IMAGINE

Syndicate 2525

Annual Report 2006

Annual accounting contents

Closing year of account contents

Annual Report and Accounts for the year ended 31 December 2006

Managing agent: Directors and administration

Managing agent

Imagine Syndicate Management Limited

Directors

I J Bremner (Managing Director)
G E Morrison (Chairman)
M P Daly
R J Forness
L J Gibbins
M A Petzold
M W Petzold*
A T West*

*Non-executive directors

Company secretary

Sarah Pattni

Managing agent's registered office

4th Floor
70 Gracechurch Street
London EC3V 0XL

Managing agent's registered number

03304600

Syndicate:

Active underwriter

D L Pratt

Bankers

Citibank N.A
The Royal Bank of Scotland

Investment managers

Crédit Agricole Asset Management (UK) Limited

Registered auditors

KPMG Audit Plc, London

Report of the directors of the managing agent at 31 December 2006

The managing agent presents its report for the year ended 31 December 2006.

Fair review

Principal activity and review of the business

Syndicate 2525 writes employers' and public liability insurance primarily in the United Kingdom.

Results

The result for calendar year 2006 is a profit before other recognised gains and losses of £11.29m (2005: profit of £12.98m). Profits or losses will continue to be distributed or collected by reference to the results of individual underwriting years. The contribution of the three open underwriting years to the calendar year profit is stated below:

Year	**Profit/(loss)** **£m**
2004	9.35
2005	3.38
2006	(1.42)
Calendar year 2006	11.29

2004 year in 2006

Profit for the year	£9.35m

The 2004 year has outperformed our expectations with the closing year profit (discussed in full in the 2004 closing year report) ahead of the forecast at 31 December 2005. We steadily improved our forecast profit for the closing year throughout 2006 and are pleased that the final result is at the top end of the forecast range. The contribution of the 2004 year to the result for 2006 of £9.35m is largely the product of the continued improvement in ultimate loss ratios during the year.

2005 year in 2006

Profit for the year	£3.38m

The 2005 year was the first full year that a revised approach to claims reserving was implemented. This more prudent approach resulted in an earlier development of reserves and has resulted in the year recording a lower profit after 24 months than the 2004 year of account at the same stage. It has continued to perform well in 2006, with the level of claims incurred being such that ultimate loss ratios have again improved since 31 December 2005.

2006 year in 2006

Loss for the year	£1.42m

The prudent reserving methodology adopted in 2005 continued to be applied in 2006. This factor combined with the continuing pressure on reserves resulted in the year reporting a loss in line with that of 2005 as reported last year.

Future developments

The syndicate's capital aspirations for 2007 were met with a capacity of £42m. The market however, is competitive and this may have some impact on our ability to achieve premium income forecasts for the 2007 account. Despite this we remain satisfied that with very stringent risk selection, rates for our targeted business segments remain adequate to achieve a profit commensurate with business plan objectives.

Principal risks and uncertainties

Key to the performance of the syndicate is the adequacy of its reserves. As a longer tail liability class business, development of claims over the 7 to 10 year tail will have a material impact on its profitability. This will be impacted on by both claims development volatility and changing trends in claims inflation rates.

Similarly, the stability of the prevalent interest rates may affect the ongoing results of the syndicate, as the interest rate environment will influence both pricing and reserving.

Equally important to the syndicate is the ability to successfully manage its own risk exposure through the outwards cession of risk to reinsurers. Careful modelling and assessment of underlying risks borne inform the purchase of the syndicate's reinsurance programme; it is key that this programme mitigates the syndicate's gross exposure in the manner expected.

The rating environment is also a significant area of future uncertainty. Rates continue to soften from their peaks a few years ago and whilst one can project the end of this phase of the insurance cycle

Report of the directors of the managing agent at 31 December 2006

Principal risks and uncertainties *(continued)*

based on historical precedent there can be no certainty over when rates will start to harden again.

It is expected that this business will be subject to the vagaries of the market cycle and must strive always to deal effectively with the problems that this presents. Managing the expectations of clients and brokers within the prevalent softer market conditions, whilst maintaining the underwriting standards necessary to produce an adequate return for capital providers, remains the syndicate's biggest challenge.

Finally, as a business dependent on human capital, the syndicate is exposed to the risk of loss of key staff, especially in the underwriting teams. Loss of key individuals could have a material impact on the syndicate's future profitability. To mitigate this, syndicate management endeavours to structure appropriate incentivisation packages to align underwriters' interests and retain staff loyalty.

Key performance indicators

The principal financial Key Performance Indicators (KPI) relevant to the syndicate are:

Gross Written Premium – this has decreased to £45.7m from £53.1m in 2005
Net underwriting income – this has decreased in 2006 to £19.0m (2005: £23.2m)
Investment return – this has seen a decrease to 3.9% (2005: 4.1%)
Year of account return on capacity – 2004 account 20.7% (2003 account: 31.3%)

Given the nature of the syndicate's business, the main regulatory financial KPI considered relevant is:

Capacity utilisation – this has been 80.3% for 2006 (2005: 95.3%)

Active underwriter

The active underwriter during 2006 was David Pratt.

Directors and their participations

I J Bremner (Managing Director)
R J Wallace (Chairman – resigned 15/03/2007)
M P Daly
L J Gibbins (appointed 31/01/2007)
R J Forness
M A Petzold
M W Petzold*
A T West*
G E A Morrison (appointed 08/08/2006, assumed Chairman with effect from 16/03/2007)
R R Dally (resigned 30/01/2007)

*Non-executive directors

Corporate governance

Imagine is managed by a board of directors consisting of a management team of six executives, including an executive chairman and two non-executives. The board meets regularly throughout the year and a number of matters are specifically reserved for its consideration and approval. In addition the board delegates a number of items to various sub-committees, that have clearly defined terms of reference.

Investment policy and performance

Imagine operates an investment management committee, which is responsible for recommending to the agency board the longer term strategy and investment policy of the syndicate, and the appointment of investment managers of the syndicate's funds. The committee is also responsible for monitoring the performance of investment managers and ensuring that all relevant Lloyd's and other regulatory requirements are met.

Credit Agricole Asset Management (UK) were appointed as investment managers to the syndicate with effect from 1 January 2001 and have continued in office since.

Investment policy

The investment policy is to invest in a manner calculated to maximise return within agreed restraints and in line with policies approved by the agency. In consideration of this policy, portfolios are predominantly invested in short-term, high quality fixed income securities. The investment managers have been instructed to invest for the highest total

Report of the directors of the managing agent at 31 December 2006

Investment policy *(continued)*

return consistent with maintaining adequate liquidity and security, and their performance is measured against benchmarks defined by the investment committee. The investment managers have discretion to invest in private sector securities for a limited proportion of the portfolio and within diversity limits for individual credits. Limiting the target duration of the overall portfolio controls the exposure of the investments to adverse price conditions. The committee is also responsible for ensuring that all relevant Lloyd's and other regulatory requirements are met.

Review of calendar year 2006

During the year the portfolio the overall fund size for syndicate 2525 decreased to £110m, from £119m at 31 December 2005, due to some negative cash flows and a decrease in the sterling value of the US dollar and Euro portfolios due to sterling's appreciation. The performance of the portfolio as a whole was a little lower than in 2005 with an average return of 3.9% (2005: 4.1%).

During the year sterling investments yielded returns above those derived from cash and 1-3 year bonds as the syndicate maintained a conservative portfolio with short duration throughout the year. During the first quarter yields increased as expectations of an interest rate cut receded. The duration of the portfolio was cut in early January and then the short was reduced as yields rose later in the quarter. During the second quarter market yields moved higher to the extent that the central expectation was for the next move in U.K. base rates to be upward. Over this period gilt yields increased by 25-35 basis points.

