

Admiral Group Limited

Directors' report and financial
statements

Registered number 03849958

31 December 2003

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Directors and advisers

Non-executive directors

A D Lyons CBE (Chairman)
M Aldag (appointed 13 March 2003)
O J Clarke
D K M James
W P Thompson

Executive directors

H A Engelhardt (Chief Executive)
A C Probert
D G Stevens

Secretary

S D Clarke

Registered office

Capital Tower
Greyfriars Road
Cardiff CF10 3AZ

Auditor

KPMG Audit Plc
Marlborough House
Fitzalan Court
Fitzalan Road
Cardiff CF24 0TE

Actuaries

Ernst & Young
1 More London Place
London SE1 2AF

Bankers

Lloyds TSB
113-116 Leadenhall Street
London EC3 4AX

Bankers

Bank of Scotland Corporate Banking
55 Temple Row
Birmingham B2 5LS

Investment Managers

Alliance Capital Limited
Devonshire House
1 Mayfair Place
London W1J 8AJ

Chief Executive's statement

2003 was a brilliant year!

Let me try and list the highlights of 2003:

- Made a record profit of £71.2m, up 29% from 2002;
- Saw continued improvement in loss ratios across all the back years;
- Total turnover for the year was £427m, up 13% from 2002.
- Premium income grew to £372m, up 12% from 2002;
- Produced a combined ratio of 67.7%;
- Gave more than 4.7m quotes, of which 3.4m started on the internet (72%);
- Named by the Financial Times as the 7th Best Workplace in the UK and one of the Top 100 Workplaces in the EU. Named by The Sunday Times as one of the Top 100 Places To Work in the UK for the fourth consecutive year.

What We Do:

For those of you looking through our accounts for the first time, Admiral's primary business is to sell car insurance direct to the public in the UK. We operate through a number of targeted brands: Admiral (younger drivers, London area), Bell Direct (credit card payers), Diamond (women) and Elephant.co.uk (internet users). We have two other brands, Gladiator Commercial, which operates as an intermediary in the commercial vehicle market, and Confused.com, which operates as an internet 'shopper' for car insurance.

2003 was our 11th year of trading. The first 7 were under the auspices of a Lloyd's of London Managing Agent. However, toward the end of 1999 Management teamed up with Barclays Private Equity to buy the business. The result of this transaction was the creation of Admiral Group Ltd. (AGL) as the holding company. This is the fourth set of accounts for AGL.

When we did the buyout we also put in place a long-term co-insurance agreement with Great Lakes UK, a wholly owned subsidiary of Munich Re, one of the world's largest reinsurers. In 2002 Munich Re also became a shareholder in AGL, taking an 18.6% stake.

Key Performance Information:

Our total written premium for 2003, before sharing premium with our co-insurance and reinsurance partners, was £371.6m, accounting for 87% of our total turnover. The number of customers we service rose to 808,000 from 705,000 (+15%). All our growth has been organic.

Chief Executive's statement *(continued)*

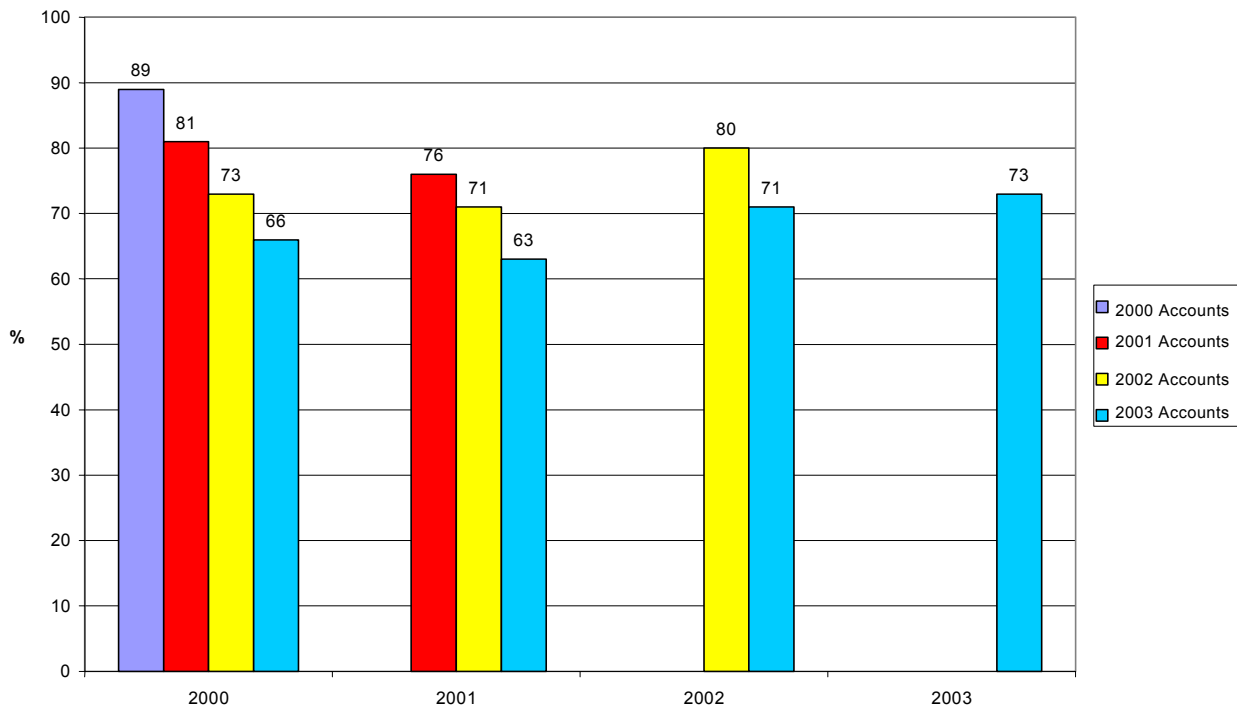
In 2003, 75% of our premium was underwritten by two external insurers. Therefore, AGL's net written premium income was £93m. The same risk sharing agreements are in place for 2004.

Some key numbers from the accounts which follow:

- Claims ratio 52.1% an improvement from 64.6%;
- Expense ratio, adjusted for non-recurring items, 15.6% up from 15.4%;
- Combined ratio 67.7% an improvement from 80.0%;
- Income from products and services we do not underwrite totalled £50.8m up from £40.1m (+27%).

The improvement in claims ratio from 2002 is largely down to reserve releases from 2000, 2001 and 2002 of £16m, accounting for 20 percentage points. The claims ratio without any past or future releases still represents an excellent performance at 72%. We believe that even this figure will prove to be at or better than the market average for 2003. But one cannot discount the releases, since they have become a regular feature of our results. The releases stem from our fundamentally prudent reserving methodology. So, if you read this year's loss ratio as 72% rather than 52.1%, don't forget to go back and reduce prior years' loss ratios! The bar-chart below clearly shows the development of the loss ratios for the back-years. You should read the chart by comparing the different coloured bars across years.

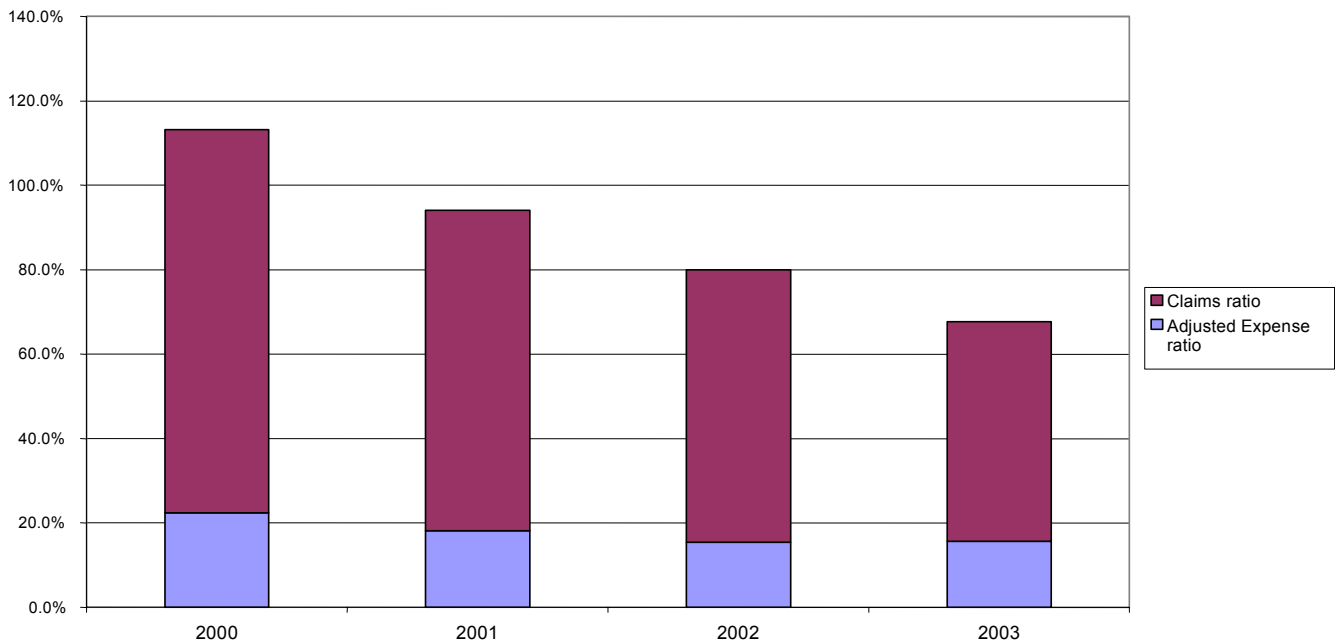
Development of underwriting year



Chief Executive's statement *(continued)*

The slight rise in expense ratio is due to the larger, but very well deserved, staff profit share payment (£1.9m in 2003 v £0.6m in 2002). If the 2003 payment had been the same as the 2002 payment the 2003 expense ratio would have been half a percentage point better than 2002.

Combined Ratio



Ancillary income moved forward due to the increased customer count as well as greater penetration of sales of ancillary products. To put this income into context, I've done a little calculation where the ancillary income is added to earned premium to give a 'big picture' combined ratio. I think this gives an interesting measure of the entire business. Expressed in this way, the combined ratio would drop from 67.7% to 50.9%!

