts are not accounted for as insurance contracts in accordance with IFRS 4.

The Group made a loss on event linked future contracts of £609,000 (2008: gain of £45,000) as included in note 7.

Foreign exchange option collar contracts

During the fourth quarter of 2008 the Group's capital benefited from a significant uplift in net asset value due to the appreciation of the US Dollar to Pound Sterling exchange rate which increased the translated values of its net investments in the Bermuda and Guernsey insurance operations. During September and October 2008 the US Dollar fluctuated significantly and in order to protect the majority of the exchange gains earned to date the Group progressively hedged the risk of subsequent US Dollar weakness impacting this capital by entering into a series of currency option collar contracts. These over the counter instruments have no initial purchase cost and consist of covered call and protective put options which essentially protect the Group against material downside movements in US Dollar to Pound Sterling exchange rate whilst at the same time limiting further participation in material US Dollar strengthening beyond an upper cap. These contracts settled in 2009 and the Group made a gain of £314,000 (2008: loss of £42,540,000) as included in notes 7 and 14. The related exchange loss recognised on the retranslation of the hedged portion of underlying net investments concerned was £5,207,000 and is included within the overall loss of £69,589,000 recognised in other comprehensive income (note 13).

23 Fair value measurements

In accordance with the *Amendments to IFRS7 Financial Instruments: Disclosures*, the fair value of financial instruments based on a three-level fair value hierarchy that reflects the significance of the inputs used in measuring the fair value is provided below.

As at 31 December 2009	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial assets				
Debt and fixed income securities	**627,702**	**1,628,035**	**–**	**2,255,737**
Equities and shares in unit trusts	**162**	**129,419**	**4,260**	**133,841**
Deposits with credit institutions	**11,394**	**–**	**–**	**11,394**
Catastrophe bonds	**–**	**11,310**	**–**	**11,310**
Derivative financial instruments	**–**	**1,018**	**–**	**1,018**
Total	**639,258**	**1,769,782**	**4,260**	**2,413,300**
Financial liabilities				
Derivative financial instruments	**–**	**539**	**–**	**539**

As at 31 December 2008	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Financial assets				
Debt and fixed income securities	605,222	1,323,377	–	1,928,599
Equities and shares in unit trusts	2,043	122,282	539	124,864
Deposits with credit institutions	22,392	–	5,877	28,269
Catastrophe bonds	–	–	–	–
Derivative financial instruments	–	–	40	40
Total	629,657	1,445,659	6,456	2,081,772
Financial liabilities				
Derivative financial instruments	–	53,072	–	53,072

The levels of the fair value hierarchy are defined by the standard as follows:

- Level 1 – fair values measured using quoted prices (unadjusted) in active markets for identical instruments;
- Level 2 – fair values measured using directly or indirectly observable inputs or other similar valuation techniques for which all significant inputs are based on observable market data;
- Level 3 – fair values measured using valuation techniques for which significant inputs are not based on market observable data.

The fair values of the Group's financial assets are based on prices provided by investment managers who obtain market data from numerous independent pricing services. The pricing services used by the investment manager obtain actual transaction prices for securities that have quoted prices in active markets. For those securities which are not actively traded, the pricing services use common market valuation pricing models. Observable inputs used in common market valuation pricing models include, but are not limited to, broker quotes, credit ratings, interest rates and yield curves, prepayment speeds, default rates and other such inputs which are available from market sources.

The fair values of the Group's investments in catastrophe bonds are based on quoted market prices or, where such prices are not available, by reference to broker or underwriter bid indications.

Investments in mutual funds comprise a portfolio of stock investments in trading entities which are invested in various quoted investments. The fair value of shares in unit trusts are based on the net asset value of the fund as reported by independent pricing sources or the fund manager.

Included within Level 1 of the fair value hierarchy are Government bonds, Treasury bills and exchange traded equities which are measured based on quoted prices.

23 Fair value measurements continued

Level 2 of the hierarchy contains US Government Agencies, Corporate Securities, Asset Backed Securities and Mortgage Backed Securities and Catastrophe bonds. The fair value of these assets are based on the prices obtained from both investment managers and investment custodians as discussed above. The Group records the unadjusted price provided and validates the price through a number of methods including a comparison of the prices provided by the investment managers with the investment custodians and the valuation used by external parties to derive fair value. Quoted prices for US Government Agencies and Corporate Securities are based on a limited number of transactions for those securities and as such the Group considers these instruments to have similar characteristics of those instruments classified as Level 2. Also included within Level 2 are units held in traditional long funds and long and short special funds and over the counter derivatives.

Level 3 contains investments in a limited partnership and unquoted equity securities which have limited observable inputs on which to measure fair value. In the prior year, investments in a mutual fund were included within level 3 as redemptions from the fund were suspended. The fund was redeemed in full in 2009. Unquoted equities are carried at cost, which is deemed to be comparable to fair value. The effect of changing one or more inputs used in the measurement of fair value of these instruments to another reasonably possible assumption would not be significant and no further analysis has been performed.

Derivative instruments included within Level 3 in the prior year represented event linked future contracts which are transacted on the Chicago Climate Futures Exchange. During the current year, the classification of these instruments was reviewed and they have been transferred into Level 2 as the valuation of the derivative is based on observable inputs used by the exchange to determine fair value.

In certain cases, the inputs used to measure the fair value of a financial instrument may fall into more than one level within the fair value hierarchy. In this instance, the fair value of the instrument in its entirety is classified based on the lowest level of input that is significant to the fair value measurement.

During the year, there were no transfers made between Level 1 and Level 2 of the fair value hierarchy.

The following table sets forth a reconciliation of opening and closing balances for financial instruments classified under Level 3 of the fair value hierarchy:

31 December 2009	Equities and shares in unit trusts £000	Deposits with credit institutions £000	Derivative Instruments £000	Total £000
Balance at 1 January	**539**	**5,877**	**40**	**6,456**
Total gains or losses through profit or loss*	**245**	**–**	**–**	**245**
Purchases	**3,353**	**–**	**–**	**3,353**
Issues	**123**	**–**	**–**	**123**
Settlements	**–**	**(5,877)**	**–**	**(5,877)**
Transfer into Level 2	**–**	**–**	**(40)**	**(40)**
Closing balance	**4,260**	**–**	**–**	**4,260**

*Total gains/(losses) are included within the investment result in the income statement.

31 December 2008	Equities and shares in unit trusts £000	Deposits with credit institutions £000	Derivative Instruments £000	Total £000
Balance at 1 January	–	–	–	–
Total gains or losses through profit or loss*	–	–	–	–
Purchases	539	–	40	579
Transfers into Level 3	–	5,877	–	5,877
Settlements	–	–	–	–
Closing balance	539	5,877	40	6,456

*Total gains/(losses) are included within the investment result in the income statement.