Portfolio duration was maintained short relative to the benchmark. During the third quarter short dated gilt yields again moved sharply higher. The market priced in further base rate increases; the August rise came earlier than expected and the market increasingly expected a November increase, which did indeed materialise. Yields continued to climb higher during the fourth quarter as inflationary pressures built, GDP growth continued to accelerate, the housing market remained strong and the MPC remained hawkish. Although there was some switching a little longer during this period, the duration of the portfolio was allowed to decline.

The overall calendar year return of 4.12% for sterling compared favourably to the 1-3 gilt index return of 3.05%, but under-performed compared to the cash index (4.70%).

The US dollar portfolio was also managed with a short duration. Two-year US Treasury yields increased from 4.4% to 5.2% in the first half of the year, as the FOMC raised rates at their first four meetings of the year. Rates remained on hold for the rest of the year as the US economy showed some signs of weakness, notably in the housing market, which saw a sharp slowdown in both construction and buyer activity. The Treasury market rallied in the second half of the year and two-year yields finished the year at 4.8%. The dollar portfolio returned 5.12% in 2006, which compared favourably to both the 1-3 year US Treasury index return of 3.97% and the cash index return of 5.08%. A large exposure to floating rate notes positively contributed to performance as yield increases translated into higher overall portfolio yields.

The Euro market saw yields increasing steadily throughout the year, as the ECB raised rates five times during the year, driven by surprisingly strong German export-led growth, above-target inflation and excessive money supply growth. Portfolio duration was maintained short relative to benchmark throughout the year. The portfolio return of 2.64% compares favourably to the 1.77% from the 1-3 year Euro Government Bond index, but under-performed compared to the cash index return of 2.81%

2007 outlook

2007 will start with yet higher expectations for investment returns, in all currencies. Portfolio durations are likely to be at or above those seen during 2006, although the relatively parallel shift in short-term yield curves during 2006 means that flat yield curves continue to offer little or no additional return for potentially higher risk levels. Once again, short-term volatility may provide tactical opportunities to enhance returns through more active duration management. Credit fundamentals remain good, but default rates, in lower grade credit, have increased in 2006 whilst credit spreads have not reflected any change in risk profile. As money remains relatively cheap and LBOs aim for ever larger targets, the potential for a significant credit 'event' remains. Therefore selective increases in exposure to high-grade, non-Government, issuers is likely to continue focussing on 'carry' trades whilst minimising 'basis' risk of credit spread widening.

Report of the directors of the managing agent at 31 December 2006

Accounting records

As required by the Syndicate Accounting Byelaw, reinsurance resumes setting out a summary of the reinsurance programme protecting all years of account have been approved by the directors of Imagine and are available for inspection at the registered office of Imagine.

Subcontracted functions

The managing agent has sub contracted the following functions:

Maintenance of accounting records and certain data processing functions: Capita London Market Services Limited.

Investment management: Credit Agricole Asset Management (UK) Limited.

Errors and omissions insurance

Lloyd's underwriting agents errors and omission insurance cover is not a mandatory requirement by Lloyd's. With only uncommercial terms currently available, no errors and omissions insurance has been purchased by Imagine. The matter continues to be under review.

Names' annual general meeting

In accordance with the conditions of the Syndicate Meetings (Amendment No 1) Byelaw, the managing agent proposes not to hold a Names' annual general meteing. Any member of the syndicate who wishes to object to this proposal should do so by 24 April 2007.

Disclosure of information to auditors

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Syndicate's auditors are unaware; and each director has taken all the steps that he/she ought to have taken as a director to make himself/herself aware of any relevant audit information and to establish that the Syndicate's auditors are aware of that information.

Auditors

The managing agent appointed KPMG Audit Plc as auditors for the first time in the year. The prior year auditors were Mazars.

Bob Wallace

Bob Wallace recently retired from his position as Chairman of Imagine Syndicate Management Limited. Since joining Imagine at the end of 2005, Bob has been instrumental in helping Imagine assimilate its London businesses into one cohesive unit. On behalf of us all I would like to take this opportunity to thank Bob for the contribution he has made to our success and congratulate him on 36 years of service in the London insurance market. We wish him a long and happy retirement.

Greg Morrison has been appointed Chairman of Imagine Syndicate Management Limited with effect from 16 March 2007.

On behalf of the Board

Iain Bremner
Managing Director

London

22 March 2007

Underwriter's report for the year ended 31 December 2006

2004 year of account

Allocated Capacity	£73.99m
Capacity Utilisation	74%
Profit	£9.35m

I am very pleased to confirm a bottom line profit of £9.35M which is just below the top of the most recent forecast range.

By the end of calendar year 2003 the UK liability sector had seen the peak of the much vaunted and well documented hard market. The subsequent year experienced a gradual decline in rates as new capacity came into the market to take advantage of the benign trading conditions. Whilst this resulted in a premium rate reduction of between 10 and 12.5 percent during calendar year 2004, trading conditions in the UK liability sector continued to be very strong. It is sometimes easy to forget the soundness of the trading conditions in previous years but it is nevertheless true to say that 2004 was a very good year. As a result of the influx of new capital, we were unable to fully utilise our premium capacity which at the close was just under 75% of stamp.

I have previously reported that my team made fundamental changes to the account in 2003 and these changes were consolidated in 2004 and subsequent years. Our original philosophy regarding the make up of the account has not altered since we began underwriting at 2525 although we have continued where necessary to refine, fine tune, and develop the processes we have set in place to manage the business successfully.

Our objective following the formation of our Leeds office in September 2003 and a radical overhaul of all our claims systems was to post robust and sustainable reserves at the earliest opportunity. The reason for this is simple; it provides our strongest tool for making informed underwriting decisions. There is strong evidence to suggest that reserving inadequacy follows a downturn in the premium cycle.

The result of this change in the way business is managed is now reflected in the account. We have had significant earlier development within the first 24 months of the 2004 Year of Account compared with 2003 and all prior years but we have also experienced a marked slowing down of this development from that point. The net incurred loss ratio for 2004 has only moved 4.3 per cent in the last fifteen months and at the close stood at 46.6 per cent. Conversely, in the same period of its development the 2000 Year of Account moved 23.9 per cent whilst the 2001 Year of Account moved 27.8 per cent.

Since the close of the 2003 Year of Account the net incurred loss ratio for the 2000 year has improved by 7 per cent, the 2001 year has remained largely unchanged, the 2002 year improved by 1 per cent and the 2003 year has also remained unchanged. This stability has had a marked change on how the actuaries now predict the ultimate development of our account and this has allowed for a release from prior years that boosts the 2004 account result.

Specific accounts to which I have previously referred, namely the Homebond Capital Cover and the Hong Kong Workmen's Compensation account, have continued to run off well. In the latter case, our decision to change claims handler over eighteen months ago has proved very effective in that we have been able to settle over 75% of all outstanding claims on the troublesome CT9 account.

All of this has been achieved by the comprehensive work that our claims team have undertaken and the sure guidance of Rob Turner (Claims Director) and Rob Carroll (Leeds based UK Claims Manager) to whom I am in debt for their sheer hard work and continuous innovation.

There is still considerable competition within our sector of the market and competition from outside Lloyds's generally takes a far less measured approach. Currently, our market within the UK transacts in excess of £2.6bn premium of which perhaps £400m is placed within Lloyd's. Notwithstanding this, the rate reductions to which I previously referred have not been as great as feared especially when one considers just how hard the market was at its peak in 2003.