The UK Car Insurance Market Cycle: What Next?

Despite the cyclical nature of the UK car insurance market, we believe these levels of profitability are sustainable. In fact, we fully expect to increase profits in 2004.

The car insurance market is turning, slowly, as I write this report. The maths are not complicated: claims costs are still rising, albeit less than previously thought, but still some 4-6% a year. And premiums aren't!

Last year I noted that the market was at a precarious point, teetering as it was on the precipice. However, I'm pleased to say that there's growing evidence to support our view that cycles will be less extreme going forward. I think we were right in that there were (and still are) a lot of forces tugging the market in two directions. But I was wrong in that the market has not gone downhill.

Chief Executive's statement *(continued)*

There is, of course, within the market result, some jockeying for market share between firms happening behind the scenes, but by and large most of the firms in the market are reporting similar or improved results in 2003 over 2002. In the near term, I think the market will deteriorate at the rate of claims inflation, since we are seeing little movement of rates.

The biggest development of the year was Direct Line/RBS' consumption of Churchill. Unfortunately, I'm not privy to the strategy meetings of that enlarged group, so I cannot tell you what their strategy might be. However, to date they have not decreased rates in any dramatic fashion.

If the market leader is not aggressive in its pricing it would then be up to the next largest insurers to be aggressive if there is to be a large decline in results. However, given unstable investment returns coupled with the published desire of these firms to be profitable it would seem unlikely that any of them would champion a large decrease in rates.

To say none of the other firms in the market mean very much might seem a bit insensitive. However, as the Top Five have nearly 70% share, the rest of us are rather like flies on an elephant's back and therefore unlikely to influence the overall market result. (However, it is worth noting that a fly can live a full and rich life on the back of an elephant!)

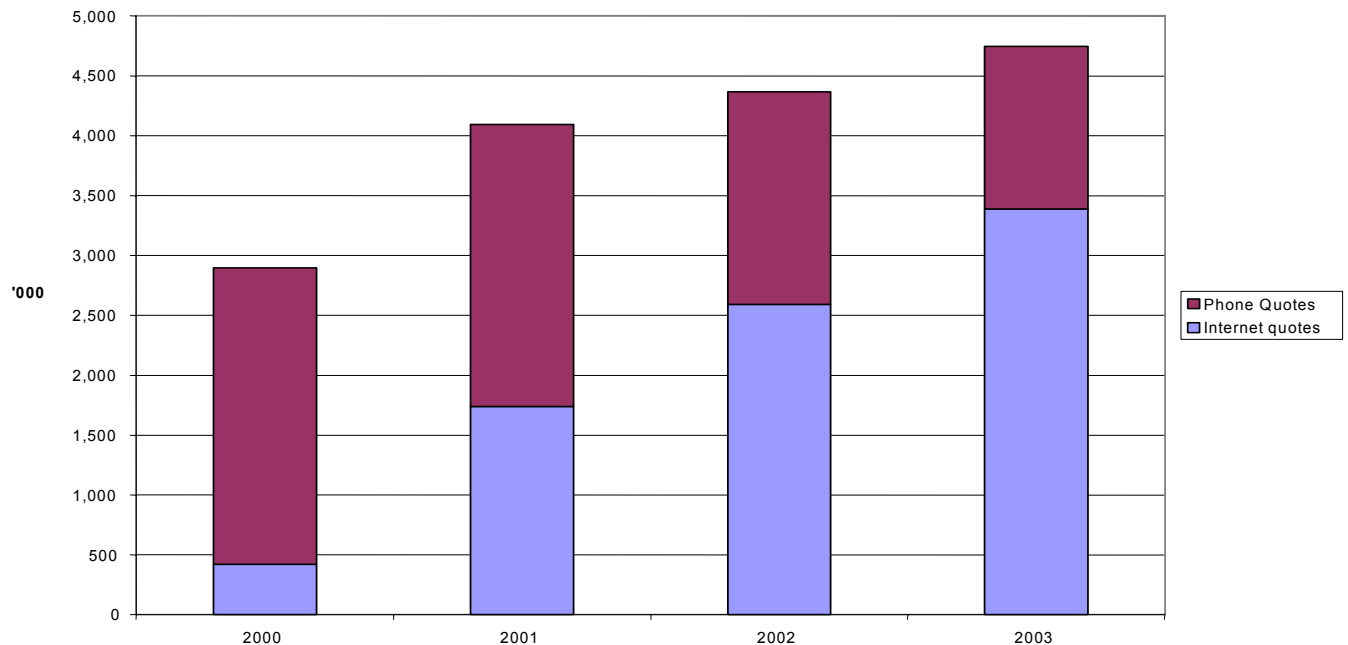
AGL remains well placed in this competitive environment. Our achievements over the last few years in beating the market averages for claims ratio and, separately, expense ratio, mean that we can weather any downturn far better than the competition. And we will have bigger smiles in the upturn.

A Brief Explanation of Why Our Results Are So Good!

Some explanation of our excellent numbers lies with our ability to make the internet work. This is also a source of confidence in our future. Our 2003 internet results exceeded our forecasts and, in the absolute, are quite stunning. Of the more than 4.7m quotes we did last year 72% were started on the internet. Around 57% of all our sales came from these internet quotes. I believe that there is still a huge amount of growth in internet distribution. Research we commissioned in October indicated that more than 70% of consumers have not yet used the internet even to get a quote. As a leader in the internet delivery of car insurance we are well placed for continued success through this channel in the coming years. (In 2004 we expect to have some 800m hits to our websites!)

Chief Executive's statement *(continued)*

Quote volumes split by phone and internet



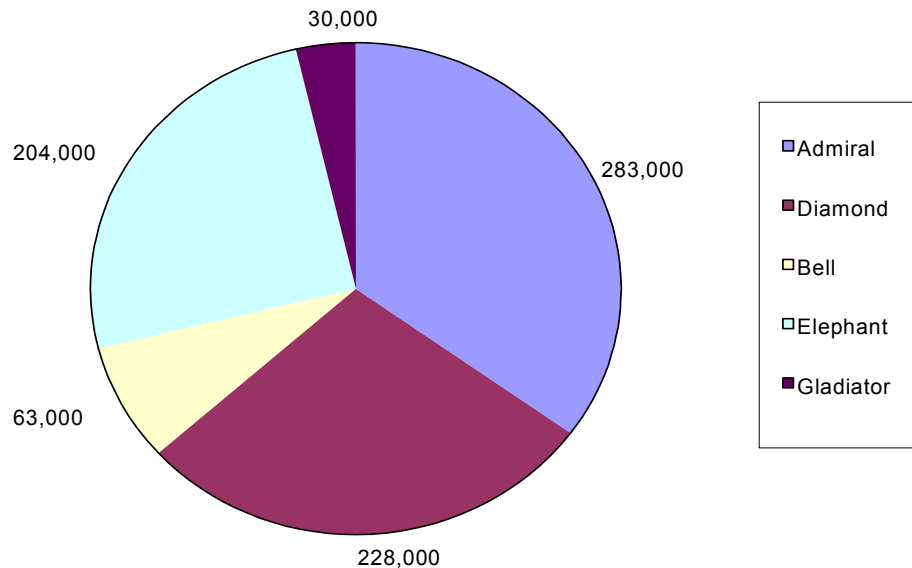
Elephant's end-of-year customer count reached 204,000 (almost doubling from the year before). Elephant quote volumes were up from 1.7m in 2002 to 2.0m in 2003. However, Elephant was not the only internet winner in the Group. In particular, Diamond transacted a much greater proportion of its business over the net than a year ago. Diamond doubled its volume of internet quotes from 2002, 687k up from 340k. The Admiral brand also grew its internet presence. Admiral's volume of internet quotes jumped 62%, to 692k from 426k.

Elephant is now clearly the leading sales brand in the group. It is growing so quickly that it might even end 2004 as the largest brand in the Group. A tremendous achievement considering it launched only in August 2000.

Bell Direct also made news during 2003 by winning the 'Inbound Contact Centre of the Year' award at the National Sales Awards sponsored by the Chartered Institute of Marketing and Institute of Professional Sales. Although Bell is the smallest of the direct brands, its spirit and enthusiasm for quality and innovation serves to validate our strategy of keeping working groups small. (The last paragraph is virtually the same as I wrote last year, the last sentence still true, but this year's award was different and even more prestigious!)

Chief Executive's statement *(continued)*

Customers, by brand, at 31-12-03



Beyond Direct Response Car Insurance:

It was also another good year for Gladiator Commercial. Gladiator sells van insurance, largely to private tradesmen, as an intermediary. Admiral Group does not take any underwriting risk with this business. At the end of 2003 Gladiator's customer count stood at 29,475 and it contributed £1.6m to the Group's bottom line.

2003 was a big growth year for Confused.com. Confused.com is an intelligent, automated car insurance shopper. Simply put, all a customer has to do is put his or her details into Confused.com and Confused then goes out to the major car insurance websites, populates the appropriate fields, and brings the customer back a list of prices. One-stop shopping! Confused actually made a profit in 2003, of £126k. It generated over 580,000 quotes at a cost per quote 43% under budget. We expect a lot of growth from Confused in 2004.

Structural Changes:

2003 was our first year where we did not write business into Lloyd's of London. We began the year underwriting through Admiral Insurance Gibraltar Ltd. (AIGL) and, in the middle of the year, began underwriting through Admiral Insurance Company Ltd. (AICL), an FSA regulated entity.

We did not take on any additional debt nor did we add or subtract any shareholders during the year. We did pay down the anticipated portion of our debt and interest (£14.5m). One further item to note, early in 2004 we paid our first (special) dividend, £15m. The business is highly cashflow generative and future distributions should not be ruled out.

Financial Review

Introduction

The following section presents an analysis of the key financial highlights of the Admiral Group during 2003. The information contained expands on the Chief Executive's statement and also the financial statements.