24 Cash and cash equivalents

	2009 £000	2008 £000
Cash at bank and in hand	**166,780**	353,542
Short-term bank deposits	**92,867**	87,080
	259,647	440,622

The Group holds its cash deposits with a well diversified range of banks and financial institutions.

Cash and cash equivalents include amounts of US$334,000 (2008: US$17,775,000) held in escrow to settle deferred consideration on acquisitions.

25 Share capital

Group	Share capital £000 31 December 2009	Number of shares 31 December 2009	Share capital £000 31 December 2008	Number of shares 31 December 2008
Issued share capital	**20,158**	**403,148,858**	20,067	401,330,601

The amounts presented in the equity structure of the Group above relate to Hiscox Ltd, the legal parent Company.

Changes in Group share capital and contributed surplus	Ordinary share capital £000	Share premium £000	Contributed surplus £000
At 1 January 2008	19,898	4,955	398,834
Employee share option scheme – proceeds from shares issued	169	4,463	–
Dividends to owners of the Company	–	–	(46,756)
At 31 December 2008	20,067	9,418	352,078
Employee share option scheme – proceeds from shares issued	91	2,413	–
Dividends to owners of the Company	–	–	(48,613)
At 31 December 2009	**20,158**	**11,831**	**303,465**

In accordance with the reverse acquisition provisions of IFRS 3 Business Combinations, the amount of issued share capital included in the consolidated balance sheet reflects that of Hiscox plc, the Group's former legal parent company, up until the date of the reverse acquisition on 12 December 2006 together with that issued subsequently by Hiscox Ltd, the new legal parent, up until each respective balance sheet date.

Contributed surplus is a distributable reserve and arose on the reverse acquisition of Hiscox plc on 12 December 2006.

Equity structure of Hiscox Ltd	Number of 5p ordinary shares in issue (thousands) 2009	Number of 5p ordinary shares in issue (thousands) 2008
At 1 January	**401,331**	397,938
Employee share option scheme – ordinary shares issued	**1,818**	3,393
At 31 December	**403,149**	401,331

All issued shares are fully paid.

Share options and performance share plan awards

Performance share plan awards are granted to Directors and to senior employees. Up until 2005, share options were also granted. The exercise price of the granted options is equal to the closing mid-market price of the shares on the day before the date of the grant. No exercise price is attached to performance plan awards, although their attainment is conditional on the employee completing three years' service (the vesting period) and the Group achieving targeted levels of returns on equity. Share options are also conditional on the employee completing three years' service (the vesting period) or less under exceptional circumstances (death, disability, retirement or redundancy). The options are exercisable starting three years from the grant date only if the Group achieves its targets of return on equity; the options have a contractual option term of ten years. The Group has no legal or constructive obligation to re-purchase or settle the options in cash.

In accordance with IFRS 2 the Group recognises an expense for the fair value of share option and performance share plan award instruments issued to employees, over their vesting period through the income statement. The expense recognised in the Consolidated Income Statement during the year was £5,260,000 (2008: £5,269,000). This comprises charges of £4,972,000 (2008: £4,960,000) in respect of performance share plan awards and £288,000 (2008: £309,000) in respect of share option awards. The Group has applied the principles outlined in the Black-Scholes option pricing model when determining the fair value of each share option instrument and discounted cash flow methodology in respect of performance share plan awards.

The range of principal Group assumptions applied in determining the fair value of share based payment instruments granted during the year under review are:

Assumptions affecting inputs to fair value models	2009	2008
Annual risk free rates of return and discount rates (%)	**1.4**	3.2-5.6
Long-term dividend yield (%)	**4.24**	4.75
Expected life of options (years)	**3.25**	3.25
Implied volatility of share price (%)	**31**	27-30
Weighted average share price (p)	**310.8**	247.9

25 Share capital continued

Share options and performance share plan awards continued

The weighted average fair value of each share option granted during the year was 85.5p (2008: 60.5p). The weighted average fair value of each performance share plan award granted during the year was 308.0p (2008: 213.4p).

Movements in the number of share options during the year and details of the balances outstanding at 31 December 2009 are shown in the Directors' remuneration report.

The implied volatility assumption is based on historical data for periods of between five and ten years immediately preceding grant date.

For options issued after 1 January 2006 the assumptions regarding long-term dividend yield have been aligned to the progressive dividend policy announced during the 2005 Rights Issue.

Additional details on the Group's share option schemes are shown in the Directors' remuneration report accompanying these financial statements.

26 Retained earnings and other reserves

	2009 £000	2008 £000
Currency translation reserve at 31 December	**37,728**	107,317
Retained earnings at 31 December	**784,104**	462,146

The currency translation reserve comprises qualifying net investment gains and losses and foreign exchange differences arising from the translation of the financial statements of, and investments in, foreign operations.

There were no transactions by the Company in its own shares during the year.

During 2008, Hiscox Ltd purchased 28,300,742 of ordinary shares of 5p each in open market transactions. These shares are held in treasury. In addition, during 2008, 1,000,000 ordinary shares of 5p each were purchased and held in trust. Retained earnings reduced by £65,066,000 being the consideration paid for these transactions. Included within this amount were transaction cost expenses of £125,000 directly related to the purchases. The highest price paid per share was 260p, the lowest price paid was 191.5p and the average price paid was 221.7p per share.

At 31 December 2009 Hiscox Ltd held 28,142,874 shares in treasury. Additional details are shown in note 38 to these financial statements in respect of additional Hiscox Ltd shares held by subsidiaries.

Included within Group retained earnings is an amount of £27,068,000 (2008: £23,932,000), which is not distributable and is held to meet solvency capital requirements to maintain an equalisation provision. The amounts in the equalisation provision are realised when particular entities in the Group have suffered insurance losses in excess of levels set out in the relevant solvency capital regulations. In addition, the Group maintains certain levels of capital to meet minimum solvency requirements for regulatory and rating purposes.

27 Insurance liabilities and reinsurance assets

	Note	2009 £000	2008 £000
Gross			
Claims reported and claim adjustment expenses		**800,307**	885,905
Claims incurred but not reported		**749,016**	881,823
Unearned premiums		**573,028**	509,688
Total insurance liabilities, gross		**2,122,351**	2,277,416
Recoverable from reinsurers			
Claims reported and claim adjustment expenses		**173,987**	180,406
Claims incurred but not reported		**154,903**	245,897
Unearned premiums		**91,236**	77,491
Total reinsurers' share of insurance liabilities	19	**420,126**	503,794
Net			
Claims reported and claim adjustment expenses		**626,320**	705,499
Claims incurred but not reported		**594,113**	635,926
Unearned premiums		**481,792**	432,197
Total insurance liabilities, net		**1,702,225**	1,773,622

The amounts expected to be recovered and settled before and after one year, based on historical experience, are estimated as follows:		
Within one year	**939,565**	979,380
After one year	**762,660**	794,242
	1,702,225	1,773,622

Notes to the consolidated financial statements continued

27 Insurance liabilities and reinsurance assets continued

The gross claims reported, the loss adjustment expenses liabilities and the liability for claims incurred but not reported are net of expected recoveries from salvage and subrogation. The amounts for salvage and subrogation at the end of 2009 and 2008 are not material.