During 2005 rate reductions totalled just less than 10 per cent and in 2006 were just over 8 per cent. I had predicted rate reductions for 2006 of 5 per cent at this time last year. However, unfortunately, we have not managed to achieve this and I suspect that rate reductions for 2007 may well be similar to those experienced in 2006.

Underwriter's report for the year ended 31 December 2006

2005 year of account

Stamp Capacity	£44.28m
Forecast Utilisation	92.67%
Profit in 2006	£3.37m

Due to the change in the trading conditions we experienced in 2004 and subsequent under utilisation of our stamp capacity the business plan we submitted to Lloyd's for 2005 contained a de-emption to £57m. The capital outturn was £44.28m following the downgrade of the 2002-year profit forecast.

This has, however, allowed us to improve significantly our premium utilisation and furthermore helped us to maintain our underwriting focus and concentrate on risk selection. The account was broadly similar to 2004 and we have remained close to our business plan targets whilst rating reductions amounted to just less than 10% of the renewal book.

I am confident that a profit will be delivered for the 2005 year of account at the 36 month stage.

2006 year of account

Stamp Capacity	£49.99m
Forecast Utilisation	69.49%
Loss in 2006	£1.42m

Our stamp increased marginally for 2006 following the significant drop in premium capacity we experienced in 2005. Competition within our sector was still strong creating pressure on rating. The reductions we experienced on our renewal book were just below 9%. I had originally forecast these to be approximately 5% but we have found it difficult to achieve this and at the same time keep retention levels stable.

The income for the year is predicted to be between £38m and £39m which will equate to a premium utilisation of just under 80%. This is disappointing in light of our increased capacity but stands well as a comparison with the income written in 2005. The account as in all years was very similar to 2005 and there was no significant change to our business ratios.

2007 year of account and the future

Stamp Capacity	£42.00m

At this point in the cycle, there are some who clamour for change. We are strong believers in our philosophy and have thus far not considered it necessary to deviate from the course we have taken. Our strong broker relationships allow us to mitigate some of the impact of soft market conditions but we underwrite in a marketplace which means that we cannot completely avoid the impact of falling prices.

I have written in some detail of the systems and processes that we have installed since our arrival at 2525 to ensure as far as we are able a positive return to capital providers notwithstanding the state of the market. These are the parts of the business that we have complete control of and within which we can exercise sound business judgement. We recognise that no system or process is perfect and that we will need to re-assess them constantly. It is therefore in these areas that we shall focus our energies.

We have innovative ways by which we differentiate ourselves and believe that they allow us to compare favourably to our peers in the market. We are always happy to discuss this face to face in more detail with capital providers who so desire.

One cannot always guarantee a positive return but I do believe that we will always compare well with our peers in any given market conditions. These are difficult times for us and there is no doubt that we need some correction in the market. My feeling is that it will more likely in the latter part of 2008. I thank you all for your support and trust that you will keep faith in us.

D L Pratt
Active Underwriter

22 March 2007

Statement of managing agent's responsibilities

The managing agent is responsible for preparing the syndicate annual report and annual accounts in accordance with applicable laws and regulations.

The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2004 require the managing agent to prepare annual accounts for Syndicate 2525 at 31 December each year in accordance with UK GAAP which give a true and fair view of the state of affairs of the syndicate as at the date and of its profit or loss for that year.

In preparing the syndicate annual accounts, the managing agent is required to:

1. select suitable accounting policies which are applied consistently, with the exception of changes arising on the adoption of new accounting standards in the year;

2. make judgements and estimates that are reasonable and prudent;

3. prepare the financial statements on the basis that the syndicate will continue to write future business unless it is inappropriate to presume that the syndicate will do so;

4. follow applicable United Kingdom accounting standards, subject to any material departures disclosed and explained in the annual report.

The directors confirm that they have complied with the above requirements in preparing the financial statements of Syndicate 2525.

The managing agent is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the syndicate and enable it to ensure that the syndicate annual accounts comply with the 2004 Regulations. It is also responsible for safeguarding the assets of the syndicate and hence for taking reasonable steps for prevention and detection of fraud and other irregularities.

The managing agent is responsible for the maintenance and integrity of the corporate and financial information included on the business' website. Legislation in the UK governing the preparation and dissemination of the financial statements may differ from legislation in other jurisdictions.

Independent auditors' report to the members of syndicate 2525

We have audited the syndicate annual accounts for the year ended 31 December 2006 which comprise the profit and loss account, the balance sheet, the cash flow statement, the statement of total recognised gains and losses and the related notes. The syndicate annual accounts have been prepared under the accounting policies set out therein.

This report is made solely to the members of the syndicate, as a body, in accordance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2004. Our audit work has been undertaken so that we might state to the syndicate's members those matters we are required to state in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the syndicate's members as a body for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of managing agent and auditors

The managing agent's responsibilities for preparing the syndicate annual accounts in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the statement of managing agent's responsibilities on page 11.

Our responsibility is to audit the syndicate annual accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the syndicate annual accounts give a true and fair view and are properly prepared in accordance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2004. We also report to you if in our opinion the managing agent's report is not consistent with the syndicate annual accounts, if the managing agent has not kept proper accounting records in respect of that syndicate, if the syndicate annual accounts are not in agreement with the accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding remuneration of the directors of the managing agent and other transactions is not disclosed.

We read the other information attached to the syndicate annual accounts and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the syndicate annual accounts. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the syndicate annual accounts. It also includes an assessment of the significant estimates and judgements made by the managing agent in the preparation of the syndicate annual accounts, and of whether the accounting policies are appropriate to the syndicate'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 syndicate annual accounts 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 syndicate annual accounts.

Opinion

In our opinion:

- the syndicate annual accounts give a true and fair view in accordance with UK Generally Accepted Accounting Practice, of the state of syndicate 2525's affairs as at 31 December 2006 and of its profit for the year then ended;

- the syndicate annual accounts have been properly prepared in accordance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2004; and

- the information given in the managing agent's report is consistent with the syndicate annual accounts.

KPMG Audit Plc
Chartered Accountants
Registered Auditor

22 March 2007

Profit and loss account: technical account – general business at 31 December 2006

	Notes	2006 £000	2006 £000	2005 £000	2005 £000
Earned premiums, net of reinsurance					
Gross premiums written	3	45,670		53,102	
		45,670		53,102	
Outward reinsurance premiums		(7,373)		(9,759)	
Change in the provision for unearned premiums					
Gross amount		2,072		949	
Reinsurers' share		(482)		(593)	
			39,887		43,699
Allocated investment return transferred from the non-technical account			4,779		4,323
Claims incurred, net of reinsurance					
Claims paid – Gross amount		(15,959)		(17,691)	
– Reinsurers' share		919		3,260	
		(15,040)		(14,431)	
Change in the provision for claims					
Gross amount		(14,638)		(2,587)	
Reinsurers' share		(8,748)		(3,522)	
		(5,890)		(6,109)	
			(20,930)		(20,540)
Net operating expenses	4		(12,443)		(14,505)
Balance on the technical account – for general business			11,293		12,977

The syndicate's turnover and expenses all relate to continuing operations.

The notes on pages 19 to 27 form part of the financial statements.

Profit and loss account: non-technical account at 31 December 2006

	Notes	2006 £000	2005 £000
Balance on the general business technical account		11,293	12,977
Investment income	9	6,132	5,171
Unrealised gains on investments		27	31
Investment expenses and charges	10	(750)	(695)
Unrealised losses on investments		(630)	(184)
Allocated investment return transferred to general business technical account		(4,779)	(4,323)
Profit for the financial year	14	11,293	12,977

The notes on pages 19 to 27 form part of the financial statements.