Key financial highlights

The results for the year, as set out in the technical and non-technical accounts on pages 21 and 22, require some explanation and analysis, as Admiral operates a relatively unusual business model. The majority of Group profits are generated from two sources: firstly, the net motor insurance business that the Group retains and underwrites itself; and secondly from what is effectively an agency business, where the Group manages a larger motor insurance book on behalf of other insurers – sharing a large proportion of the insurance risk with these third parties, whilst earning significant non-insurance income from ancillary product sales on the whole book. These ancillary sales generate a material level of profits.

This model has two key favourable impacts on the business risks the Group faces. Firstly, the underwriting risk retained within the Group is a relatively small share of a larger motor book – a net 25% (as will be explained below). This means that the Group is cushioned from any potential volatility arising in the motor market, but can still enjoy underwriting profits on the net retained share. As noted below, the Group has made significant underwriting profits in the last few years. Secondly, the larger book, combined with the commission arrangements Admiral has in place with the co-insurers and reinsurers, means that the business benefits from significant economies of scale, and importantly, a contribution from the third parties towards expenses.

Group core profits (the measure considered by the directors to best reflect the underlying profitability of the Group) increased by 29% in the year to £71.2m (2002: £55.2m). This figure is reconciled to the profit and loss account figures on page 43 of this report, and is further analysed as follows:

	2003 £'000	2002 £'000
Insurance business profit	32,226	27,186
Ancillary product & instalment contribution	37,113	29,153
Broking & intermediary activities	1,176	425
Aggregate interest receipts	1,166	1,229
Agency profit commission	269	-
Other Group / central expenses	(754)	(2,802)
	<hr/>	<hr/>
	71,196	55,191
	<hr/>	<hr/>

Interest receivable is included in core profits, because the Group generates substantial cash inflow as part of its ongoing business operations, and therefore, this interest represents part of our operations. Interest payable is excluded as this is incurred mainly on servicing the long-term borrowings of the Group.

Group core profits in the first Admiral Group Limited ("AGL") consolidated accounts for the year ended 31 December 2000 were £19.4m, and the 2003 result means that the Group has achieved a compounded annual earnings growth rate of almost 55% in the last four years.

Total gross written motor premium income generated by the Group rose 12% to £372m (2002: £333m), whilst other income jumped 27% to £50.8m (2002: £40.1m). Aggregate Group turnover, which is referred to in the Chief Executive's statement, rose 13% to £427.3m, and this is analysed as follows:

Financial Review *(continued)*

Key financial highlights *(continued)* – Analysis of Group Turnover

	2003 £'000	2002 £'000	
Total written premium	371,600	333,000	Page 21 & note 3
Other income	50,783	40,123	Page 22 & note 7
Technical account investment income	4,881	5,338	Page 21
	<hr/>	<hr/>	
	427,264	378,461	
	<hr/>	<hr/>	

Each key area of Admiral's business is discussed in further detail below:

Insurance business

Some significant changes have been made to the Group's underwriting arrangements for the 2003 year. As mentioned in last year's report, 65% of the total motor insurance business is underwritten by Great Lakes Reinsurance UK Plc ("Great Lakes") – a UK subsidiary of Munich Re. This co-insurance contract runs until the end of 2008, with a possibility of extending for a further year. The remaining 35% is underwritten through the Group's two regulated insurance companies – Admiral Insurance Company Limited ("AICL") and Admiral Insurance (Gibraltar) Limited ("AIGL"). Both of these companies commenced trading in 2003. AICL received permission from the Financial Services Authority ("FSA") to underwrite motor business during the year, whilst AIGL received its license from the Gibraltar Financial Services Commission ("FSC") at the end of 2002.

In addition to the Great Lakes co-insurance contract, there is a quota share reinsurance contract with Converium Re, another leading reinsurer, through AIGL. 10% of the total business written is ceded to Converium. The current contract runs until 31 December 2004. The net effect of all the above is that Admiral bears insurance risk on only 25% of the total book in 2003, up from 20% in 2002. In common with other insurers, the Group also has in place a robust excess of loss reinsurance programme that is designed to protect the Group (and its underwriting partners) against the impact of large individual claims.

Prior to the 2003 underwriting year, the Group's net business was underwritten by the Group's Syndicate (Syndicate 2004) through Lloyd's of London. As noted in detail in last year's report, the decision was taken during 2002 to withdraw from Lloyd's and the Group is now managing the run-off of Syndicate 2004. One of AGL's wholly owned subsidiaries, Admiral Syndicate Limited ("ASL") will continue to provide capital to support the Syndicate until the run-off is complete.

Despite retaining only 25% of the business after co-insurance and reinsurance, the Group has made significant underwriting profits over the period under review. The growth in business written noted above is accompanied by excellent combined ratios (i.e. the ratio of net claims incurred plus net operating expenses to net earned premium). The Group ratios are, once again expected to rank us towards the top of the motor market. The Financial Summary at page 43 sets out our underwriting results over the period from 2000 to 2003, and this demonstrates the favourable development of this element of Admiral's business since the Group's first report in 2000.

2003's loss ratio, after deducting claims handling costs from net claims as noted on page 11, is 52.1% (2002: 64.6%) – an improvement of over 12 percentage points. It is worth noting that the claims management strategy adopted by Admiral has again impacted the ratios favourably, creating significant releases of prior year claims reserves in the financial statements. The 2003 loss ratio is boosted by net reserve releases of £16.1m, compared with £8.7m in 2002. These releases form an ongoing feature of the underwriting results, and are analysed further below. The table shows the actual net value of the releases, along with the relative size of each in relation to the Group's net retained written premium. (Note that there were no releases in the 2000 financial statements, as this was the first year of trading under the current ownership structure.)

Financial Review *(continued)*

Insurance business *(continued)*

Underwriting year & Group net share of GWP	Releases made in each financial year		
	2003 £000 (%)	2002 £000 (%)	2001 £000 (%)
2000 (£75,437,000)	5,176 (6.9)	3,422 (4.5)	3,923 (5.2)
2001 (£100,820,000)	7,938 (7.9)	5,256 (5.2)	-
2002 (£66,391,000)	2,975 (4.5)	-	-
Total net release	16,089	8,678	3,923

As well as these favourable loss ratios, the Group has also produced extremely competitive expense ratios, reflecting a culture of cost control, and the benefits gained from scale and the expense sharing arrangements in place. 2003's expense ratio (as adjusted below) was 15.6%, compared to 15.4% in 2002. The non-recurring expense commission included in the 2002 accounts has now been replaced by profit commission clauses in both the co-insurance and reinsurance contracts. Income from these arrangements is stated separately in the profit and loss account.

Taking the above into account, the adjusted combined ratio for 2003 is 67.7% (2002: 80.0%).

The Group's expense ratio, when taken simply from the profit and loss account includes some material non-recurring items – most notably in 2002. The figures can be adjusted to provide comparability as follows:

	2003 £'000	2002 £'000	
Net earned premium	79,327	81,336	Page 21
Net technical expenses	10,308	7,729	Page 21 & note 4
add non-recurring commission received	-	6,915	
less non-recurring Lloyd's costs	(193)	(2,117)	
add back claims handling costs *	2,230	-	
Adjusted technical expenses	12,345	12,527	
Adjusted expense ratio	15.6%	15.4%	
Adjusted combined ratio	67.7%	80.0%	

* *The Group has reallocated £2.2m of claims handling costs in 2003 from net operating expenses into net claims incurred following commencement of trading of AICL and AIGL during 2003. When calculating ratios these should be included in the expense ratio and not the loss ratio.*

The above figures were matched by another feature of the Admiral business model - exceptional cash inflow. Net cash inflow from operating activities was up 23% to £96.2m (2002: £78.3m), whilst net cash inflow before investment portfolio movements rose 41% to £67.6m (2002: £47.8m).

Financial Review *(continued)*

Ancillary product sales & intermediary activities

A key part of the Group's business strategy is to offer customers a range of attractive ancillary products that complement the motor insurance policy. Whilst a large proportion of the motor insurance risk is co-insured with third parties, Admiral retains full ownership of the policy base, and makes ancillary sales to the whole book. The most significant of these are legal expenses cover, breakdown cover, personal accident protection, instalment payment protection and hire-car cover. The Group does not underwrite these products, and hence no insurance risk is borne on them. They therefore generate stable profit flows at all parts of the insurance cycle. Customers are also offered the option of paying their premium in instalments by direct debit and the Group earns additional income on these policies. These income streams generated £37.1m (2002: £29.2m) of profit for the Group.

The Group also operates a commercial vehicle insurance broker that trades as Gladiator Commercial ("Gladiator") (through Able Insurance Services Limited). Gladiator offers insurance underwritten by a panel of around 22 leading insurers, and earns a variable rate of commission on the policies sold. Gladiator also derives income from ancillary product sales – similar to those discussed above, but with additional products specific to the commercial vehicle market.

Accounting policies

There have been no significant changes to Group accounting policies during 2003. The policies adopted in the preparation of the AGL accounts are set out on pages 27 to 29.

Two significant new sources of accounting guidance were issued during 2003, being the revised ABI Statement of Recommended Practice on accounting for insurance business, and a technical release on Application Note G ("Revenue Recognition by insurance intermediaries"). The impacts of both of these have been fully considered when preparing these financial statements.

Treasury management & cashflow

At the year-end, the Group was holding £239.0m in cash and investments – up 37% (2002: £173.9m).

The Group has three separate managed investment funds – the Syndicate 2004 fund, and one each for AICL and AIGL. Investment management is contracted out to a third party – Alliance Capital Management. Investment strategy is set by the Group Investment Committee (and approved by the directors of each company as appropriate). The strategy is conservative, and all three funds are invested in fixed and variable interest corporate and government securities only. The Group has never invested in equities, and the corporate bond holdings are generally 'A-rated' or better.

Cash held outside these funds also earns interest at a rate just below the UK base rate.