27.1 Insurance contracts assumptions
(a) Process used to decide on assumptions
The risks associated with insurance contracts and in particular with casualty insurance contracts are complex and subject to a number of variables that complicate quantitative sensitivity analysis. Delays in the notification of claims necessitate the holding of significant reserves for liabilities that may only emerge a number of accounting periods later.

The impact of inflation on ultimate claim estimates is therefore significant. In addition a greater level of risk may be inherent in reserving estimates for newer types of insurance products where there is a lack of past historical development experience.

For all risks, the Group uses several statistical methods to incorporate the various assumptions made in order to estimate the ultimate cost of claims. The reserves for outstanding claims are actuarially estimated primarily by using both the Chain Ladder and Bornhuetter-Ferguson methods. There is close communication between the actuaries involved in the estimation process and the Group's underwriters to ensure that, when applying both estimation techniques, both parties are cognisant of all material factors relating to outstanding claims, and allowance is also made for the rating environment. Catastrophe events which are expected to impact multiple business units in the Group are analysed by the central analysis team. They combine information from underwriters, the claims team and past experience of similar events to produce gross and net estimates of the ultimate loss cost to each part of the Group. These figures are then incorporated by the acturial team into the quarterly reserving exercise. This process ensures that a consistent approach is taken across the Group.

The Chain Ladder method is adopted for mature classes of business where sufficient claims development data is available in order to produce estimates of the ultimate claims and premiums by actuarial reserving group and underwriting year, or year of account for the managed Syndicate. This methodology produces optimal estimates when a large claims development history is available and the claims development patterns throughout the earliest years are stable.

Where losses in the earliest underwriting years or years of account have yet to fully develop, a 'tail' arises on the reserving data, i.e. a gap between the current stage of development and the fully developed amount. The Chain Ladder methodology is used to calculate average development factors which, by fitting these development factors to a curve, allows an estimate to be made of the potential claims development expected between the current and the fully developed amount, known as a 'tail reserve'. This tail reserve is added to the current reserve position to calculate the total reserve required.

Chain Ladder methods may be applied to premiums, paid claims or incurred claims (i.e. paid claims plus case estimates). The basic technique involves the analysis of historical claims development factors 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 that is not yet fully developed to produce an estimated ultimate claims cost for each accident year.

Chain Ladder techniques are less suitable in cases in which the insurer does not have developed claims history data for a particular class of business (e.g. in relation to more recent underwriting years or years of account). In these instances the Group's actuaries make reference to the Bornhuetter-Ferguson method.

The Bornhuetter-Ferguson method is based on the Chain Ladder approach but utilises estimated ultimate loss ratios. This method uses a combination of a benchmark or market-based estimate and an estimate based on claims experience. The former is based on a measure of exposure such as premiums; the latter is based on the paid or incurred claims to date. The two estimates are combined using a formula that gives more weight to the experience-based estimate as time passes. This technique has been used in situations in which developed claims experience was not available for the projection (recent accident years or new classes of business).

In exceptional cases the required provision is calculated with reference to the actual exposures on individual policies. Adjustments are made within the claims reserving methodologies to remove distortions in the historical claims development patterns from large or isolated claims not expected to re-occur in the future. In addition, the reserves determined for the managed Syndicate are converted to annually accounted figures using earnings patterns that are consistent with those for the underlying Syndicate business.

The choice of selected results for each accident year of each class of business depends on an assessment of the technique that has been most appropriate to observed historical developments. In certain instances, this has meant that different techniques or combinations of techniques have been selected for individual accident years or groups of accident years within the same class of business.

(b) Claims development tables
The development of insurance liabilities provides a measure of the Group's ability to estimate the ultimate value of claims. The Group analyses actual claims development compared with previous estimates on an accident year basis. This exercise is performed to include the liabilities of Syndicate 33 at the 100% level regardless of the Group's actual level of ownership, which has increased significantly over the last eight years. Analysis at the 100% level is required in order to avoid distortions arising from reinsurance to close arrangements which subsequently increase the Group's share of ultimate claims for each accident year, three years after the end of that accident year.

27 **Insurance liabilities and reinsurance assets** continued
27.1 Insurance contracts assumptions continued
(b) Claims development tables *continued*

The top half of each table, on the following pages, illustrates how estimates of ultimate claim costs for each accident year have changed at successive year ends. The bottom half reconciles cumulative claim costs to the amounts still recognised as liabilities. A reconciliation of the liability at the 100% level to the Group's share, as included in the Group balance sheet, is also shown.

Insurance claims and claim adjustment expenses reserves – gross at 100%

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	2008 £000	**2009 £000**	**Total £000**
Estimate of ultimate claims costs as adjusted for foreign exchange*										
at end of accident year	687,619	407,142	456,946	688,408	1,147,193	595,682	798,296	1,105,836	**849,316**	**6,736,438**
one year later	667,957	431,162	468,733	762,649	1,268,711	569,356	715,890	941,165	**–**	**5,825,623**
two years later	740,854	439,171	440,712	727,804	1,270,977	548,523	679,971	–	**–**	**4,848,012**
three years later	764,878	423,316	453,703	687,872	1,252,857	517,992	–	–	**–**	**4,100,618**
four years later	807,184	419,019	448,878	690,802	1,246,928	–	–	–	**–**	**3,612,811**
five years later	803,540	394,730	438,322	673,061	–	–	–	–	**–**	**2,309,653**
six years later	801,393	390,836	433,836	–	–	–	–	–	**–**	**1,626,065**
seven years later	799,815	392,092	–	–	–	–	–	–	**–**	**1,191,907**
eight years later	805,284	–	–	–	–	–	–	–	**–**	**805,284**
Current estimate of cumulative claims	805,284	392,092	433,836	673,061	1,246,928	517,992	679,971	941,165	**849,316**	**6,539,645**
Cumulative payments to date	(700,222)	(342,993)	(381,214)	(579,121)	(1,089,428)	(425,122)	(464,969)	(507,312)	**(178,036)**	**(4,668,417)**
Liability recognised at 100% level	105,062	49,099	52,622	93,940	157,500	92,870	215,002	433,853	**671,280**	**1,871,228**
Liability recognised in respect of prior accident years at 100% level										**95,065**
Total gross liability to external parties at 100% level										**1,966,293**

*The foreign exchange adjustment arises from the retranslation of the estimates at each date using the exchange rate ruling at 31 December 2009.