Statement of total recognised gains and losses at 31 December 2006

	2006 £000	2005 £000
Profit for the financial year	11,293	12,977
Foreign exchange movement on member's funds	(67)	120
Total recognised gains and losses since last annual report	11,226	13,097

Balance sheet – assets at 31 December 2006

	Notes	2006 £000	2006 £000	2005 £000	2005 £000
Assets					
Investments					
Other financial investments	11		110,914		119,104
Reinsurers' share of technical provisions					
Provision for unearned premiums		2,883		3,365	
Claims outstanding		24,952		16,220	
			27,835		19,585
Debtors					
Due within 1 year:					
Debtors arising out of direct insurance operations	12	10,586		15,789	
Debtors arising out of reinsurance operations	13	549		2,508	
Other debtors		1,417		5,605	
			12,552		23,902
Due after 1 year:					
Amounts due from members		146		813	
Other debtors		–		130	
			146		943
Other assets					
Cash at bank and in hand		19,536		5,439	
Overseas deposits		11,278		8,626	
			30,814		14,065
Prepayments and accrued income					
Deferred acquisition costs		3,710		4,248	
Other prepayments and accrued income		421		366	
			4,131		4,614
Total assets			186,392		182,213

The notes on pages 19 to 27 form part of the financial statements.

Balance sheet – liabilities at 31 December 2006

	Notes	2006 £000	2006 £000	2005 £000	2005 £000
Liabilities					
Capital and reserves					
Members' balances	14		14,354		15,576
Technical provisions					
Provision for unearned premiums		18,544		20,652	
Claims outstanding		146,512		132,288	
			165,056		152,940
Creditors					
Due within 1 year:					
Creditors arising out of direct insurance operations	15	3,077		2,629	
Creditors arising out of reinsurance operations	16	–		2,388	
Other creditors including taxation and social security		3,224		6,406	
Accruals and deferred income		–		226	
			6,301		11,649
Due after 1 year:					
Other creditors		285		2,048	
Accruals and deferred income		396		–	
			681		2,048
Total liabilities			186,392		182,213

The financial statements on pages 13 to 27 were approved by the Board of Imagine Syndicate Management Limited on 22 March 2007 and were signed on its behalf by

I J Bremner
Managing Director

22 March 2007

The notes on pages 19 to 27 form part of the financial statements.

Statement of cash flows at 31 December 2006

	Notes	2006 £000	2005 £000
Reconciliation of operating profit to net cash inflow from operating activities			
Operating profit on ordinary activities		11,293	12,977
Realised and unrealised investments gains/(losses)		1,422	(948)
Increase in net technical provisions		3,867	4,825
Decrease in debtors		11,497	997
(Decrease)/Increase in creditors		(6,715)	2,606
Foreign exchange movements on balance due to members		(67)	–
Net cash inflow from operating activities		21,297	20,457
Net cash inflow from operating activities		21,297	20,457
Payment of agency fees		(285)	–
Transfer to members in respect of underwriting participations:		(11,035)	(1,134)
Financing:			
Cash calls received/distribution losses		4	1,254
		9,981	20,577
Cash flows were invested as follows:			
Increase/(Decrease) in cash holdings	17	14,117	(21,630)
Net portfolio investment	17	(4,136)	42,207
Net investment of cash flows		9,981	20,577

Notes to the financial statements at 31 December 2006

1. Basis of preparation

These financial statements have been prepared in accordance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2004, applicable Accounting Standards in the United Kingdom, and comply with the Statement of Recommended Practice issued by the Association of British Insurers in December 2005 (as amended in December 2006) ("the ABI SORP").

2. Accounting policies

The financial statements have been prepared on an annual basis of accounting, whereby the incurred cost of claims, commission and related expenses are charged against the earned proportion of premiums, net of reinsurance as follows:

(a) Premiums written

Premiums written comprise premiums on contracts incepted during the financial year. Premiums are shown gross of brokerage payable and exclude taxes and duties levied on them. Estimates are made for pipeline premiums, representing amounts due to the syndicate not yet notified, as well as adjustments made in the year to premiums written in prior accounting periods.

(b) Unearned premiums

Written premium is earned according to the risk profile of the policy. Unearned premiums represent the proportion of premiums written in the year that relate to unexpired terms of policies in force at the balance sheet date, calculated on the basis of established earnings patterns or time apportionment as appropriate.

(c) Reinsurance premium ceded

Outwards reinsurance premiums are accounted for in the same accounting period as the premiums for the related direct or inwards business being reinsured.

(d) Claims provisions and related recoveries

The provision for claims comprises amounts set aside for claims notified and claims incurred but not yet reported (IBNR).

Claims incurred comprise claims and settlement expenses (both internal and external) paid in the year and the movement in provision for outstanding claims and settlement expenses, including an allowance for the cost of claims incurred by the balance sheet date but not reported until after the year end.

The amount included in respect of IBNR is based on statistical techniques of estimation applied by the syndicate's external consulting actuaries. These techniques generally involve projecting from past experience of the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. The provision for claims also includes amounts in respect of internal and external claims handling costs. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions.

The reinsurers' share of provisions for claims is based on calculated amounts of outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the year and the current security rating of the reinsurance companies involved. The syndicate uses a number of statistical techniques to assist in making these estimates.

Accordingly the two most critical assumptions as regards claims provisions are that the past is a reasonable predictor of the likely level of claims development and that the rating and other models used for current business are fair reflections of the likely level of ultimate claims to be incurred.

The directors consider that the provisions for gross claims and related reinsurance recoveries are fairly stated on the basis of the information currently available to them. However, ultimate liability will vary as a result of subsequent information and events and this 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. The methods used, and the estimates made, are reviewed regularly.

(e) Unexpired risks provision

A provision for unexpired risks is made where claims, related expenses and deferred acquisition costs, likely to arise after the end of the financial period in respect of contracts concluded before that date, are expected to exceed the unearned premiums and premiums receivable under these contracts, after the deduction of any acquisition costs deferred.

Notes to the financial statements at 31 December 2006

2. Accounting policies *(continued)*

The provision for unexpired risks is calculated separately by reference to classes of business which are managed together, after taking into account relevant investment return.

(f) Acquisition costs

Acquisition costs, comprising commission and other costs related to the acquisition of new insurance contracts are deferred to the extent that they are attributable to premiums unearned at the balance sheet date. Deferred acquisition costs represent the proportion of acquisition costs incurred in respect of unearned premiums at the balance sheet date.

(g) Foreign currencies

Income and expenditure in US dollars, Candian dollars, and Euros are translated into sterling at the average rates of exchange. Underwriting transactions denominated in other foreign currencies are included at the rate of exchange ruling at the date the transaction is processed.

Syndicate assets and liabilities, are translated into sterling at the rates of exchange at the balance sheet date. Differences arising on translation of foreign currency amounts in syndicates are included in the statement of total recognised gains and losses.

(h) Investments

Investments are stated at current value at the balance sheet date. For this purpose listed investments are stated at mid-market value and deposits with credit institutions and overseas deposits are stated at cost. Unlisted investments for which a market exists are stated at the average price at which they were traded on the balance sheet date or the last trading day before that date.

(i) Investment return

Investment return comprises all investment income, realised investment gains and losses and movements in unrealised gains and losses, net of investment expenses, charges and interest.

Realised gains and losses on investments carried at market value are calculated as the difference between sale proceeds and purchase price. Movements in unrealised gains and losses on investments represent the difference between the valuation at the balance sheet date, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

Investment return is initially recorded in the non-technical account. A transfer is made from the non-technical account to the general business technical account to reflect the investment return on funds supporting underwriting business.

(j) Taxation

Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct basic rate income tax from trading income. In addition, all UK basic rate income tax (currently at 22%) deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members or their members’ agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax.