Financial Review *(continued)*

Treasury management & cashflow *(continued)*

An analysis of the year end cash and investments balance is as follows:

	2003	2002
	£'000	£'000
Group "free cash" *	30,035	24,328
Group cash held in regulated entities	40,040	38,668
Deposits with credit institutions	24,464	20,778
Government & sovereign bond holdings	63,525	40,897
Corporate bond holdings	80,936	49,202
	<hr/> 239,000 <hr/>	<hr/> 173,873 <hr/>

(* Free cash represents all cash held outside regulated companies)

Bank borrowings

In 2002 a commercial loan was taken out with Lloyds TSB and Bank of Scotland to replace loan notes supporting the Management Buyout of the Group in late 1999. Details of the borrowing can be found at note 18. During 2003, £12.3m of the capital was repaid, along with £2.2m in interest. Part of the borrowing arrangement is a £10m revolving credit facility, which was not drawn down at the year-end.

Taxation

The charge to taxation in the profit and loss account for 2003 is £18.0m, compared to £12.0m in 2002. This represents 31.5% of profit before taxation (2002: 28%). A reconciliation of the current charge back to 30% of pre-tax profit is set out in note 8 on page 33.

Corporate and social responsibility

Whilst the Group's activities do not have a substantial impact on the environment in most respects, management are conscious that measures can be put in place to minimise any environmental disruption. To this end, the Group has implemented a successful recycling policy. A substantial portion of the Group's waste is sent to a number of plants for recycling.

Admiral has also worked with several independent bodies on environmental matters, including "Keep Wales Tidy" which awarded the Group its top award for "Tidy Business Standards". Further, management consults with experts to ensure the most efficient use possible of building systems, including heating and lighting.

The Group is also mindful of its responsibility to the communities in which it operates and within which its staff live. The Group's Chief Executive has established a scheme called 'Henry's Pot', where staff nominate local charities and organisations to receive donations from the Group. A wide range of organisations have benefited from donations from the fund. In 2003, a total of £16,000 was donated.

In addition to donations to local charities, the Group also supports larger national charities. During 2003, the Group donated around £25,000 to such causes, which included the Born Free Foundation and Breast Cancer Care.

Corporate Governance

The following report summarises the key elements of the Group's corporate governance practices, setting out how the Group manages risk and how the management of the Group's operations is carried on.

The revised guidance (including the Smith and Higgs reports) published during the summer of 2003 has been considered, and the directors are satisfied that the majority of the key features are reflected in the Group's activities. A section at the end of the report analyses areas where the Group does not meet the guidance, and explains why these departures exist.

The Board of Directors

The Board of directors of AGL is structured to ensure an appropriate balance of executive and non-executive directors, and to represent all groups of shareholders. Currently, it comprises an independent non-executive Chairman, non-executive representatives of the corporate shareholders, one further independent non-executive director and three executive directors. The names of all directors appear on page 1 of this report. The number of non-executives outweighs the executive directors by five to three.

The Group has separated the roles of Chairman and Chief Executive, and each has separate, clearly defined responsibilities. The three executive directors have substantial experience in the Group's operations, and all have been with the Group since it commenced trading (then under different ownership) in January 1993.

In addition, three of the Group's subsidiary companies – Admiral Insurance Company Limited ("AICL"), Admiral Insurance (Gibraltar) Limited ("AIGL") and Admiral Syndicate Management Limited ("ASML") have separate non-executive directors on their Boards, over and above or including those referred to above.

The Board has overall responsibility for controlling the Group, making decisions relating to the Group's strategic direction, and measuring progress towards these goals. It is ultimately responsible to shareholders for financial and operational performance.

The Board meets at least eight times a year and more if specific circumstances require it. It is provided with comprehensive reports before each meeting (and throughout the year), covering both financial and operational aspects of the Group's activities.

Operational Committees

In order to ensure it has effective control over the Group's activities, the Board has established a number of committees, each with responsibility for a certain aspect of Group's operations. A summary of the responsibilities and activities of the key committees is set out below:

1. Audit Committee

The Audit Committee comprises Mr James (Committee Chairman), Mr Lyons and Mr A Keys (an independent non-executive director of ASML). Mr James is an independent non-executive director and Mr Lyons is Chairman of AGL. In addition, all the remaining non-executive directors of AGL are entitled to attend meetings.

The main responsibilities of the Audit Committee are:

- a) to monitor the adequacy of the control environment within the Group, including approving and reviewing the work programme for Internal Audit;
- b) to recommend approval to the Board, of the Group financial statements (including key accounting policies and subjective areas) and review any reports on internal controls from the external auditors;
- c) to ensure compliance with all aspects of regulation to which the Group is subject; and
- d) to actively consider and manage the risk of the Group being subject to fraud.

Corporate Governance *(continued)*

1. Audit Committee *(continued)*

The Committee is also responsible for monitoring the independence of the external auditors and approving their remuneration. The Committee also considers and approves the engagement of the external auditors for non-audit services, for which the fees incurred are considered material.

The Group's external auditors attend at least one meeting annually, of which in total there are generally three per year. The directors are confident that members have adequate financial experience, and this is supplemented by training where appropriate.

2. Remuneration Committee

The Remuneration Committee is responsible for considering and approving the remuneration of directors and the Group's structure of bonuses and share scheme incentivisation. The Remuneration Committee's membership consists of the AGL Chairman, a non-executive director (Mr O Clarke) and the Chief Executive. No director is involved in setting his own remuneration package.

3. Additional Committees

In addition to the high level committees above, there are a number of additional committees that are responsible for ensuring the efficient day-to-day operation of the Group and the implementation of the Board's strategies and objectives. These include:

- Independent Review Committee – underwriting and pricing matters;
- Risk Management Committee – regulatory, risk management and compliance matters;
- Investment Committee – investment strategy;
- Nominations Committee – recommendation of top executive positions within the Group.

The Senior Managers of the Group meet monthly, as do the individual departmental managers. The individual brand managers also meet weekly with the Group Chief Executive to discuss business performance and other issues.

Performance Evaluation

The executive directors and the Chairman are subject to regular performance evaluation through an appraisal process. The directors have also performed an evaluation of the Audit Committee during 2003, and will review the performance of other committees where it considers this appropriate.

Internal Control, Risk Management & Internal Audit

The ultimate responsibility for the Group's system of internal control and risk management lies with the Board. Whilst they have not delegated the responsibility for these matters, they have delegated the main supervision of them to the Audit Committee as detailed above.

The Audit Committee is responsible for agreeing in advance the work that Internal Audit carries out. Internal Audit plays a key role in identifying control weaknesses, and considering the extent of business risk to which the Group is exposed. The Audit Committee is also responsible for the review of systems and controls to prevent and detect fraud.

The Audit Committee recommends the approval of the Group financial statements to the main Board of directors. Appropriate financial and accounting qualifications exist among the membership and attendees, and there is significant experience of the Group's accounting policies and practices to ensure appropriate discussion can take place and decisions are made.

Corporate Governance *(continued)*

Internal Control, Risk Management & Internal Audit *(continued)*

As a provider of financial services, the Group is subject to regulation from a number of different bodies – most notably the Financial Services Authority (“FSA”), and is consequently exposed to a level of regulatory risk. The ultimate responsibility for regulatory compliance lies with the Boards of directors of the regulated companies within the Group together with the Approved Persons sponsored by those companies. With the approval of these Boards, each regulated Company has delegated the supervision of (but not responsibility for) regulatory compliance to the Group Compliance Officer.

The Compliance Officer provides advice and support to the Boards of directors, other Approved Persons and to the relevant operational committees. The Compliance Officer has direct access to the Boards of directors of all regulated entities within the Group, as does the Internal Audit Manager.

FSA, FSC and Other Regulation

During 2003, AICL received authorisation from the FSA to underwrite a proportion of the Group's motor business. This has placed an additional level of regulatory requirements on the Group, but one that was well prepared for, and given the regimes already in place (see below), one that has not resulted in any significant changes to Group operations.

ASML is regulated by Lloyd's, and has had to comply with the Lloyd's Acts, Byelaws and other regulations for some time. This has meant that robust controls, systems and procedures have been implemented across all aspects of its business.

AIGL is regulated by the Financial Services Commission (“FSC”) of Gibraltar. These FSC rules must comply with the appropriate EU insurance legislation, and are similar in nature to those adopted in the UK by the FSA.

Two of the main non-underwriting trading subsidiaries of AGL are also members of the General Insurance Standards Council (“GISC”). They are both required to comply with the General Insurance Code for Private Customers, and Gladiator Commercial is obligated to adhere to the Commercial Code. From 2005, the FSA will also assume responsibility for the regulation of general insurance sales and administration. The impact of this on the Group is being carefully monitored, and work is well underway to ensure all appropriate action is taken.

Other significant regulations that the Group has to comply with, such as the Data Protection Act and the Consumer Credit Act, are dealt with in similar ways to the above regulatory frameworks.

“Gap” analysis

The key area where the Group does not comply fully with the Combined Code guidance involves the number of independent non-executive directors. The Group currently has two fully “independent” non-executives (the Chairman - Mr Lyons and Mr James) under the definition of the guidance. The Board does, however, consider that the interests of all shareholders are fully represented on the Board and given the Company's private status, this Board structure is felt to be the most appropriate and effective one at present.

There are two further key departures from the guidance:

- 1) The Audit Committee's membership includes the Group's Chairman, which is contrary to the Combined Code. The Board feels, however, that Mr Lyons' skills and experience make him a key member of the Committee and the fact he is also AGL Chairman does not impact adversely on his performance of the role;
- 2) The Remuneration Committee membership includes the Chief Executive, which is contrary to the guidance. Again, the Board feels that the Group's private status, combined with the fact that the Chief Executive is not party to any discussions about his own remuneration, make the current structure appropriate.

Directors' report

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

Principal activity, business review and future developments

The Company's principal activity is to act as a holding company for the Group's trading and non-trading entities. The Group's principal activity continues to be the selling and administration of private motor insurance and related products.

Detailed descriptions of the Group's activities, results and prospects are contained in the Chief Executive's statement and the Financial Review on pages 2 to 13.

Group results and dividends

The profit for the year, after tax, amounted to £39.2m (2002: £30.9m). No dividend is proposed (2002: £nil).

Directors' interests

The present directors of the Company are shown on page 1.