Reconciliation of 100% disclosures above to Group's share – gross

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	2008 £000	**2009 £000**	**Total £000**
Current estimate of cumulative claims	805,284	392,092	433,836	673,061	1,246,928	517,992	679,971	941,165	**849,316**	**6,539,645**
Less: attributable to external Names	(198,488)	(79,763)	(96,473)	(153,764)	(311,634)	(107,151)	(129,670)	(182,655)	**(149,469)**	**(1,409,067)**
Group's share of current ultimate claims estimate	606,796	312,329	337,363	519,297	935,294	410,841	550,301	758,510	**699,847**	**5,130,578**
Cumulative payments to date	(700,222)	(342,993)	(381,214)	(579,121)	(1,089,428)	(425,122)	(464,969)	(507,312)	**(178,036)**	**(4,668,417)**
Less: attributable to external Names	169,966	67,275	83,332	134,861	274,605	86,974	83,412	89,268	**23,319**	**1,013,012**
Group's share of cumulative payments	(530,256)	(275,718)	(297,882)	(444,260)	(814,823)	(338,148)	(381,557)	(418,044)	**(154,717)**	**(3,655,405)**
Liability for 2001 to 2009 accident years recognised on Group's balance sheet	76,540	36,611	39,481	75,037	120,471	72,693	168,744	340,466	**545,130**	**1,475,173**
Liability for accident years before 2001 recognised on Group's balance sheet										**74,150**
Total Group liability to external parties included in balance sheet – gross**										**1,549,323**

**This represents the claims element of the Group's insurance liabilities.

27 Insurance liabilities and reinsurance assets continued
27.1 Insurance contracts assumptions continued
(b) Claims development tables continued

Insurance claims and claim adjustment expenses reserves – net at 100%

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	2008 £000	**2009 £000**	**Total £000**
Estimate of ultimate claims costs as adjusted for foreign exchange*										
at end of accident year	332,353	274,882	360,173	575,992	678,058	528,238	691,257	768,934	**686,588**	**4,896,475**
one year later	373,821	299,911	379,825	628,824	778,298	520,805	629,054	687,294	**–**	**4,297,832**
two years later	445,270	310,031	346,071	603,964	768,654	503,643	609,807	–	**–**	**3,587,440**
three years later	484,110	286,691	357,087	566,162	743,791	460,391	–	–	**–**	**2,898,232**
four years later	473,028	280,039	348,250	567,034	733,182	–	–	–	**–**	**2,401,533**
five years later	458,392	265,680	343,189	552,954	–	–	–	–	**–**	**1,620,215**
six years later	452,230	259,680	339,738	–	–	–	–	–	**–**	**1,051,648**
seven years later	454,670	265,416	–	–	–	–	–	–	**–**	**720,086**
eight years later	452,892	–	–	–	–	–	–	–	**–**	**452,892**
Current estimate of cumulative claims	452,892	265,416	339,738	552,954	733,182	460,391	609,807	687,294	**686,588**	**4,788,262**
Cumulative payments to date	(391,233)	(216,919)	(290,986)	(467,304)	(605,267)	(374,184)	(387,771)	(397,569)	**(154,283)**	**(3,285,516)**
Liability recognised at 100% level	61,659	48,497	48,752	85,650	127,915	86,207	222,036	289,725	**532,305**	**1,502,746**
Liability recognised in respect of prior accident years at 100% level										**42,040**
Total net liability to external parties at 100% level										**1,544,786**

*The foreign exchange adjustment arises from the retranslation of the estimates at each date using the exchange rate ruling at 31 December 2009.

Reconciliation of 100% disclosures above to Group's share – net

Accident year	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000	2006 £000	2007 £000	2008 £000	**2009 £000**	**Total £000**
Current estimate of cumulative claims	452,892	265,416	339,738	552,954	733,182	460,391	609,807	687,294	**686,588**	**4,788,262**
Less: attributable to external Names	(105,631)	(52,130)	(74,278)	(126,704)	(175,504)	(95,039)	(117,227)	(130,913)	**(117,174)**	**(994,600)**
Group's share of current ultimate claims estimate	347,261	213,286	265,460	426,250	557,678	365,352	492,580	556,381	**569,414**	**3,793,662**
Cumulative payments to date	(391,233)	(216,919)	(290,986)	(467,304)	(605,267)	(374,184)	(387,771)	(397,569)	**(154,283)**	**(3,285,516)**
Less: attributable to external Names	88,950	39,665	61,805	109,032	144,904	76,539	72,739	65,647	**20,906**	**680,187**
Group's share of cumulative payments	(302,283)	(177,254)	(229,181)	(358,272)	(460,363)	(297,645)	(315,032)	(331,922)	**(133,377)**	**(2,605,329)**
Liability for 2001 to 2009 accident years recognised on Group's balance sheet	44,978	36,032	36,279	67,978	97,315	67,707	177,548	224,459	**436,037**	**1,188,333**
Liability for accident years before 2001 recognised on Group's balance sheet										**32,100**
Total Group liability to external parties included in the balance sheet – net**										**1,220,433**

**This represents the claims element of the Group's insurance liabilities and reinsurance assets.

27 Insurance liabilities and reinsurance assets continued

27.2 Movements in insurance claims liabilities and reinsurance claims assets

Year ended 31 December	2009 Gross £000	2009 Reinsurance £000	2009 Net £000	2008 Gross £000	2008 Reinsurance £000	2008 Net £000
Total at beginning of year	**(1,767,728)**	**426,303**	**(1,341,425)**	(1,215,887)	222,672	(993,215)
Claims and loss adjustment expenses for year	**(508,238)**	**45,020**	**(463,218)**	(698,471)	219,091	(479,380)
Cash paid for claims settled in the year	**571,689**	**(110,924)**	**460,765**	549,106	(117,582)	431,524
Exchange differences and other movements	**154,954**	**(31,509)**	**123,445**	(402,476)	102,122	(300,354)
Total at end of year	**(1,549,323)**	**328,890**	**(1,220,433)**	(1,767,728)	426,303	(1,341,425)
Claims reported and loss adjustment expenses	**(800,307)**	**173,987**	**(626,320)**	(885,905)	180,406	(705,499)
Claims incurred but not reported	**(749,016)**	**154,903**	**(594,113)**	(881,823)	245,897	(635,926)
Total at end of year	**(1,549,323)**	**328,890**	**(1,220,433)**	(1,767,728)	426,303	(1,341,425)

The insurance claims expense reported in the consolidated income statement is comprised as follows:

Year ended 31 December	2009 Gross £000	2009 Reinsurance £000	2009 Net £000	2008 Gross £000	2008 Reinsurance £000	2008 Net £000
Current year claims and loss adjustment expenses	**(725,132)**	**122,538**	**(602,594)**	(828,940)	226,808	(602,132)
(Under)/over provision in respect of prior year claims and loss adjustment expenses	**216,894**	**(77,518)**	**139,376**	130,469	(7,717)	122,752
Total claims and claim adjustment expenses	**(508,238)**	**45,020**	**(463,218)**	(698,471)	219,091	(479,380)

28 Trade and other payables

	Note	2009 £000	2008 £000
Creditors arising out of direct insurance operations		**45,476**	35,089
Creditors arising out of reinsurance operations		**157,514**	175,134
		202,990	210,223
Obligations under finance leases	37	**393**	439
Share of Syndicate's other creditors' balances		**316**	2,714
Social security and other taxes payable		**15,424**	10,919
Other creditors		**20,448**	9,493
		36,581	23,565
Reinsurers' share of deferred acquisition costs	18	**17,584**	21,068
Accruals and deferred income		**82,328**	58,050
Total		**339,483**	312,906
The amounts expected to be settled before and after one year are estimated as follows:			
Within one year		**336,383**	300,966
After one year		**3,100**	11,940
		339,483	312,906

The amounts expected to be settled after one year of the balance sheet date primarily relate to finance leases and the Group's provision of sabbatical leave employee benefits.