(k) Pension costs

Imagine Syndicate Management Limited operates a defined contribution scheme. Pension contributions relating to Syndicate staff are charged to the syndicate and included within net operating expenses.

Notes to the financial statements at 31 December 2006

3. Segmental analysis

An analysis of the underwriting result before investment return is set out below:

2006	Gross premiums written £000	Gross premiums earned £000	Gross claims incurred £000	Net operating expenses £000	Reinsurance balance £000	Total £000
Direct insurance:						
Third party liability	45,670	47,742	(30,597)	(12,443)	1,812	6,514
Total	45,670	47,742	(30,597)	(12,443)	1,812	6,514

2005	Gross premiums written £000	Gross premiums earned £000	Gross claims incurred £000	Net operating expenses £000	Reinsurance balance £000	Total £000
Direct insurance:						
Third party liability	53,102	54,051	(20,278)	(14,505)	(10,614)	8,654
Total	53,102	54,051	(20,278)	(14,505)	(10,614)	8,654

All premiums were written in the UK. Analysis by destination is not materially different from the analysis above.

4. Net operating expenses

	2006 £000	2005 £000
Acquisition costs	8,798	9,556
Change in deferred acquisition costs	532	(53)
Administrative expenses	3,107	5,251
Loss/(Profit) on exchange	6	(249)
	12,443	14,505

Administrative expenses include:

	2006 £000	2005 £000
Auditors' remuneration		
Audit services	137	84
Other services	–	3
	137	87

Notes to the financial statements at 31 December 2006

5. Staff numbers and costs

All staff are employed by the managing agency. The following amounts were recharged to the syndicate in respect of salary costs:

	2006 £000	2005 £000
Wages and salaries	1,204	1,046
Social security costs	128	124
Other pension costs	115	142
	1,447	1,312

The average number of employees employed by the managing agency but working for the syndicate during the year was as follows:

	2006 Number	2005 Number
Administration and finance	12	9
Underwriting	6	5
Claims	8	5
	26	19

6. Emoluments of the directors of Imagine Syndicate Management Limited

The directors of Imagine Syndicate Management Limited received the following aggregate remuneration charged to the syndicate and included within net operating expenses:

	2006 £000	2005 £000
Emoluments	106	554
Contributions to pension schemes	5	81
	111	635

Notes to the financial statements at 31 December 2006

7. Active underwriter's emoluments

The active underwriter received the following aggregate remuneration charged as a syndicate expense:

	2006 £000	2005 £000
Emoluments	182	187
Contributions to defined contribution pension schemes	18	29
	200	216

8. Highest paid director's emoluments

The highest paid director received the following aggregate remuneration charged as a syndicate expense:

	2006 £000	2005 £000
Emoluments	50	187
Contributions to defined contribution pension schemes	5	29
	55	216

9. Investment income

	2006 £000	2005 £000
Income from investments	6,102	5,165
Gains on the realisation of investments	30	6
	6,132	5,171

10. Investment expenses and charges

	2006 £000	2005 £000
Investment management expenses, including interest	90	87
Losses on realisation of investments	660	608
	750	695

Notes to the financial statements at 31 December 2006

11. Other financial Investments

	Market value 2006 £000	Market value 2005 £000	Cost 2006 £000	Cost 2005 £000
Debt securities and other fixed income securities	110,189	118,757	111,064	118,515
Other loans	725	347	709	334
	110,914	119,104	111,773	118,849

12. Debtors arising out of direct insurance operations

	2006 £000	2005 £000
Due within one year		
– intermediaries	10,586	15,789
	10,586	15,789

13. Debtors arising out of reinsurance operations

	2006 £000	2005 £000
Due within one year		
– intermediaries	549	2,508
	549	2,508

14. Reconciliation of members' balances

	2006 £000	2005 £000
Members' balances brought forward at 1 January	15,576	2,479
Profit for the financial year	11,293	12,977
Exchange movement	(67)	120
Distribution to members'	(12,448)	–
Carried forward at 31 December	14,354	15,576

Members participate on syndicates by reference to years of account. Their ultimate result, assets and liabilities are assessed with reference to policies incepting in that year of account in respect of the the years on which they participate.

15. Creditors arising out of direct insurance operations

	2006 £000	2005 £000
Due within one year		
– Intermediaries	3,077	2,629
	3,077	2,629

Notes to the financial statements at 31 December 2006

16. Creditors arising out of reinsurance operations

	2006 £000	2005 £000
Due within one year – intermediaries	–	2,388
	–	2,388

17. Movement in opening and closing portfolio investments net of financing

	2006 £000	2005 £000
Net cash inflow/(outflow) from the year	14,117	(21,630)
Cash flow – portfolio investments	(4,136)	42,207
Movement arising from cash flows	9,981	20,577
Changes in market value and exchange rates	(1,422)	948
Total movement in portfolio investments net of financing	8,559	21,525
Balance brought forward at 1 January	133,169	111,644
Balance carried forward at 31 December	141,728	133,169

	At 1 January 2006 £000	Cash flow £000	Changes to market value and currencies £000	At 31 December 2006 £000
Cash at bank and in hand	5,439	14,117	(20)	19,536
Debt securities and other fixed income securities	118,757	(7,287)	(1,281)	110,189
Deposit with credit institutions	347	370	8	725
Overseas deposits	8,626	2,781	(129)	11,278
Total portfolio investments	133,169	9,981	(1,422)	141,728

18. Net cash inflow/(outflow) on portfolio investments

	2006 £000	2005 £000
Purchase of overseas deposits	3,151	(1,098)
Purchase and sale of shares	(7,287)	(41,109)
Net cash outflow on portfolio investments	(4,136)	(42,207)

Notes to the financial statements at 31 December 2006

19. Funds at Lloyd's

Every member is required to hold capital at Lloyd's which is held in trust and known as Funds at Lloyd's (FAL). These funds are intended primarily to cover circumstances where syndicate assets prove insufficient to meet participating members' underwriting liabilities.

The level of FAL that Lloyd's requires a member to maintain is determined by Lloyd's based on FSA requirements and resource criteria. FAL has regard to a number of factors including the nature and amount of risk to be underwritten by the member and the assessment of the reserving risk in respect of business that has been underwritten. Since FAL is not under the management of the managing agent, no amount has been shown in these financial statements by way of such capital resources. However, the managing agent is able to make a call on the members' FAL to meet liquidity requirements or to settle losses.

20. Disclosure of interests

Imagine Syndicate Management Limited (ISML)

Total fees payable to ISML in respect of services provided to the syndicate amounted to £300K (2005: £266K).

Profit commission of £2.70m (2005 £1.62m) is also due to ISML in respect of the profit on the 2004 (2003) closed year. Profit commission of £285K has been accrued for the 2005 year of account. Profit commission is only payable on closure of the account: the 2005 year of account will normally close at 31 December 2007 and the 2006 year of account at 31 December 2008.

Expenses totalling £1.35m (2005: £1.37m) were recharged to the syndicate by ISML. Expenses incurred jointly by the managing agent and the syndicate are apportioned between them on the basis of work performed and resources used. Expenses are charged to the year of account for which they are incurred.

Imagine Underwriting Services Limited (IUSL)

IUSL is a non-profit making service company that has been granted a binding authority to underwrite on behalf of Syndicate 2525 and 2526. IUSL places employers' liability, public liability and professional indemnity business with the syndicates.

IUSL receives an overrider commission on the premium underwritten on behalf of Syndicate 2525, in 2006 this amounted to £175K (2005: £355K). IUSL has rebated this overrider commission to Syndicate 2525 and this is included as a credit against syndicate expenses. ISML executives have not received any benefit for acting as directors of IUSL. No overriding commission is charged on premiums underwritten on behalf of Syndicate 2526.