The following directors were beneficially interested in the ordinary shares of the Company:

	Class of share	31 December 2003	31 December 2002
		Number	Number
A Lyons	C	872	872
H Engelhardt *	B	33,201	33,201
H Engelhardt	C	2,930	2,930
D Stevens	B	16,600	16,600
D Stevens	C	2,600	2,600
A Probert	B	4,150	4,150
A Probert	C	850	850
O Clarke	A	590	590

* The 33,201 B Ordinary Shares relating to H Engelhardt are held in a trust settled by his spouse.

Charitable and political donations

During the year the Group donated £41,000 (2002: £51,000) to various local and national charities. The Group has never made political donations. Refer to the Corporate and Social Responsibility section of the Financial Review on page 13 for further detail.

Employee policies

In considering applications for employment from disabled people, the Group seeks to ensure that fair consideration is given to the abilities and aptitudes of the applicant, while having regard to the requirements of the job for which he or she has applied. Employees who become unable to carry out the job for which they are employed are given individual consideration, and depending on the nature, severity and duration of the disability, may be considered for alternative work and the Group continues to train and encourage the career development of disabled persons in its employment.

Directors' report *(continued)*

Employee policies *(continued)*

The Group provides employees with regular information on its performance, other information that concerns them, and provides a forum for employee representatives to give their views. As described in note 17, the Group operates an Employee Share Trust for the benefit of employees. The charge to the 2003 profit and loss account in respect of this was £6,900,000 (2002: £3,103,000). Further, the Group has also established a non-contractual profit share scheme for staff, under which bonus payments are made according to Group profitability and numerous quality measures. The current year charge for the scheme is £1,932,000 (2002: £555,000).

Every member of staff is invited to attend an annual staff general meeting to achieve a common awareness throughout the Company of the financial and economic factors that affect the performance of the group.

The Group purchases appropriate liability insurance for all staff and directors.

Creditor payment policy

It is the policy of the Group to pay all purchase invoices by their due date, and appropriate quality measures are in place to monitor and encourage this. At the end of the year outstanding invoices represented 19 days purchases (2002: 16).

Auditor

The Company's auditor, KPMG Audit Plc, has indicated its willingness to continue in office and resolutions to reappoint it and to authorise the directors to fix its remuneration will be proposed at the annual general meeting.

By order of the Board,



S D Clarke
Company Secretary

Capital Tower
Greyfriars Road
Cardiff
CF10 3AZ

24 March 2004

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

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

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.



KPMG Audit Plc

Marlborough House
Fitzalan Court
Fitzalan Road
Cardiff CF24 0TE
United Kingdom

Independent auditors' report to the members of Admiral Group Limited

We have audited the financial statements on pages 21 to 42.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the directors' report and, as described on page 19, the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

We read the other information accompanying the financial statements and consider whether it is consistent with those statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and the group as at 31 December 2003 and of the profit of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc
Chartered Accountants
Registered Auditor

24 March 2004

Consolidated profit and loss account: technical account – general business
for the year ended 31 December 2003

	<i>Note</i>	2003		2002	
		£000	£000	£000	£000
Total premiums written	3		371,600		333,000
			<u> </u>		<u> </u>
Gross premiums written	3	129,851		69,089	
Outward reinsurance premiums		(38,555)		(3,662)	
		<u> </u>	91,296	<u> </u>	65,427
Change in the gross provision for unearned premiums		(29,015)		62,464	
Change in the provision for unearned premiums, reinsurers' share		17,046		(46,555)	
		<u> </u>	(11,969)	<u> </u>	15,909
Earned premiums, net of reinsurance			79,327		81,336
Allocated investment return transferred from the non-technical account			4,881		5,338
Interest receivable	7		705		807
			<u> </u>		<u> </u>
Total technical income			84,913		87,481
Claims paid:					
Gross amount		(55,233)		(68,083)	
Reinsurers' share		16,154		31,059	
		<u> </u>	(39,079)	<u> </u>	(37,024)
Change in the provision for claims:					
Gross amount		9,309		(9,092)	
Reinsurers' share		(13,787)		(6,450)	
		<u> </u>	(4,478)	<u> </u>	(15,542)
Claims incurred, net of reinsurance			(43,557)		(52,566)
			<u> </u>		<u> </u>
Balance on the general business technical account before net operating expenses			41,356		34,915
Net operating expenses	4		(10,308)		(7,729)
Profit commission – insurance business	9		1,178		-
			<u> </u>		<u> </u>
Balance on the general business technical account			32,226		27,186
			<u> </u>		<u> </u>

Consolidated profit and loss account: non-technical account
for the year ended 31 December 2003

	Note	2003		2002	
		£000	£000	£000	£000
Balance on the general business technical account			32,226		27,186
Investment income		7,599		6,515	
Net unrealised losses on investments		(2,518)		(1,042)	
Investment expenses and charges		(200)		(135)	
Other income	7	50,783		40,123	
Profit commission – agency business	9	269		-	
Other charges:					
Amortisation of goodwill		(3,906)		(4,285)	
Employee Share Trust	17	(6,900)		(3,103)	
Other	7	(13,248)		(13,347)	
		(24,054)		(20,735)	
Allocated Investment return transferred to the technical account		(4,881)		(5,338)	
			<hr/> 26,998		<hr/> 19,388
Operating profit			59,224		46,574
Interest receivable	7	1,166		1,229	
Interest payable	7	(3,146)		(4,852)	
			<hr/> 57,244		<hr/> 42,951
Profit on ordinary activities before tax	5	57,244		42,951	
Tax on profit on ordinary activities	8	(18,031)		(12,014)	
			<hr/> 39,213		<hr/> 30,937
Profit for the financial year after tax			39,213		30,937
Dividends proposed			-		-
			<hr/> 39,213		<hr/> 30,937
Retained profit for the financial year transferred to reserves	21		39,213		30,937

There were no acquisitions in the financial year, and no operations were discontinued. All income and expenditure therefore relates to continuing operations.

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

Consolidated balance sheet
at 31 December 2003

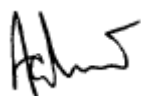
	<i>Note</i>	2003		2002	
		£000	£000	£000	£000
Assets					
Intangible fixed assets	<i>10</i>		62,354		66,260
Investments					
Other financial investments	<i>12</i>		168,925		110,877
Reinsurers' share of technical provisions					
Provision for unearned premiums	<i>19</i>	17,046		-	
Claims outstanding	<i>19</i>	39,620		53,407	
			56,666		53,407
Debtors					
Debtors arising out of direct insurance operations	<i>14</i>	73,611		68,985	
Debtors arising out of reinsurance operations		2,622		-	
Other debtors		5,099		4,743	
			81,332		73,728
Other assets					
Cash at bank and in hand		54,957		50,021	
Cash on short term deposit		15,118		12,975	
Tangible fixed assets	<i>13</i>	5,849		6,681	
			75,924		69,677
Prepayments and accrued income					
Deferred acquisition costs		2,270		1,655	
Other prepayments and accrued income		1,561		1,788	
			3,831		3,443
Total assets			449,032		377,392

Consolidated balance sheet *(continued)*
at 31 December 2003

	<i>Note</i>	2003		<i>2002 (Restated)</i>	
		£000	£000	£000	£000
Liabilities					
Capital and reserves					
Called up share capital	<i>20</i>	25		25	
Share premium account	<i>21</i>	15,746		15,746	
Profit and loss account	<i>21</i>	92,395		53,182	
		<hr/>		<hr/>	
Shareholders' funds attributable to equity interests			108,166		68,953
Technical provisions					
Provision for unearned premiums	<i>19</i>	59,660		30,645	
Claims outstanding	<i>19</i>	115,169		124,478	
		<hr/>		<hr/>	
			174,829		155,123
Creditors – amounts falling due within one year					
Creditors arising out of reinsurance operations		48,867		52,238	
Loans	<i>18</i>	6,423		2,839	
Other creditors including taxation and social Security	<i>15</i>	24,833		15,760	
Accruals and deferred income	<i>16</i>	36,368		25,998	
		<hr/>		<hr/>	
			116,491		96,835
Creditors – amounts falling due after one year					
Loans	<i>18</i>	29,000		45,000	
Other creditors	<i>15</i>	1,741		2,343	
Other accruals and deferred income	<i>16</i>	700		879	
		<hr/>		<hr/>	
			31,441		48,222
Provisions for liabilities and charges	<i>17</i>		18,105		8,259
			<hr/>		<hr/>
Total liabilities			449,032		377,392
			<hr/> <hr/>		<hr/> <hr/>

Refer to note 1 for details of the restated comparative liabilities figures.

These financial statements were approved by the Board of directors on 24 March 2004 and were signed on its behalf by:



A C Probert
Director

Parent company balance sheet
at 31 December 2003

	<i>Note</i>	2003		2002	
		£000	£000	£000	£000
Fixed assets					
Investments	<i>11</i>		101,804		92,302
Current assets					
Debtors (amounts owed by subsidiaries)		21,555		23,075	
Cash at bank and in hand		5,090		6,931	
		26,645		30,006	
Creditors: amounts falling due within one year:					
Loans	<i>18</i>	(6,423)		(2,839)	
Other creditors	<i>15</i>	(2,060)		(459)	
Accruals and deferred income	<i>16</i>	(252)		(240)	
		(8,735)		(3,538)	
Net current assets			17,910		26,468
Total assets less current liabilities			119,714		118,770
Creditors: amounts falling due after one year:					
Loans	<i>18</i>	(29,000)		(45,000)	
Accruals and deferred income	<i>16</i>	-		-	
			(29,000)		(45,000)
Net assets			90,714		73,770
Capital and reserves					
Called up share capital	<i>20</i>		25		25
Share premium account	<i>21</i>		15,746		15,746
Profit and loss account	<i>21</i>		74,943		57,999
			90,714		73,770

These financial statements were approved by the Board of directors on 24 March 2004 and were signed on its behalf by:



A C Probert
Director

Group cash flow statement
for the year ended 31 December 2003

	<i>Note</i>	2003		2002	
		£000	£000	£000	£000
Net cash inflow from operating activities	24		96,229		78,292
Servicing of finance					
Net interest paid			(2,954)		(8,505)
Taxation					
Corporation tax paid			(10,428)		(10,079)
Capital expenditure					
Purchases of fixed assets		(2,921)		(2,808)	
Sales of fixed assets		20		180	
Net purchases of fixed assets		<hr/>	(2,901)	<hr/>	(2,628)
Acquisitions			-		-
Equity dividends paid			-		-
Financing					
Issues of ordinary shares		-		15,748	
Drawdown of new loans		-		60,000	
Repayment of loan notes and other loans		(12,333)		(68,757)	
Net movement in finance lease capital		32		(586)	
Deferred consideration		-		(15,700)	
		<hr/>	(12,301)	<hr/>	(9,295)
			<hr/> 67,645 <hr/>		<hr/> 47,785 <hr/>
Cash flows were invested as follows:					
Increase in cash holdings			7,079		29,778
Debt securities and other fixed income securities			60,566		18,007
Net investment of cash flows			<hr/> 67,645 <hr/>		<hr/> 47,785 <hr/>

Notes

(forming part of the financial statements)

1. Basis of preparation

The Group financial statements, which consolidate the financial statements of the Company and its wholly owned subsidiary undertakings, have been prepared in accordance with the provisions of Section 255 of, and Schedule 9A to, the Companies Act 1985. The balance sheet of the parent Company is prepared in accordance with the provisions of Section 226 of, and Schedule 4 to, the Companies Act 1985. The financial statements have also been prepared in accordance with applicable accounting standards and under the historical cost accounting rules modified to include the revaluation of investments, and comply with the Statement of Recommended Practice ("SORP") issued by the Association of British Insurers as revised in November 2003.