29 Tax expense

The Company and its subsidiaries are subject to enacted tax laws in the jurisdictions in which they are incorporated and domiciled.

The principal subsidiaries of the Company and the country in which they are incorporated are listed in note 38.

The amounts charged in the consolidated income statement comprise the following:

	Note	2009 £000	2008 £000
Current tax expense/(credit)		**53,375**	(32,341)
Deferred tax (credit)/expense	30	**(13,254)**	66,713
		40,121	34,372

29 Tax expense continued

The standard rate of corporation tax in Bermuda is 0% whereas the effective rate of tax for the Group is 12.5% (2008: 32.7%). A reconciliation of the difference is provided below:

	2009 £000	2008 £000
Profit before tax	**320,618**	105,180
Tax calculated at the standard corporation tax rate applicable in Bermuda: 0% (2008: 0%)	**–**	–
Effects of:		
Tax on profits arising in the UK at 28%	**47,770**	45,790
Overseas tax losses for which a deferred tax asset is recognised	**(8,081)**	(1,681)
Other items	**(99)**	466
Other overseas taxes	**(2,706)**	–
Prior year tax adjustments	**3,237**	(10,203)
Tax charge for the period	**40,121**	34,372

30 Deferred tax

Deferred tax assets	2009 £000	2008 £000
Trading losses in overseas entities	**14,077**	5,996

The deferred tax asset relates to losses arising in overseas entities and is subject to overseas relief against future profits. Management consider it probable that taxable profits will arise in future in order to utilise the deferred tax asset.

Net deferred tax liabilities	2009 £000	2008 £000
Deferred tax assets	**17,658**	21,804
Deferred tax liabilities	**(87,331)**	(96,449)
Total net deferred tax liability	**(69,673)**	(74,645)

Deferred tax assets and deferred tax liabilities relating to the same tax authority are presented net in the Group's balance sheet.

(a) Group deferred tax assets analysed by balance sheet headings

At 31 December	2008 £000	Income statement (charge)/credit £000	Transfer to equity £000	2009 £000
Trading losses in overseas entities	5,996	8,081	–	**14,077**
Deferred tax assets	5,996	8,081	–	**14,077**

At 31 December	2008 £000	Income statement (charge)/credit £000	Transfer to equity £000	2009 £000
Tangible assets	863	741	–	**1,604**
Trade and other payables	4,050	(4,050)	–	**–**
Retirement benefit obligations	–	1,310	–	**1,310**
Intangible assets – Syndicate capacity	4,715	(485)	–	**4,230**
Other items	12,176	(1,461)	(201)	**10,514**
Total deferred tax assets	21,804	(3,945)	(201)	**17,658**

30 Deferred tax continued

(b) Group deferred tax liabilities analysed by balance sheet headings

At 31 December	2008 £000	Income statement (charge)/credit £000	Transfer to equity £000	**2009 £000**
Investment in associated enterprises	(17)	–	–	**(17)**
Financial assets	(922)	469	–	**(453)**
Insurance contracts – equalisation provision*	(6,703)	(10,270)	–	**(16,973)**
Other items	–	–	–	**–**
	(7,642)	(9,801)	–	**(17,443)**
Open years of account	(88,807)	18,919	–	**(69,888)**
Total deferred tax liabilities	(96,449)	9,118	–	**(87,331)**

*The solvency regulations in the UK require certain entities within the Group to establish an equalisation provision, to be utilised against abnormal levels of future losses in certain lines of business. The regulations prescribe that the provision is increased every year by an amount that is calculated as a percentage of net premiums written for those lines of business during the financial year subject to a maximum percentage. The amount of each annual increase is a deductible expense for tax purposes, and the equalisation provision is taxed when released. Equalisation provisions are not permitted under IFRS which therefore results in the temporary difference for tax purposes. Following a change in the legislation at the end of 2008, Lloyd's Corporate Members are also entitled to a tax deduction for claims equalisation losses although this is not a solvency requirement for Lloyd's. The Group has provided for the deferred tax liability on its Corporate Members' claims equalisation reserve during the year.

Deferred income tax assets are recognised for tax losses carried forward to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Group has not provided for deferred tax assets totalling £8,452,000 (2008: £7,628,000) in relation to losses in overseas companies of £22,138,000 (2008: £21,230,000). This is as a result of the transfer of these subsidiaries to Hiscox Ltd from Hiscox plc. In accordance with IAS 12, all deferred tax assets and liabilities are classified as non-current.

31 Employee retirement benefit obligations

The Company's subsidiary, Hiscox plc, operates a defined benefit pension scheme based on final pensionable salary. The scheme closed to future accrual with effect from 31 December 2006 and active members were offered membership of a defined contribution scheme from 1 January 2007. The funds of the defined benefit scheme are controlled by the trustee and are held separately from those of the Group.

The gross amount recognised in the Group balance sheet in respect of the defined benefit scheme is determined as follows:

	2009 £000	2008 £000
Present value of scheme obligations	**140,676**	101,615
Fair value of scheme assets	**(118,391)**	(115,166)
Deficit/(surplus) for funded plans	**22,285**	(13,551)
Unrecognised net actuarial (losses)/gains	**(17,648)**	9,767
Past service costs recognised in other creditors	**(11,800)**	–
Unrecognised surplus deemed irrecoverable	**7,163**	3,784
Net amount recognised as a defined benefit obligation	**–**	–

As the fair value of scheme obligations exceeds the present value of the scheme assets, the scheme reports a deficit. The Group recognises actuarial gains and losses using the corridor method as defined in the Group's accounting policy. As a result of a court ruling during the year, past service costs of £11.8 million have been recognised in respect of the equalisation of the scheme obligation for the period between May 1992 and May 1997. The requirement on the scheme to equalise is based on the Barber case in the early 1990s which established that it was unlawful under EU law for retirement ages for men and women to differ. The past service cost has been recognised immediately and has been included within other creditors as payment in full has been agreed by the Group.