Deepdale Underwriting Limited (Deepdale)

Deepdale is a NameCo formed principally by I J Bremner, A G Dore, M D Hunt, D L Pratt, R C Turner and R J Wallace. Its participations on Abacus managed services are as follows:

	2003 (£m)	2004 (£m)	2005 (£m)	2006 (£m)	2007 (£m)
2525	–	0.423	0.327	–	–
2526	–	0.195	0.225	–	–

Notes to the financial statements at 31 December 2006

20. Disclosure of interests *(continued)*

Related parties

In addition to ISML, Imagine has interests in other Lloyd's managing agencies, and related corporate capital vehicles:

Danish Re Syndicates Limited (DRSL)
Imagine Underwriting Limited (IUL)
Danish Re Capital Limited
Fenwall Limited
Polder Limited
Imagine Corporate Capital Limited
SOC Corporate Member No 6 Limited
Greenfield Underwriting Limited

For the 2006 Year of Account, Danish Re Capital Limited participates on syndicate 2525 with a line of £736,999.

For the 2006 Year of Account, SOC Corporate Capital Member No 6 Limited participates on syndicate 2525 with a line of £275,000.

The directors of ISML are also directors of DRSL and IUL. Further details can be obtained from Imagine.

During 2006 the managing agencies of ISML, DRSL and IUL were combined into ISML to form one managing agency responsible for the management of the following syndicates:

994
1400
1923
2525
2526

2004 Closing Year
Reports and Accounts

Managing agent's report for the 2004 closing year of account

We are very pleased to announce that the 2004 year has closed with a profit after profit commission and members' agents fees of £14.78m which is just below the top of the most recent forecast range.

2004 Highlights

Allocated capacity	£73.99m
Capacity utilisation	74%
Profit	£14.78m

Active Underwriter's comments on the 2004 year of account

By the end of calendar year 2003 the UK liability sector had seen the peak of the much vaunted and well documented hard market. The subsequent year experienced a gradual decline in rates as new capacity came into the market to take advantage of the benign trading conditions. Whilst this resulted in a premium rate reduction of between 10 and 12.5 percent during calendar year 2004, trading conditions in the UK liability sector continued to be very strong. It is sometimes easy to forget the soundness of the trading conditions in previous years but it is nevertheless true to say that 2004 was a very good year. As a result of the influx of new capital, we were unable to fully utilise our premium capacity which at the close was just under 75% of stamp.

I have previously reported that my team made fundamental changes to the account in 2003 and these changes were consolidated in 2004 and subsequent years. Our original philosophy regarding the make up of the account has not altered since we began underwriting at 2525 although we have continued where necessary to refine, fine tune, and develop the processes we have set in place to manage the business successfully.

Our objective following the formation of our Leeds office in September 2003 and a radical overhaul of all our claims systems was to post robust and sustainable reserves at the earliest opportunity. The reason for this is simple; it provides our strongest tool for making informed underwriting decisions. There is strong evidence to suggest that reserving inadequacy follows a downturn in the premium cycle.

The result of this change in the way business is managed is now reflected in the account. We have had significant earlier development within the first 24 months of the 2004 Year of Account compared with 2003 and all prior years but we have also experienced a marked slowing down of this development from that point. The net incurred loss ratio for 2004 has only moved 4.3 per cent in the last fifteen months and at the close stood at 46.6 per cent. Conversely, in the same period of its development the 2000 Year of Account moved 23.9 per cent whilst the 2001 Year of Account moved 27.8 per cent.

Since the close of the 2003 Year of Account the net incurred loss ratio for the 2000 year has improved by 7 per cent, the 2001 year has remained largely unchanged, the 2002 year improved by 1 per cent and the 2003 year has also remained unchanged. This stability has had a marked change on how the actuaries now predict the ultimate development of our account and this has allowed for a release from prior years that boosts the 2004 account result.

Specific accounts to which I have previously referred, namely the Homebond Capital Cover and the Hong Kong Workmen's Compensation account, have continued to run off well. In the latter case, our decision to change claims handler over eighteen months ago has proved very effective in that we have been able to settle over 75% of all outstanding claims on the troublesome CT9 account.

All of this has been achieved by the comprehensive work that our claims team have undertaken and the sure guidance of Rob Turner (Claims Director) and Rob Carroll (Leeds based UK Claims Manager) to whom I am in debt for their sheer hard work and continuous innovation.

There is still considerable competition within our sector of the market and competition from outside Lloyds's generally takes a far less measured approach. Currently, our market within the UK transacts in excess of £2.6bn premium of which perhaps £400m is placed within Lloyd's. Notwithstanding this, the rate reductions to which I previously referred have not been as great as feared especially when one considers just how hard the market was at its peak in 2003.

During 2005 rate reductions totalled just less than 10 per cent and in 2006 were just over 8 per cent. I had predicted rate reductions for 2006 of 5 per cent at this time last year. Unfortunately, we have not managed to achieve this and I suspect that rate reductions for 2007 may well be similar to those experienced in 2006.

Statement of managing agent's responsibilities

The Insurance Accounts Directive (Lloyd's Syndicates and Aggregate Accounts) Regulations 2004 (the "Lloyd's Regulations") require the managing agent to prepare syndicate underwriting year of accounts for each syndicate in respect of any underwriting year which is being closed by reinsurance to close at 31 December. These syndicate underwriting year accounts must give a true and fair view of the result of the closed year of account.

In preparing the syndicate underwriting year accounts, the managing agent is required to:

- select suitable accounting policies which are applied consistently and where there are items which affect more than one year of account, ensure a treatment which is equitable as between the members of the syndicate affected. In particular, the amount charged by way of premium in respect of the reinsurance to close shall, where the reinsuring members of the same syndicate for different years of account, be equitable between them, having regard to the nature and amount of the liabilities reinsured;
- take into account all income and charges relating to a closed year of account without regard to the date of receipt or payment;
- make judgements and estimates that are reasonable and prudent; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in these accounts.

The managing agent confirms that they have complied with the above requirements in preparing the underwriting accounts of syndicate 2525.

The managing agent is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the syndicate and enable it to ensure that the syndicate annual accounts comply with the Lloyd's Regulations and Syndicate Accounting Byelaw. It is also responsible for safeguarding the assets of the syndicate and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The managing agent is responsible for the maintenance and integrity of the corporate and financial information included on the business' website. Legislation in the UK governing the preparation and dissemination of the financial statements may differ from legislation in other jurisdictions.

Independent auditors' report to the members of syndicate 2525 – 2004 closed year of account

We have audited the syndicate underwriting year accounts for the three years ended 31 December 2006 on pages 33 to 41, which comprise the Profit and Loss Account, the Balance Sheet, Statement of Total Recognised Gains and Losses and the related notes. These have been prepared under the accounting policies set out therein.

This report is made solely to the members of the syndicate, as a body, in accordance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2004 and the Lloyd's Syndicate Accounting Byelaw (No 8 of 2005). Our audit work has been undertaken so that we might state to the syndicate's members those matters we are required to state in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the syndicate's members as a body for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the managing agent and auditors

The managing agent's responsibilities for preparing the syndicate underwriting year accounts in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the statement of managing agent's responsibilities on page 31.

Our responsibility is to audit the syndicate underwriting year accounts in accordance with the relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the syndicate underwriting year accounts give a true and fair view of the result of the closed year of account. We also report to you if, in our opinion, the managing agent's report is not consistent with the syndicate underwriting year accounts, if the managing agent has not kept proper accounting records in respect of the syndicate or if we have not received all the information and explanations we require for our audit.