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the parent Company is not presented.

The liabilities section of the balance sheet for the 2002 financial year end has been restated. This is as a result of the reclassification of the ESOT provision from accruals due after one year into provisions for liabilities and charges. The amount reallocated was £4,839,000. Refer to note 17 for further detail.

2. Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material to the group's financial statements.

Basis of accounting for general insurance business

General business is accounted for on an annual basis.

Premiums

General business written premiums comprise the premiums on contracts entered into during the year, which incept during the current financial year. Premiums are disclosed gross of commission payable to intermediaries and exclude taxes and levies based on premiums.

The provision for unearned premiums comprises the proportion of gross premiums written which is estimated to be earned in the following or subsequent financial years, computed separately for each insurance contract using the daily pro rata method, adjusted if necessary to reflect any variation in the incidence of risk during the period covered by the contract.

Claims

Claims incurred in respect of general business consist of claims and claims handling expenses paid during the period together with the movement in the provision of outstanding claims.

Claims outstanding comprise provisions for the estimated cost of settling all claims incurred but unpaid at the balance sheet date whether reported or not. Anticipated reinsurance recoveries are disclosed separately as assets.

Whilst the directors consider that the gross provisions for claims and the related reinsurance recoveries are fairly stated on the basis of the information currently available to them, the ultimate liability will vary as a result of subsequent information and events and may result in significant adjustments to the amounts provided. Adjustments to the amounts of claims provisions established in prior years are reflected in the financial statements for the period in which the adjustments are made, and disclosed separately if material. The methods used, and the estimates made, are reviewed regularly.

Notes (continued)

2. Accounting policies (continued)

Acquisition costs

Acquisition costs comprise all direct and indirect costs arising from the conclusion of insurance contracts. Deferred acquisition costs represent the proportion of acquisition costs incurred that corresponds to the unearned premiums provision.

Guarantee fund levies

Provision is made at the balance sheet date for levies declared by the Financial Services Compensation Scheme and Motor Insurers' Bureau before completion of the financial statements. Provision is also made if it is more likely than not that a levy will be raised based on premium income which has already been recognised in the financial statements.

Fixed assets and depreciation

Fixed assets are stated at cost less depreciation. Depreciation is provided to write off the cost less estimated residual value of tangible assets by equal instalments over their estimated useful economic lives as follows:

Motor vehicles	-	4 years
Fixtures, fittings and equipment	-	4 years
Computer equipment and software	-	2 to 4 years
Improvement to short lease-hold properties	-	4 years

Profit commission

Under some of the co-insurance and reinsurance contracts the Group is party to, profit commission may be earned on a particular year of account, which is usually subject to performance criteria such as loss ratios and expense ratios. The commission is dependent on the ultimate outcome of any year, and commission received may be clawed back by the third party if the criteria under which the payment was made deteriorate.

The income is allocated to the technical account (under the caption "Profit commission – insurance business") if the commission is earned by one of the Group's regulated insurance companies, or alternatively to the non-technical account (under the caption "Profit commission – agency business") if earned by other companies.

Profit commission is recognised in the profit and loss account when the right to consideration is achieved, and is capable of reliable measurement.

Leases

The rental costs relating to operating leases are charged to the profit and loss account on a straight-line basis over the life of the lease.

Assets acquired under finance leases or hire purchase contracts are included in tangible fixed assets at an amount equal to the cost that would have been payable on purchase and are depreciated in the same manner as equivalent owned assets. Finance lease and hire purchase obligations are included in creditors, and the finance costs are spread over the periods of the agreements based on the net amount outstanding.

Notes *(continued)*

2. Accounting policies *(continued)*

Ancillary income, commission and other income

Ancillary income is either credited to the profit and loss account on inception of the underlying motor policy, or the income is deferred and spread over the life of the policy. A provision is made for expected cancellations where the customer may be entitled to a refund of ancillary amounts charged.

Instalment income is credited to the profit and loss account in line with the earning of the motor premium to which the instalment income relates. Provision is made for expected cancellations.

Commission from broking activities is credited to the profit and loss account on the sale of the underlying insurance policy.

Investments

Listed investments are stated at mid-market value on the balance sheet date, or on the last stock exchange trading day before the balance sheet date.

Investments in subsidiary undertakings are valued at cost less any provision for impairment in value.

Investment return

Interest receivable is accounted for on an accruals basis. Dividend income, grossed up where appropriate by the imputed tax credit, is recognised when the related investment goes "ex-dividend".

Realised gains or losses represent the difference between net sales proceeds and purchase price or in the case of investments valued at amortised cost, the latest carrying value.

Unrealised gains and losses on investments represent the difference between the current value of investments at the balance sheet date and their purchase price. The movement in unrealised investment gains/losses includes an adjustment for previously recognised unrealised gains/losses on investments disposed of in the accounting period.

Investment return (including realised and the movement in unrealised investment gains and losses) on investments attributable to the general business and associated shareholders' funds is reported in the non-technical account.

An allocation is made from the non-technical account to the general business technical account of the longer-term investment return on investments supporting the general insurance technical provisions and related shareholders' funds.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Deferred tax assets are recognised to the extent that they are regarded as recoverable. They are regarded as recoverable to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Goodwill

Goodwill arising on acquisitions, being the difference between the fair value of the purchase consideration and the fair value of net assets acquired, is capitalised in the balance sheet and amortised on a straight line basis over its estimated useful life. The useful life of each acquisition is determined at the time of acquisition, and reviewed annually to ensure the life assigned remains appropriate.

Notes *(continued)*

3. Analysis of underwriting results

All insurance business written during both financial years is direct private motor insurance written in the United Kingdom. During 2003, the Group's share of the business was underwritten by Admiral Insurance (Gibraltar) Limited ("AIGL") and Admiral Insurance Company Limited ("AICL"). During 2002, the Group share was all underwritten by Syndicate 2004. Refer to page 10 for further detail on Group underwriting, co-insurance and reinsurance arrangements.

Year ended 31 December	2003	2002
	£000	£000
Motor insurance - total premiums written	371,600	333,000
Co-insurer share of total premiums	(241,540)	(266,400)
	<hr/>	<hr/>
Group share of total premiums	130,060	66,600
Adjustment for prior year cancellation premium	(209)	2,489
	<hr/>	<hr/>
Gross premium written per technical account	129,851	69,089
	<hr/> <hr/>	<hr/> <hr/>

AIGL, which underwrites motor insurance in Gibraltar had gross written premium of £118,443,000 during 2003 (2002: £nil), profit before taxation of £4,851,000 (2002: £9,000) and net assets of £19,862,000 (2002: £13,009,000).

4. Net operating expenses – Technical account

	2003	2002
	£000	£000
Administrative expenses incurred on motor business co-insured	37,002	42,657
Expenses recovered from co-insurers	(37,002)	(42,657)
Gross acquisition costs incurred	6,654	5,121
Movement in deferred acquisition costs	(1,402)	3,977
Gross expense and reinsurance commissions receivable	(3,710)	-
Non-recurring expense commission receivable	-	(6,915)
Movement in the deferred element of gross reinsurance commission receivable	787	(4,364)
Other administrative expenses	7,786	7,793
Lloyd's charges	193	2,117
	<hr/>	<hr/>
	10,308	7,729
	<hr/> <hr/>	<hr/> <hr/>
Staff profit share charge included in administrative expenses above	1,932	555
	<hr/> <hr/>	<hr/> <hr/>

Under the terms of the group's co-insurance arrangements, a proportion of the Group's total expenses are incurred on behalf of the co-insurers, and are reimbursed. The note above discloses these expenses and the associated recovery, and also sets out the share of the total expenses retained by AGL during the course of underwriting its own business.

Notes *(continued)*

5. Profit on ordinary activities before tax

Operating profit is stated after charging the following items:

	2003	2002
	£000	£000
Financing & refinancing costs:		
Cost of Initial financing	-	607
2002 refinancing (see note 18 for details of borrowing)	-	1,515
Costs relating to new share issues	-	50
Depreciation charge:		
Owned assets	1,283	1,372
Leased assets	1,575	1,669
Operating lease rentals:		
Machinery and equipment	-	-
Buildings	1,444	1,326
Auditor's remuneration:		
Statutory audit fees (including Company £6,000 (2002: £6,000))	106	108
Other audit fees (including Company £nil (2002: £nil))	11	3
Other services: Refinancing & new share issues	-	341
Other (including Company £23,000 (2002: £13,000))	76	60
Loss on disposal of tangible fixed assets	875	166
	<hr/> <hr/>	<hr/> <hr/>

6. Employees

Staff costs (including directors)

	2003	2002
	£000	£000
Salaries	23,651	22,069
Social security	2,158	1,844
Other pension costs	308	250
Staff profit share scheme	1,932	555
Employee share trust charge (see note 17)	6,900	3,103
	<hr/> <hr/>	<hr/> <hr/>
	34,949	27,821

Pension costs relate to contributions made by the Group into a number of Group Personal Pension Plans - matching schemes (with three different providers) open to all employees, except for directors, and subject to a maximum annual contribution of £3,000 per employee.