The unrecognised net actuarial gains are the net cumulative gains and losses on both the scheme's obligations and underlying assets.

The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit actuarial cost method. A formal full actuarial valuation is performed on a triennial basis, most recently at 31 December 2008, and updated at each intervening balance sheet date by the actuaries. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of AA rated corporate bonds that have terms to maturity that approximate to the terms of the related pension liability.

The scheme assets are invested as follows:

At 31 December	**2009 £000**	2008 £000
Equities	**42,488**	43,316
Debt and fixed income assets	**65,935**	71,670
Cash	**9,968**	180
	118,391	115,166

The majority of the scheme's debt and fixed income assets are held through the ownership of equity units in managed credit funds issued by Standard Life Assurance Limited which invest in a broad spread of high quality corporate bonds with derivatives used in controlled conditions to extend durations in some cases.

31 Employee retirement benefit obligations continued

The amounts recognised in the Group's income statement are as follows:

	Note	2009 £000	2008 £000
Current service cost		**300**	200
Interest cost		**5,720**	6,135
Expected return on scheme assets		**(7,899)**	(7,720)
Past service costs		**11,800**	–
Net actuarial gain recognised		**–**	(433)
Effect of deemed irrecoverability of surplus		**3,379**	1,818
Total included in staff costs	10	**13,300**	–

The actual return on scheme assets was a gain of £4,221,000 (2008: loss of £10,387,000).

The movement in liability recognised in the Group's balance sheet is as follows:

	Note	2009 £000	2008 £000
At beginning of year		**–**	–
Total expense charged in the income statement of the Group	10	**13,300**	–
Past service costs recognised in other creditors		**(11,800)**	–
Contributions paid		**(1,500)**	–
At end of year		**–**	–

A reconciliation of the fair value of scheme assets is as follows:

	2009 £000	2008 £000
Opening fair value of scheme assets	**115,166**	127,576
Expected return on scheme assets	**7,899**	7,720
Difference between expected and actual return on scheme assets	**(3,678)**	(18,107)
Contributions by the employer	**1,500**	–
Settlements with scheme members	**–**	–
Benefits paid	**(2,496)**	(2,023)
Closing fair value of scheme assets	**118,391**	115,166

A reconciliation of the present value of scheme obligations of the scheme is as follows:

	2009 £000	2008 £000
Opening present value of scheme obligations	**101,615**	106,793
Current service cost	**300**	200
Interest cost	**5,720**	6,135
Actuarial losses/(gains)	**23,737**	(9,490)
Past service costs	**11,800**	–
Benefits paid from scheme	**(2,496)**	(2,023)
Settlements with scheme members	**–**	–
Closing present value of scheme obligations	**140,676**	101,615

A summary of the scheme's recent experience is shown below:

	2009 £000	2008 £000	2007 £000	2006 £000	2005 £000
Experience gains/(losses) on scheme obligations	**–**	–	2,783	(3,310)	(1,223)
Experience (losses)/gains on scheme assets	**(3,678)**	(18,107)	75	6,480	10,764

31 Employee retirement benefit obligations continued

Additional memorandum information at the end of the current and previous four accounting periods is presented below:

	2009 £000	2008 £000	2007 £000	2006 £000	2005 £000
Present value of scheme obligations	**140,676**	101,615	106,793	137,461	137,533
Fair value of scheme assets	**(118,391)**	(115,166)	(127,576)	(133,660)	(101,409)
Present value of unfunded obligations/(surplus scheme assets)	**22,285**	(13,551)	(20,783)	3,801	36,124
Gross liability recognised on balance sheet	**–**	–	–	3,801	16,677

Assumptions regarding future mortality experience are set based on professional advice, published statistics and actual experience.

The average life expectancy in years of a pensioner retiring at age 60 on the balance sheet date is as follows:

	2009 years	2008 years
Male	**24.5**	24.5
Female	**27.6**	27.6

The average life expectancy in years of a pensioner retiring at 60, 15 years after the balance sheet date is as follows:

	2009 years	2008 years
Male	**25.6**	25.6
Female	**28.6**	28.6

Other principal actuarial assumptions are as follows:

	2009 %	2008 %
Discount rate	**5.70**	6.70
Expected return on scheme assets	**6.50**	6.90
Inflation assumption	**3.90**	3.00
Pension increases	**3.90**	3.00

The triennial valuation carried out as at 31 December 2008, resulted in a deficit position of £5.1 million and excludes the impact of the equalisation of scheme obligations. The equalisation of scheme obligations has been included in the valuation as at 31 December 2009 and an amount of £11.8 million has been recognised as past service costs. The Group has agreed to fund the £5.1 million deficit paying equal instalments over four years and to pay the full amount relating to the equalisation of obligations in 2010. During the year the Group made the first instalment of £1.5 million to the defined benefit scheme (2008: £nil). 61% of any scheme surplus or deficit calculated is recharged or refunded to Syndicate 33.

The expected return on scheme assets is based on historical data and management's expectations of long-term future returns. While management believe that the actuarial assumptions are appropriate, any significant changes to those could affect the balance sheet and income statement. Whilst an additional one year of life expectancy for all scheme members might be expected to reduce the present value of unfunded obligations at 31 December 2009 by approximately £4 million, the Group considers that the most sensitive and judgemental assumptions are the discount rate and inflation.

The Group has estimated the sensitivity of the net obligation recognised in the consolidated balance sheet to isolated changes in these assumptions at 31 December 2009 as follows:

	Present value of unfunded obligations before change in assumption £000	Present value of unfunded obligations after change £000	(Increase) /decrease in obligation recognised on balance sheet £000
Effect of a change in discount rate			
Use of discount rate of 5.45%	**(22,285)**	**(30,165)**	**–**
Effect of an increase in inflation			
Use of inflation assumption of 4.15%	**(22,285)**	**(24,454)**	**–**

32 Earnings per share

Basic earnings per share are calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of shares in issue during the year, excluding ordinary shares held by the Group and held in treasury as own shares.

Basic

	2009	2008
Profit for the year attributable to the owners of the Company (£000)	**280,497**	70,808
Weighted average number of ordinary shares (thousands)	**372,848**	377,506
Basic earnings per share (pence per share)	**75.2p**	18.8p

32 Earnings per share continued

Diluted

Diluted earnings per share is calculated adjusting for the assumed conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares, share options and awards. For the share options, a calculation is made to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	2009	2008
Profit for the year attributable to the owners of the Company (£000)	**280,497**	70,808
Weighted average number of ordinary shares in issue (thousands)	**372,848**	377,506
Adjustments for share options (thousands)	**14,966**	13,351
Weighted average number of ordinary shares for diluted earnings per share (thousands)	**387,814**	390,857
Diluted earnings per share (pence per share)	**72.3p**	18.1p

Diluted earnings per share has been calculated after taking account of 14,345,744 (2008: 13,003,000) options and awards under employee share option and performance plan schemes and 619,870 (2008: 348,000) options under SAYE schemes.