We read the managing agent's report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the syndicate underwriting year accounts. It also includes an assessment of the significant estimates and judgements made by the directors of the managing agent in the preparation of the syndicate underwriting year accounts, and of whether the accounting policies are appropriate to the syndicate'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 syndicate underwriting year accounts 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 syndicate underwriting year accounts.

Opinion

In our opinion the syndicate underwriting year accounts give a true and fair view in accordance with UK Generally Accepted Accounting Practice of the profit for the 2004 closed year of account

KPMG Audit Plc
Chartered Accountants
Registered Auditor
8 Salisbury Square
London EC4Y 8BB

28 March 2007

Profit and loss account for the 36 months ended 31 December 2006

Technical account – general business

	Notes	2006 £000	2006 £000
Earned premiums, net of reinsurance			
Gross premiums written	3	64,944	
Outward reinsurance premiums		(12,806)	
			52,138
Reinsurance to close premiums received, net of reinsurance			69,608
Allocated investment return transferred from the non-technical account			4,751
Claims incurred, net of reinsurance			
Claims paid – Gross amount		(31,225)	
– Reinsurers' share		15,437	
		(15,788)	
Reinsurance to close premium payable, net of reinsurance		(78,294)	
			(94,082)
Net operating expenses	5		(17,578)
Balance on the technical account for general business			14,837

The underwriting year has closed: all items therefore relate to discontinued operations.

Profit and loss account for the 36 months ended 31 December 2006

Non-technical account

	Notes	2006 £000
Balance on the general business technical account		14,837
Investment income	6	5,859
Unrealised gains on investments		34
Investment expenses and charges		(44)
Unrealised losses on investments		(535)
Realised gains on investments		27
Realised losses on investments		(590)
Allocated investment return transferred to the general business technical account		(4,751)
Profit for the closed year of account		14,837

Statement of total recognised gains and losses for the 36 months ended 31 December 2006

	2006 £000
Profit for the closed year of account	14,837
Foreign exchange movement on members' funds	(61)
Total recognised gains and losses	14,776

Balance sheet at 31 December 2006

	Notes	2006 £000	£000
ASSETS			
Investments	7		71,803
Debtors			
Debtors arising out of direct insurance operations	8	9	
Debtors arising out of reinsurance operations	9	694	
Other debtors		296	
			999
Reinsurance recoveries anticipated on gross reinsurance to close premiums payable to close the account			14,505
Cash at bank and in hand			23,953
TOTAL ASSETS			111,260
LIABILITIES			
Amounts due to members	10		14,776
Reinsurance to close premiums payable to close the account – gross amount			92,799
Creditors			
Creditors arising out of direct insurance operations	11	989	
Other creditors including taxation and social security		2,696	
			3,685
TOTAL LIABILITIES			111,260

The syndicate underwriting year accounts were approved by the Board of Imagine Syndicate Management Limited on 28 March 2007 and were signed on its behalf by

L Gibbins
Director
28 March 2007

The notes on pages 37 to 41 form part of these financial statements.

Notes to the accounts for the 36 months ended 31 December 2006

1. Basis of preparation

The syndicate underwriting year accounts have been prepared under the Insurance Accounts Directive (Lloyd's Syndicates and Aggregate Accounts) Regulations 2004 ("the Lloyd's Regulations) and in accordance with the Syndicate Accounting Byelaw and applicable accounting standards in the United Kingdom. They comply with the Statement of Recommended Practice issued by the Association of British Insurers in December 2005 (as amended in December 2006) ("the ABI SORP").

Members participate on a syndicate by reference to a year of account and each syndicate year of account is a separate annual venture. These accounts relate to the 2004 year of account which has been closed by reinsurance to close at 31 December 2006; consequently the balance sheet represents the assets and liabilities of the 2004 year of account and the profit and loss account and cash flow statement reflect the transactions for that year of account during the 36 months period until closure.

As each syndicate year of account is a separate annual venture, there are no comparative figures.

2. Accounting policies

Underwriting transactions

(a) The underwriting accounts for each year of account are normally kept open for three years before the result on that year is determined. At the end of the three year period, outstanding liabilities can normally be determined with sufficient accuracy to permit the year of account to be closed by payment of a reinsurance to close premium to the successor year of account.

(b) The reinsurance to close premium is determined by reference to the outstanding technical provisions (including those for outstanding claims, unearned premiums, net of deferred acquisition costs, and unexpired risks) relating to the closed year and to all previous closed years reinsured therein. Although this estimate of net outstanding liabilities is considered to be fair and reasonable, it is implicit in the estimation procedure that the ultimate liabilities will be at variance from the premium so determined. The reinsurance to close premium transfers the liability in respect of all claims, reinsurance premiums, return premiums and other payments in respect of the closing year (and previous closed years reinsured therein) to the members of the successor year of account and gives them the benefit of refunds, recoveries, premiums due and other income in respect of those years in so far as they have not been credited in these accounts.

(c) Gross premiums are allocated to years of account on the basis of the inception date of the policy. Commission and brokerage are charged to the year of account to which the relevant policy is allocated. Policies written under binding authorities, lineslips or consortium arrangements are allocated to the year of account into which the arrangement incepts. Additional and return premiums follow the year of account of the original premium. Premiums are shown gross of brokerage payable and exclude taxes and duties levied on them. Estimates are made for pipeline premiums, representing amounts due but not yet notified to the syndicate year of account.

Written premium is earned according to the risk profile of the policy. Unearned premiums represent the balance of premiums written in the period to the balance sheet date that relate to unexpired terms of policies in force at that date, calculated on the basis of established earnings patterns or time apportionment as appropriate.

Outwards reinsurance premiums ceded are attributed to the same year as the original risk being protected.

(d) Gross claims paid are allocated to the same year of account as that to which the corresponding premiums are allocated and include internal and external claims settlement expenses. Reinsurance recoveries are allocated to the year of account to which the claim was charged.

(e) The outstanding claims comprise amounts set aside for claims notified and claims incurred but not yet reported (IBNR).

Notified claims are estimated on a case by case basis with regard to the circumstances as reported, any information available from loss adjusters and previous experience of the cost of settling claims with similar characteristics. The amount included in respect of IBNR is based on statistical techniques of estimation applied by

Notes to the accounts for the 36 months ended 31 December 2006

2. Accounting policies *continued*

the syndicate's external consulting actuaries. These techniques generally involve projecting from past experience of the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions.

The provision for claims includes amounts in respect of internal and external claims handling costs.

The reinsurers' share of provisions for claims is based on calculated amounts of outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the year and the current security rating of the reinsurance companies involved.

The syndicate uses a number of statistical techniques to assist in making the above estimates.

The two most critical assumptions as regards claims provisions are that the past is a reasonable predictor of the likely level of claims development and that the rating and other models used for current business are fair reflections of the likely level of ultimate claims to be incurred. The methods used, and the estimates made, are reviewed regularly.

(f) A provision for unexpired risks is created where claims, related expenses and deferred acquisition costs, likely to arise after the balance sheet date in respect of contracts relating to the closing year of account, are expected to exceed the unearned premiums and premiums receivable under these contracts, after the deduction of any acquisition costs deferred.

(g) Acquisition costs, comprising commission and other internal and external costs related to the acquisition of new insurance contracts are deferred to the extent that they are attributable to premiums unearned at the balance sheet date.

Investments and investment return

(h) Investment return comprises investment income, realised investment gains and losses and movements in unrealised gains and losses, net of investment expenses and charges. Investment return arising in each calendar year on all the syndicate's investments is allocated to open years of account in proportion to the average funds available for investment attributable to those years. Investment returns in respect of overseas deposits are allocated to the year of account which funded these deposits.