Number of staff (including directors)

	Average for the year	
	2003	2002
	Number	Number
Direct customer contact staff	1,078	1,140
Support staff	284	254
	<hr/> <hr/>	<hr/> <hr/>
	1,362	1,394

Notes *(continued)*

6. Employees *(continued)*

Directors' emoluments

	2003	2002
	£000	£000
Emoluments (including Company £113,000; 2002: £65,000)	1,027	827
	<hr style="border-top: 3px double #000;"/>	<hr style="border-top: 3px double #000;"/>
Emoluments of the highest paid director (including Company £nil; 2002: £nil)	272	312
	<hr style="border-top: 3px double #000;"/>	<hr style="border-top: 3px double #000;"/>
No contributions were made into pension schemes on behalf of directors.		

7. Net interest, other income and other charges

	2003	2002
	£000	£000
Bank and other interest receivable		
Allocated to technical account	705	807
Allocated to non-technical account	1,166	1,229
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	1,871	2,036
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Interest payable		
Commercial loan interest payable	2,142	820
Loan note interest payable	-	2,838
Finance lease interest	270	304
Letter of credit charges	734	890
	<hr style="border-top: 1px solid #000;"/>	<hr style="border-top: 1px solid #000;"/>
	3,146	4,852
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Other income		
Revenue from ancillary sales	44,687	34,759
Commissions from broker operations	3,767	3,350
Instalment income	1,257	1,836
Other	1,072	178
	<hr style="border-top: 1px solid #000;"/>	<hr style="border-top: 1px solid #000;"/>
	50,783	40,123
	<hr style="border-top: 3px double #000;"/>	<hr style="border-top: 3px double #000;"/>
Other charges		
Costs associated with ancillary sales	8,831	7,442
Broker operations operating costs	2,096	2,257
Other costs	2,321	3,648
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	13,248	13,347
	<hr style="border-top: 3px double #000;"/>	<hr style="border-top: 3px double #000;"/>

Notes *(continued)*

8. Taxation on profit on ordinary activities

	2003	2002
	£000	£000
UK corporation tax		
Current year at 30% (2002: 30%)	15,192	9,123
Over provision relating to prior years	(107)	(529)
Deferred taxation movement (note 17)	2,946	3,420
	18,031	12,014
	18,031	12,014

Factors affecting tax charge for the period:

	2003	2002
	£000	£000
Profits on ordinary activities before taxation	57,244	42,951
	57,244	42,951
Corporation tax thereon at 30%	17,173	12,885
Syndicate profits taxed on Lloyd's basis (see note below)	(5,251)	(4,997)
Expenses and provisions not deductible for tax purposes	3,291	1,350
Other timing differences	(12)	(104)
Impact of using lower tax rate	(9)	(11)
	15,192	9,123
	15,192	9,123

Lloyd's Syndicate taxation rules

Under Syndicate taxation rules, the liability for a year of account is only agreed after the year is closed, typically two years after the end of the period, when the taxation computations are submitted by the Syndicate's Managing Agent. Only one of Syndicate 2004's years of account (that being 2002) remains open.

The results of the Syndicate, however, are converted in line with appropriate accounting standards and included in the consolidated results of the Group (by way of their inclusion in the Admiral Syndicate Limited financial statements). The effect of this is to reduce the current year corporation tax charge, but increase the deferred taxation liability.

9. Profit commission

	2003	2002
	£000	£000
Profit commission receivable:		
Allocated to technical account	1,178	-
Allocated to non-technical account	269	-
	1,447	-
	1,447	-

Profit commission is allocated to either the technical or non-technical account, depending on whether it is earned from underwriting or agency activities. Where a regulated insurer (being AICL or AIGL) earns the income, it is credited to the technical account. All other profit commission is credited to the non-technical account.

Notes *(continued)*

10. Intangible assets – goodwill

	Group £000
Cost	
At 31 December 2002 and 2003	78,879
<hr/>	
Amortisation	
At 1 January 2003	12,619
Charged in the year	3,906
At 31 December 2003	16,525
<hr/>	
Net book amount	
At 31 December 2003	62,354
<hr/>	
At 31 December 2002	66,260
<hr/>	

The goodwill above is being amortised over an estimated useful economic life of 20 years.

11. Investments in group undertakings

	2003 Company Cost £000	2002 Company Cost £000
Shares in group undertakings	101,804	92,302
<hr/>		<hr/>

The movement in the cost figures above is made up of two transactions that occurred during 2003. These were: 1) Capitalisation of Admiral Insurance Company Limited - £7,500,000; and 2) Further capitalisation (to fund growth in premium income) of Admiral Insurance (Gibraltar) Limited - £2,002,000.

The Company's principal subsidiaries (all of which are 100% directly owned) are as follows:

	Country of incorporation	Class of shares held	Principal activity
Admiral Insurance Services Limited	England and Wales	Ordinary	Service company
Admiral Insurance Company Limited	England and Wales	Ordinary	Insurance company
Admiral Insurance (Gibraltar) Limited	Gibraltar	Ordinary	Insurance company
Admiral Syndicate Limited	England and Wales	Ordinary	Lloyd's corporate capital vehicle
Admiral Syndicate Management Limited	England and Wales	Ordinary	Lloyd's managing agency
Able Insurance Services Limited	England and Wales	Ordinary	Intermediary
Inspop.com Limited	England and Wales	Ordinary	Internet services

Notes (continued)

12. Other financial investments

Group	Historic cost at 31 December 2003 £000	Market value at 31 December 2003 £000	Historic cost at 31 December 2002 £000	Market value at 31 December 2002 £000
Debt securities and other fixed income securities	146,979	144,461	91,141	90,099
Deposits with credit institutions	24,464	24,464	20,778	20,778
	<u>171,443</u>	<u>168,925</u>	<u>111,919</u>	<u>110,877</u>

13. Tangible fixed assets

Group	Improvements to short leasehold buildings £000	Computer equipment and software £000	Office equipment £000	Furniture and fittings £000	Motor vehicles £000	Total £000
<i>Cost</i>						
At 1 January 2003	1,602	15,000	2,751	1,563	10	20,926
Additions	56	2,795	34	20	16	2,921
Disposals	-	(3,934)	-	-	(26)	(3,960)
At 31 December 2003	<u>1,658</u>	<u>13,861</u>	<u>2,785</u>	<u>1,583</u>	<u>-</u>	<u>19,887</u>
<i>Depreciation</i>						
At 1 January 2003	1,209	9,979	1,732	1,322	3	14,245
Charge for the year	196	2,103	395	161	3	2,858
Disposals	-	(3,059)	-	-	(6)	(3,065)
At 31 December 2003	<u>1,405</u>	<u>9,023</u>	<u>2,127</u>	<u>1,483</u>	<u>-</u>	<u>14,038</u>
<i>Net book amount</i>						
At 31 December 2003	<u>253</u>	<u>4,838</u>	<u>658</u>	<u>100</u>	<u>-</u>	<u>5,849</u>
<i>At 31 December 2002</i>	<u>393</u>	<u>5,021</u>	<u>1,019</u>	<u>241</u>	<u>7</u>	<u>6,681</u>

Net book amounts for the group include the following amounts related to leased assets:

	2003 £000	2002 £000
Computer equipment and software	4,187	3,438
Office equipment	125	140
Furniture and fittings	-	64
	<u>4,312</u>	<u>3,642</u>

Notes *(continued)*

14. Debtors arising out of direct insurance operations

	Company 2003 £000	Group 2003 £000	Company 2002 £000	Group 2002 £000
Amounts owed by policyholders	-	72,678	-	68,234
Commissions due	-	933	-	751
	<hr/>	<hr/>	<hr/>	<hr/>
	-	73,611	-	68,985
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

15. Other creditors including taxation and social security

	Company 2003 £000	Group 2003 £000	Company 2002 £000	Group 2002 £000
Amounts falling due within one year:				
Corporation tax payable	1,455	8,717	-	4,060
Other tax and social security	-	2,570	-	1,148
Finance leases	-	2,052	-	1,418
Other creditors	-	11,494	459	9,134
Amounts owed to subsidiary companies	605	-	-	-
	<hr/>	<hr/>	<hr/>	<hr/>
	2,060	24,833	459	15,760
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

	Company 2003 £000	Group 2003 £000	Company 2002 £000	Group 2002 £000
Amounts falling due after one year:				
Finance leases	-	1,741	-	2,343
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

16. Accruals and deferred income

	Company 2003 £000	Group 2003 £000	Company 2002 £000	Group 2002 £000
Amounts falling due within one year:				
Premiums receivable in advance of policy inception	-	16,495	-	11,417
Claims handling expenses	-	5,289	-	4,267
Motor Insurers' Bureau levy	-	5,797	-	6,517
Deferred income	-	5,190	-	3,472
Other	252	3,597	240	325
	<hr/>	<hr/>	<hr/>	<hr/>
	252	36,368	240	25,998
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

Notes *(continued)*

16. Accruals and deferred income *(continued)*

	Company 2003 £000	Group 2003 £000	Company 2002 £000	Group 2002 £000
Amounts falling due after one year:				
Claims handling expenses	-	700	-	759
Deferred income	-	-	-	120
	<hr/>	<hr/>	<hr/>	<hr/>
	-	700	-	879
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

17. Provisions for liabilities and charges

Group

	Deferred taxation¹ £000	ESOT² £000	Total £000
Balance at 1 January 2003	3,420	4,839	8,259
Movement in period, being charge to profit and loss account	2,946	6,900	9,846
	<hr/>	<hr/>	<hr/>
Balance at 31 December 2003	6,366	11,739	18,105
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

1 – Deferred tax

The net balance provided at the end of the current year is made up of a gross deferred tax liability of £8,878,000 relating to the tax treatment of Lloyd's Syndicates (refer to note 8), and a deferred tax asset of £2,512,000 in respect of other timing differences.