33 Dividends paid to owners of the Company

	2009 £000	2008 £000
Interim dividend for the year ended:		
31 December 2009 of 4.5p (net) per share	**16,834**	–
31 December 2008 of 4.25p (net) per share	**–**	15,615
Final dividend for the year ended:		
31 December 2008 of 8.5p (net) per share	**31,779**	–
31 December 2007 of 8.0p (net) per share	**–**	31,141
	48,613	46,756

A second interim dividend in respect of 2009 of 10.5p per share, amounting to a total dividend of 15.0p for the year, was approved by the Board of Directors on 25 February 2010. These financial statements do not reflect this dividend as a distribution or liability in accordance with IAS 10 Events after the reporting period.

34 Acquisitions

The Group did not acquire any associates or subsidiaries during the current year. On 30 September 2008, the Group acquired 100% of the issued share capital of Amershill Limited. Cash consideration of £2,000,000 was paid and goodwill of £1,909,000 was recognised. The fair value of the identifiable net assets acquired was £91,000.

On 16 August 2007, the Group acquired 100% of the share capital of ALTOHA Inc. in the US. The total consideration was £29,052,000 which included contingent consideration of £7,530,000. No goodwill arose on acquisition. Intangible assets of £5,083,000 were initially recognised in respect of the US State authorisation licences held by ALTOHA Inc.'s consolidated operations. During 2008, further cash consideration of £1,225,000 was paid in finalisation of their ultimate purchase value.

35 Disposals

There were no disposals during the current year. The Group disposed of its Hiscox Select A to J Limited subsidiaries on 3 November 2008. The fair value of the net assets were £nil and a cash payment and loss on disposal of £42,000 was incurred. These entities were all non-trading corporate capital vehicles.

36 Contingencies and guarantees

The Group's subsidiaries are like most other insurers, continuously involved in legal proceedings, claims and litigation in the normal course of business.

The Group is subject to insurance solvency regulations in all the territories in which it issues insurance contracts. There are no contingencies associated with the Group's compliance or lack of compliance with these regulations.

36 Contingencies and guarantees continued

The following guarantees have also been issued:
(a) On 18 November 2009, Hiscox Capital Ltd and Hiscox Ltd entered into a deed of covenant in respect of a fellow subsidiary, Hiscox Dedicated Corporate Member Limited, in order to meet the subsidiary's obligations to Lloyd's. The total guarantee given under the deed of covenant (subject to limited exceptions) amounts to US$350 million provided by Hiscox Capital Ltd and £15 million provided by Hiscox Ltd. In the prior year, and up to 18 November 2009, a similar guarantee was provided by Hiscox Ltd and Hiscox Insurance Company (Bermuda) Limited for £138,831,798. The obligations in respect of this deed of covenant are secured by a fixed and floating charge over certain of the investments and other assets of the Company in favour of Lloyd's. Lloyd's has a right to retain the income on the charged investments in circumstances where it considers there to be a risk that the covenant might need to be called and may be met in full.

(b) In the prior year Hiscox plc negotiated a new Letter of Credit and revolving credit facility with Lloyds TSB Bank, for a total of £350 million which may be drawn as cash (under a revolving credit facility), Letter of Credit or a combination thereof, providing that the cash portion does not exceed £200 million. In addition, the terms also provide that upon request the facility may be drawn in foreign currency. At 31 December 2009 $225 million (2008: £137.5 million) was drawn by way of Letter of Credit to support the Funds at Lloyd's requirement and a further £138 million by way of cash (2008: US$130 million).

(c) Hiscox Insurance Company Limited has arranged a Letter of Credit of £50,000 (2008: £50,000) with NatWest Bank plc to support its consortium activities with Lloyd's.

(d) The managed syndicate is subject to the New Central Fund annual contribution, which is an annual fee calculated on gross premiums written. This fee was 0.5% for 2009 and 2008. In addition to this fee, the Council of Lloyd's has the discretion to call a further contribution of up to 3% of capacity if required.

(e) As Hiscox Insurance Company (Bermuda) Limited is not an admitted insurer or reinsurer in the US, the terms of certain US insurance and reinsurance contracts require Hiscox to provide Letters of Credit or other terms of collateral to clients. On 27 February 2009, Hiscox replaced its previous US$300 million facility and entered into a Letter of Credit Reimbursement and Pledge Agreement with Citibank for the provision of a Letter of Credit facility in favour of US ceding companies. The agreement was a three-year secured facility that allowed Hiscox to request the issuance of up to US$450 million in Letters of Credit. Letters of Credit issued under these facilities are collateralised by pledged cash and cash equivalents of Hiscox Bermuda. Letters of Credit under this facility totalling approximately US$109 million were issued with an effective date of 31 December 2009 (2008: US$38 million).

37 Capital and lease commitments

Capital commitments

The Group's capital expenditure contracted for at the balance sheet date but not yet incurred for property, plant and equipment was £614,000 (2008: £225,000).

Operating lease commitments

The Group acts as both lessee and lessor in relation to various offices in the UK and overseas which are held under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights. The Group also has payment obligations in respect of operating leases for certain items of office equipment. Operating lease rental expenses for the year totalled £5,656,000 (2008: £5,499,000). Operating lease rental income for the year totalled £468,000 (2008: £468,000).

The aggregate minimum lease payments required by the Group under non-cancellable operating leases, over the expected lease terms, are as follows:

		2009 £000	2008 £000
No later than one year	Land and buildings	**5,683**	5,621
	Office equipment	**177**	144
Later than one year and no later than five years	Land and buildings	**15,730**	17,913
	Office equipment	**457**	99
Later than five years	Land and buildings	**14,501**	17,497
		36,548	41,274

The total future aggregate minimum lease rentals receivable by the Group as lessor under non-cancellable operating property leases are as follows:

	2009 £000	2008 £000
No later than one year	**468**	468
Later than one year and no later than five years	**1,053**	1,521
Later than five years	**–**	–
	1,521	1,989

37 Capital and lease commitments continued

Obligations under finance leases

It is the Group's policy to lease certain of its motor vehicles under finance lease arrangements. The leases have a typical term of three years and are on a fixed repayment basis with a final lump sum component at the end of each agreement should the Group decide to acquire ownership of the vehicle. Interest rates are fixed at the contract commencement date. The Group's obligations under leases are secured by the lessors' charges over the leased assets.

Finance lease interest expense for the year totalled £20,000 (2008: £35,000).

The finance lease obligations to which the Group is committed include the following minimum lease payments:

	2009 £000	2008 £000
Current liabilities due for settlement no later than one year	**226**	246
Non-current liabilities due for settlement after one year and no later than five years	**177**	223
	403	469
Less: future finance lease interest charges	**(10)**	(30)
	393	439

The present value of the minimum lease payments is not materially different to the currently disclosed obligation.