Realised gains and losses on investments carried at market value are calculated as the difference between sale proceeds and purchase price. Movements in unrealised gains and losses on investments represent the difference between their valuation at the balance sheet date and their purchase price or, if they have been previously valued, their valuation at the end of the previous calendar year, together with the reversal of unrealised gains and losses recognised in earlier calendar years in respect of investment disposals in the current period.

Investment return is initially recorded in the non-technical account. A transfer is made from the non-technical account to the general business technical account to reflect the investment return on funds supporting underwriting business. All investment return is considered to arise on such funds.

Investments are stated at current value at the balance sheet date. For this purpose listed investments are stated at mid-market value and deposits with credit institutions and overseas deposits are stated at cost. Unlisted investments for which a market exists are stated at the average price at which they were traded on the balance sheet date or the last trading day before that date.

Notes to the accounts for the 36 months ended 31 December 2006

2. Accounting policies *continued*

Syndicate operating expenses

(i) Costs incurred by the managing agent in respect of the syndicate are charged to the syndicate and included within the relevant profit and loss account heading. Where expenses do not relate to any specific year of account they are apportioned between years of account on a basis which reflects the benefit obtained by each year of account from each type of expense.

Where expenses are incurred jointly by the managing agent and the syndicate, they are apportioned as follows:

Salaries and related costs – according to time of each individual spent on syndicate matters
Accommodation costs – according to number of personnel
Other costs – as appropriate in each case

The managing agent operates a defined contribution pension scheme and its recharges to the syndicate in respect of salaries and related costs include an element for pension costs. These pension costs are expensed in full in the period to which the recharge relates.

Amounts recharged by the managing agent include costs arising from the use of assets in the period. These rental costs are expensed in full in the period to which the recharge relates.

Taxation

(j) Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct basic rate income tax from trading income. In addition, all UK basic income tax deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members or their members' agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax. It is the responsibility of members to agree and settle their individual tax liabilities with HM Revenue & Customs.

Members resident overseas for tax purposes are responsible for agreeing and settling any tax liabilities with the taxation authorities of their country of residence.

Basis of currency translation

(j) Transactions in US dollars, Candian dollars and Euros are translated at the rate of exchange at the date of the transaction or at an approximate average rate. Underwriting transactions denominated in other foreign currencies are included at the rate of exchange ruling at the date the transaction is processed.

Assets and liabilities are re-translated into sterling at the rate of exchange at the balance sheet date.

Although transactions are translated as described above, the final result for the year of account is calculated with US dollars, Canadian dollars and Euros translated at the balance sheet rates of exchange.

Differences arising on the re-translation of foreign currency amounts are included in the non technical account under "other charges" or "other income", dependent on whether it is a loss or profit.

Where Euros are sold or bought relating to the profit or loss of a closed underwriting account after 31 December, any exchange profit or loss arising is reflected in the underwriting account into which the liabilities of that year have been reinsured. Where United States dollars and Canadian dollars relating to the profit or loss of a closed underwriting account are bought or sold by members on that year, any exchange profit or loss accrues to those members.

Notes to the accounts for the 36 months ended 31 December 2006

3. Particulars of business written

TYPE OF BUSINESS

An analysis of the underwriting result before investment return is set out below:

2006	Gross premiums written and earned £000	Gross claims incurred £000	Gross operating expenses £000	Reinsurance balance £000	Total £000
Direct insurance:					
Third party liability	64,944	(109,519)	(17,578)	72,239	10,086
Total	64,944	(109,519)	(17,578)	72,239	10,086

All business is written in the United Kingdom. Analysis by destination is not materially different from the analysis above.

Gross operating expenses are the same as net operating expenses.

4. Technical account balance before allocated investment return and net operating expenses

	2006 £000
Balance attributable to business allocated to the 2004 year of account	23,453
Balance attributable to the reinsurance to close for the 2003 year of account	4,211
	27,664

5. Net operating expenses

	2006 £000
Acquisition costs	11,737
Change in deferred acquisition costs	1
Member's agent fee	504
Administrative expenses	5,336
	17,578

The closed year profit is stated after charging:

	2006 £000
Auditors' remuneration	
Audit services	63

The auditors did not receive any other remuneration other than that stated above.

Notes to the accounts for the 36 months ended 31 December 2006

6. Investment income

	2006 £000
Income from investments	5,859
	5,859

7. Investments

	Market value 2006 £000
Debt securities and other fixed income securities	71,803
	71,803

8. Debtors arising out of direct insurance operations

	2006 £000
Due within one year	
– intermediaries	9
	9

9. Debtors arising out of reinsurance operations

	2006 £000
Due within one year	549
Due after one year	145
	694

10. Amounts due to members

	2006 £000
Profit for the closed year of account	14,837
Foreign exchange movement on members' funds	(61)
Members' balances carried forward at 31 December 2006	14,776

11. Creditors arising out of direct insurance operations

	2006 £000
Due within one year	989
	989

Summary of closed year results at 31 December 2006

	2000 £000	2001 £000	2002 £000	2003 £000	2004 £000
Syndicate allocated capacity	£25,612	£37,087	£44,786	£41,992	£73,988
Number of underwriting members	307	307	294	280	514
Aggregate net premiums	£19,597	£31,667	£32,315	£29,690	£40,400
Results for an illustrative share of £10,000	**£**	**£**	**£**	**£**	**£**
Gross premiums	9,846	11,394	9,593	11,442	8,778
Net premiums	7,651	8,539	7,215	7,070	5,460
Reinsurance to close from and earlier account	–	4,877	10,364	15,802	9,408
Net claims	(2,248)	(2,552)	(2,770)	(3,352)	(2,134)
Reinsurance to close	(6,890)	(12,489)	(14,971)	(16,576)	(10,582)
Loss on exchange	(33)	(75)	(88)	33	(4)
Syndicate operating expenses	(843)	(634)	(231)	(274)	(118)
Balance on technical account	(2,363)	(2,334)	(481)	2,073	2,030
Investment income less investment expenses and charges and investment gains less losses	635	715	688	984	642
Profit/(loss) on ordinary activities	(1,728)	(1,619)	207	3,687	2,672
Illustrative personal expenses					
Managing agent's fee	60	60	60	60	60
Profit commission	–	–	–	525	373
Other personal expenses (excluding members' agents fees)	125	100	125	125	125
	185	160	185	710	558
Profit/(loss) on ordinary activities after illustrative managing agent's fee and profit commission and illustrative personal expenses	(1,913)	(1,779)	22	2,977	2,114
Total of syndicate operating expenses, managing agent's fee and profit commission	£903	£694	£291	£859	£551
Capacity utilised	98.46%	113.94%	95.93%	96.14%	74.03%
Net capacity utilised	76.51%	85.39%	69.92%	77.60%	54.60%
Underwriting loss ratio	(24.0%)	(20.5%)	(5.0%)	18.13%	16.30%

Notes

1. The summary of closed year results has been prepared from the audited accounts of the syndicate.
2. Personal expenses have been stated at the amount which would be incurred pro rata by individual Names writing the illustrative premium income in the syndicate irrespective of any minimum charge applicable. Corporate members may be charged at different rates. Foreign tax, which may be treated as a credit for personal tax purposes, has been excluded.
3. As regards the 2005 and 2006 years of account, an illustrative share of £10,000 represents 0.0226% and 0.0200% of the respective allocated capacity.

Produced by Stephen Duke Ltd 020 7422 0040 (10593)

I M A G I N E

Imagine Syndicate Management Limited
4th Floor
70 Gracechurch Street
London EC3V 0XL

tel: 020 3102 3100