At the year-end, there was an unprovided deferred tax asset of £1,113,000 (2002: £1,222,000) relating to losses carried forward.

There was neither a deferred tax asset nor a liability provided in the Company accounts. There was an unprovided asset of £171,000 (2002: £176,000) relating to carried forward losses at the year-end.

2 – Employee Share Ownership Trust ("ESOT")

During 2000 the Group established an ESOT, under which 14,706 C ordinary shares are to be made available to a trust in which the Group's employees are allocated units. Shares or the proceeds of their sale will be issued to Group employees on the earlier of a sale or flotation of the Company's shares. Awards for participation in the scheme are made annually by the trustees of the Group's Employee Share Trust.

The Group makes provision for the costs of making the shares available under the terms of the trust, and is accruing the cost of doing this over the period leading up to the date at which the directors estimate the awards will be made. Details of the charge for the current and preceding years are shown in note 6.

Notes (continued)

18. Loans

The Company's debt consists of a facility negotiated in 2002 with Lloyds TSB and Bank of Scotland. This consists of a £40m term loan (paid down during the year to £35m), along with a £10m revolving credit facility. The term loan is to be repaid according to a set repayment schedule over six years from October 2002. As at 31 December 2003 the £10m revolving credit facility was not drawn down.

Interest is charged on amounts drawn down under the facility based on three elements:

- a) LIBOR
- b) A margin – as set out in the facility agreement, varying between 1.25% and 2.25%
- c) A “mandatory costs” contribution – currently around 0.01%

Accrued interest is paid off at the end of quarterly interest periods. Security granted in respect of the facility is in the form of fixed and floating charges over most Group assets (excluding assets subject to regulatory restriction) and charges over the shares in some subsidiary companies.

Amounts outstanding (including accrued interest) at 31 December were as follows:

Repayable:	2003	2002
	£000	£000
Within one year	6,423	2,839
Two to five years	29,000	28,000
Greater than five years	-	17,000
	<hr/>	<hr/>
	35,423	47,839
	<hr/> <hr/>	<hr/> <hr/>

19. Technical provisions & estimation techniques

2003	Gross	Reinsurance	Net
	£000	£000	£000
Claims outstanding	115,169	39,620	75,549
Unearned premiums	59,660	17,046	42,614
	<hr/>	<hr/>	<hr/>
At end of year	174,829	56,666	118,163
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
2002	Gross	Reinsurance	Net
	£000	£000	£000
Claims outstanding	124,478	53,407	71,071
Unearned premiums	30,645	-	30,645
	<hr/>	<hr/>	<hr/>
At end of year	155,123	53,407	101,716
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

Notes *(continued)*

19. Technical provisions & estimation techniques *(continued)*

Analysis of movements in claims reserves:

2003	Gross £000	Reinsurance £000	Net £000
Claims reserve brought forward	124,478	53,407	71,071
Provision movement – current year	19,894	(673)	20,567
Releases of prior year reserves	(29,203)	(13,114)	(16,089)
	<hr/>	<hr/>	<hr/>
Claims reserve carried forward	<u>115,169</u>	<u>39,620</u>	<u>75,549</u>
	<hr/>	<hr/>	<hr/>
 2002	 Gross £000	 Reinsurance £000	 Net £000
Claims reserve brought forward	115,386	59,857	55,529
Provision movement – current year	26,448	2,228	24,220
Releases of prior year reserves	(17,356)	(8,678)	(8,678)
	<hr/>	<hr/>	<hr/>
Claims reserve carried forward	<u>124,478</u>	<u>53,407</u>	<u>71,071</u>
	<hr/>	<hr/>	<hr/>

Estimation techniques used in calculation of claims reserves

Estimation techniques are used in the calculation of the technical provision for claims outstanding, which represents a projection of the ultimate cost of settling claims that have occurred prior to the end of 2003 and remain unsettled at the end 2003.

The key area where these techniques are used relates to the ultimate cost of reported claims. A secondary area relates to the emergence of claims that occurred prior to the end of 2003, but had not been reported at the year-end.

The estimates of the ultimate cost of reported claims are based on the accurate setting of claim reserves on a case by case basis, for all but the simplest of claims.

The sum of these reserves are compared with projected ultimate costs using a variety of different projection techniques (including incurred and paid chain ladder and an average cost of claim approach) to allow an actuarial assessment of their likely accuracy and to include allowance for unreported claims.

The most significant sensitivity in the use of the projection techniques arises from any future step change in claims costs, which would cause future claim cost inflation to deviate from historic trends. This is most likely to arise from a change in the regulatory or judicial regime that leads to an increase in awards or legal costs for bodily injury claims that is significantly above or below the historical trend.

The claims provisions are subject to annual independent review by external actuaries.

Notes *(continued)*

20. Called up share capital

	2003	2002
	£000	£000
Authorised		
132,488 (2002: 5,970,164) A ordinary shares of 10p each	13	597
60,176 (2002: 2,000,000) B ordinary shares of 10p each	6	200
27,500 (2002: 2,000,000) C ordinary shares of 10p each	3	200
29,836 D ordinary shares of 10p each	3	3
20,164 E ordinary shares of 10p each	2	2
	27	1,002
	2003	2002
	£000	£000
Issued, called up and fully paid		
132,488 A ordinary shares of 10p each	13	13
60,176 B ordinary shares of 10p each	6	6
12,042 C ordinary shares of 10p each	1	1
29,836 D ordinary shares of 10p each	3	3
20,164 E ordinary shares of 10p each	2	2
	25	25
	2003	2002
	£000	£000

Rights of shares

In the event of a winding up of the Company or other return of capital, the assets of the Company available for distribution to shareholders will be distributed amongst the holders of the ordinary shares *pari passu*, as if they were all shares of the same class. This is provided that, after the distribution of the first £500m of such balance, the Deferred Shares (as defined in the Company's Articles of Association) (if any) shall be entitled to receive an amount equal to the nominal value of such Deferred Shares. Any payment made to the holders of shares of a particular class shall be made in proportion to the numbers of shares of the relevant class held by each of them.

Immediately prior to a Sale or Listing (a "Conversion Date"), 61,552 A ordinary shares, 13,861 D ordinary shares and 9,368 E ordinary shares shall convert into the same number of fully paid Deferred Shares ("The Conversion") which have limited rights.

21. Movements on shareholders funds

	Share Capital	Share Premium	Profit and loss account	Total
Group	£'000	£'000	£'000	£'000
At 1 January 2003	25	15,746	53,182	68,953
Retained profit for the financial year	-	-	39,213	39,213
	25	15,746	92,395	108,166
	2003	2003	2003	2003
	£'000	£'000	£'000	£'000

Notes *(continued)*

21. Movements on shareholders funds *(continued)*

Company	Share Capital £'000	Share Premium £'000	Profit and loss account £'000	Total £'000
At 1 January 2003	25	15,746	57,999	73,770
Retained profit for the financial year	-	-	16,944	16,944
At 31 December 2003	25	15,746	74,943	90,714

The Company made a profit after tax of £16,944,000 in the year (2002: £21,210,000).

22. Financial Commitments

Annual commitments of the group under non-cancellable operating leases are as follows:

	2003		2002	
	Land and buildings £'000	Other £'000	Land and buildings £'000	Other £'000
Operating leases which expire:				
Within one year	16	-	-	-
In the second to fifth years inclusive	460	-	-	-
Over five years	1,147	-	1,506	-
	1,623	-	1,506	-

At the year-end, the Group had contracted to spend approximately £167,000 on fixed assets during 2004 (2002: £330,000 over 2003 and 2004). The Company itself does not hold tangible fixed assets, and was not committed to any expenditure after 31 December 2003.

23. Contingent liabilities

The Group had no contingent liabilities at the year-end, other than those arising out of insurance contracts, and other agreements entered into in the normal course of business.

Notes *(continued)*

24. Cash flow statement

Reconciliation of operating profit to net cash inflow from operating activities

	2003	2002
	£000	£000
Operating profit	59,224	46,574
Add back:		
Depreciation charge	2,858	3,041
Amortisation charge	3,906	4,285
Unrealised losses on investments	2,518	1,042
ESOT charge	6,900	3,103
Loss on disposal of tangible fixed assets	875	166
Change in gross technical provisions	19,706	(53,372)
Change in reinsurers' share of technical provisions	(3,259)	53,005
Change in debtors and prepayments	(7,992)	15,593
Change in creditors and accruals - excluding tax and social security	10,071	7,030
Change in tax and social security creditor	1,422	(2,175)
	96,229	78,292
Net cash inflow from operating activities	96,229	78,292

25. Related Party Transactions

There were no related party transactions occurring during 2003 that require disclosure.

26. Post balance sheet event

On 28th January 2004, the directors proposed a special dividend of £55.67 per share, which was paid on 27th February.

Consolidated Financial Summary

Profit and Loss Account

<i>Notes</i>	2003 £000	2002 £000	2001 £000	2000 £000
Total Written Premium – 100% level	371,600	333,000	284,415	232,000
Gross Written Premium – Group Share	129,851	69,089	198,950	151,074
Net Earned Premium	79,327	81,336	84,135	40,392
Technical account balance	32,226	27,186	11,330	(832)
Other income	50,783	40,123	35,432	29,929
Operating profit	59,224	46,574	31,266	14,414
add: Interest receivable	1,166	1,229	1,065	797
Goodwill amortisation	3,906	4,285	4,358	3,976
ESOT charge	6,900	3,103	1,500	236
Group core profits	71,196	55,191	38,189	19,423

Balance Sheet

	2003 £000	2002 £000	2001 £000	2000 £000
Total assets	449,032	377,392	405,512	299,475
Shareholders' funds	108,166	68,953	22,268	3,932

The above presents a four year history from 2000, which was the first year of trading for the Group and the first year for which Admiral Group Limited prepared accounts.

Notes:

- 1: Due to changes in the co-insurance and reinsurance arrangements the gross share of business written increased from 20% to 35% from 2002 to 2003 whilst the net share retained also increased from 20% to 25%. Refer to page 10 for further detail.