38 Principal subsidiary companies of Hiscox Ltd at 31 December 2009

Company	Nature of business	Country
Hiscox plc*	Holding company	Great Britain
Hiscox Insurance Company Limited	General insurance	Great Britain
Hiscox Insurance Company (Guernsey) Limited*	General insurance	Guernsey
Hiscox Inc.	Underwriting agent	USA (Delaware)
Hiscox Holdings Inc.	Insurance holding company	USA (Delaware)
ALTOHA Inc.	Holding company	USA (Delaware)
American Live Stock Inc.	Underwriting agent	USA (Illinois)
Hiscox Insurance Company Inc.	General insurance	USA (Illinois)
Hiscox ASM Limited	Insurance intermediary	Great Britain
Hiscox Insurance Company (Bermuda) Limited*	General insurance and reinsurance	Bermuda
Hiscox Dedicated Corporate Member Limited	Lloyd's corporate Name	Great Britain
Hiscox Select Insurance Fund PLC	Insurance holding company	Great Britain
Hiscox Select Holdings Limited	Insurance holding company	Great Britain
Hiscox Holdings Limited**	Insurance holding company	Great Britain
Hiscox Insurance Holdings Limited	Insurance holding company	Great Britain
Hiscox Assurances Services SARL	Underwriting agent	France
Hiscox International Holdings B.V.	Insurance holding company	Netherlands
Hiscox Syndicates Limited	Lloyd's managing agent	Great Britain
Hiscox Underwriting Ltd	Underwriting agent	Great Britain
Hiscox AG	Underwriting agent	Germany
Hiscox Overseas Holdings B.V.*	Holding company	Netherlands
Hiscox bv	Underwriting agent	Netherlands
Hiscox Connect Limited	Online intermediary	Great Britain
Hiscox Underwriting Group Services Limited	Service company	Great Britain
Hiscox NV	Underwriting agent	Belgium
Hiscox Trustees Limited†	Corporate trustee	Great Britain
Hiscox Pension Trustees Limited	Pension trustee	Great Britain
Hiscox Qualifying Employees Share Ownership Trustees Limited	Share scheme trustee	Great Britain
Amershill Limited	Underwriting agent	Great Britain
Hiscox Insurance Services (Guernsey) Limited	Underwriting agent	Guernsey
Hiscox Capital Ltd*	General insurance	Bermuda
Hiscox Agency Ltd*	Underwriting agent	Bermuda
Hiscox Services Ltd*	Service company	Bermuda
Hiscox Europe Underwriting Limited	Insurance intermediary	Great Britain
Hiscox Europe Services Limited	Service company	Great Britain

*Held directly.
**Hiscox Holdings Limited held 54,560 shares in Hiscox Ltd (2008: 54,560) at 31 December 2009.
†Hiscox Trustees Limited is the trustee of the Hiscox Employee Share Ownership Plan (ESOP). The ESOP owned 132,399 shares in Hiscox Ltd (2008: 132,399) at 31 December 2009. The shares have been purchased by the ESOP for future use in employee share option schemes and are held as own shares. None of these shares are currently under option to employees, nor have any been conditionally gifted to them.

38 Principal subsidiary companies of Hiscox Ltd at 31 December 2009 continued

All companies are wholly owned. The proportion of voting rights of subsidiaries held is the same as the proportion of equity shares held.

39 Related-party transactions

Details of the remuneration of the Group's key personnel are shown in the Directors' remuneration report on pages 37 to 44. A number of the Group's key personnel hold insurance contracts with the Group, all of which are on normal commercial terms and are not material in nature.

The following transactions were conducted with related parties during the year.

(a) Syndicate 33 at Lloyd's

Hiscox Syndicates Limited, a wholly owned subsidiary of the Company, received management fees and profit commissions for providing a range of management services to Syndicate 33.

	2009 £000	2008 £000
Value of services provided by Hiscox Syndicates Limited to Syndicate 33	**50,845**	55,947
Amounts receivable from Syndicate 33 at 31 December excluding profit commission accrued	**964**	745

(b) Transactions with associates

Certain companies within the Group conduct insurance and other business with associates. These transactions arise in the normal course of obtaining insurance business through brokerages, and are based on arm's length arrangements.

	Total 2009 £000	Total 2008 £000
Gross premium income achieved through associates	**18,530**	20,443
Commission expense charged by associates	**4,632**	4,974
Amounts payable to associates at 31 December	**–**	–
Amounts receivable from associates at 31 December	**–**	128

Details of the Group's associates are given in note 17.

(c) Internal reinsurance arrangements

During the current and prior year, there were a number of reinsurance arrangements entered into in the normal course of trade between various Group companies.

The related results of these transactions have been eliminated on consolidation.

Five year summary

	2009 £000	2008† £000	2007 £000	2006 £000	2005 £000
Results					
Gross premiums written	**1,435,401**	1,147,364	1,198,949	1,126,164	861,174
Net premiums written	**1,157,023**	898,394	974,910	975,397	681,236
Net premiums earned	**1,098,102**	928,095	965,190	888,828	693,299
Profit before tax	**320,618**	105,180	237,199	201,062	70,221
Profit for the year after tax	**280,497**	70,808	191,248	163,846	48,630
Assets employed					
Intangible assets	**50,413**	48,557	40,452	33,212	33,099
Financial assets carried at fair value	**2,413,300**	2,081,772	1,747,827	1,241,910	1,237,778
Cash and cash equivalents	**259,647**	440,622	302,742	502,871	413,759
Insurance liabilities and reinsurance assets	**(1,702,225)**	(1,773,622)	(1,433,799)	(1,291,329)	(1,216,624)
Other net assets	**100,151**	153,697	167,082	195,421	110,001
Net assets	**1,121,286**	951,026	824,304	682,085	578,013
Net asset value per share (p)	**299.2**	258.1	209.5	173.2	147.7
Key statistics					
Basic earnings per share (p)	**75.2**	18.8	48.4	41.7	15.6
Diluted earnings per share (p)	**72.3**	18.1	46.8	40.5	15.1
Combined ratio (%)	**86.0**	75.3	84.4	89.1	96.0
Return on equity (%)	**30.1**	9.2	28.8	28.9	12.8
Dividends per share (p)	**15.00**	12.75	12.00	10.00	7.00
Share price – high* (p)	**362.00**	361.00	304.50	280.25	234.50
Share price – low* (p)	**277.00**	194.75	246.75	193.75	152.25

*Closing mid market prices.
†The 2008 comparatives have been updated from those previously reported to reflect the reclassification of acquisition costs on the purchase of reinsurance contracts from 'outward reinsurance premiums' to 'expenses for the acquisition of insurance contracts' (see note 2.2). Earlier year results have not been adjusted.

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