HAMILTON INSURANCE COMPANY LIMITED

FINANCIAL STATEMENTS

FOR THE YEAR ENDED

31 DECEMBER 2005

The Company's registered number is 1655888

HAMILTON INSURANCE COMPANY LIMITED

Board of directors
S G Boyle - Chairman
P J Blackmore
P A de Chazal
A H Doggart
A R Hill (resigned 31 December 2005)
A P Hope
J F Uphoff (appointed 19 December 2005)
S J Young - Managing Director

Secretary
C J Rivers

Registered and Head Office
North Street
Winkfield
Windsor
Berkshire SL4 4TD
Telephone +44(0)1344 890000

Registered in England
No: 1655888

Bankers
The Royal Bank of Scotland plc
Corporate Banking Office
PO Box 450
5-10 Great Tower Street
London EC3P 3HX

Auditors
KPMG Audit Plc
8 Salisbury Square
London EC4Y 8BB

HAMILTON INSURANCE COMPANY LIMITED

Directors' report

The directors present their annual report on the affairs of the Company, together with the financial statements and auditors' report, for the year ended 31 December 2005.

Principal activity

The principal activity of the Company continues to be the transaction of accident and health, property and payment or credit protection general insurance business.

Financial results

Gross written premium income increased during the year to £244 million from £209 million in 2004. There was a profit for the year of £4.7 million (2004: £3.7 million).

The directors do not recommend payment of a dividend (2004: £nil).

Accounting policies

For all periods up to and including year ended 31 December 2004, the Company prepared its financial statements in accordance with UK Generally Accepted Accounting Principles ("UK GAAP"). From 1 January 2005, the Company prepared its financial statements in accordance with International Financial Reporting Standards ("IFRS") as endorsed by EU and effective for reporting for the year ended 31 December 2005. In line with our ultimate parent, Hamilton Insurance Company Limited has also adopted the requirements of IFRS 7 'Financial Instruments: Disclosure' ("IFRS 7") prior to its effective date of 1 January 2007.

Directors

The directors of the Company are shown on page 1.

Directors' interests

Directors' interests in the shares of HSBC Holdings plc, the ultimate parent undertaking, required to be disclosed under the Companies Act 1985 are set out below:

	HSBC Holdings plc ordinary shares of US$0.50 each	
	31 December 2005	1 January 2005
S G Boyle - Chairman	2,082	1,698
P J Blackmore	3,997	3,613
P A de Chazal	2,460	2,119
A H Doggart	505	1,862
A P Hope	49,342	50,461
J F Uphoff	5,357 *	5,357 *
S J Young - Managing Director	2,082	1,698

* Held as 'American Depository Receipts'

The terms of a number of Employee Benefit Trusts provide that all employees of HSBC Holdings plc and any of its subsidiary undertakings are potential beneficiaries of the Trusts. As potential beneficiaries of the Trusts, each director of the Company is deemed to have a technical interest in all of the HSBC Holdings plc ordinary shares of US$0.50 each held by the Trusts. At 31 December 2005, the Trusts held a total of 130.8 million ordinary shares of US$0.50 each (2004: 123.1 million).

During the year, no options over HSBC Holdings plc ordinary shares were granted/exercised to directors of the Company.

Employee information

The Company does not employ any staff directly. All staff used by the Company were employed and provided by HFC Bank Limited and HSBC Bank plc for both 2005 and 2004.

Equality of opportunity

The group of which the Company is a member is an equal opportunity employer. The aim is to ensure that all job applicants and employees are treated in the same way regardless of their sex, marital status, age, race, colour, disability, sexual preference, nationality or ethnic origin.

HAMILTON INSURANCE COMPANY LIMITED

Directors' report (continued)

Auditors

The Company passed an elective resolution in accordance with section 379(A) Companies Act 1985 to dispense with the obligation to appoint auditors annually as permitted by section 386 Companies Act 1985. KPMG Audit plc shall be deemed to be re-appointed as auditors to the Company for the next financial year.

Statement of directors' responsibilities

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in *accordance with IFRSs as adopted by the EU.*

The financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position of the Company and the performance for that period; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; 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 that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have a 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.

By order of the board

C J Rivers
Secretary

13 February 2006

North Street
Winkfield
Windsor
Berkshire SL4 4TD

Independent auditors' report to the members of Hamilton Insurance Company Limited

We have audited the financial statements of Hamilton Insurance Company Ltd ("the Company") for the year ended 31 December 2005 which comprise the income statement, the balance sheet, the cash flow statement, the statement of total recognised income and expense and the related notes. These financial statements have been prepared under the accounting policies set out therein.

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

As described in the 'statement of directors' responsibilities' on page 3, the Company's directors are responsible for the preparation of the financial statements in accordance with applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the EU.

Our responsibility is to audit the financial statements 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 financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. 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 other transactions is not disclosed.

We read the directors' 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 financial statements. It also includes an assessment of the significant estimates and judgments 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, in accordance with IFRSs as adopted by the EU, of the state of the Company's affairs as at 31 December 2005 and of its profit for the year then ended; and
- have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

KPMG Audit Plc

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

13 February 2006

Income statement

For the year ended 31 December

	Notes	2005	2005	2004	2004
		£000	£000	£000	£000
Gross premiums written	3	243,500		208,785	
Outward reinsurance premiums	3	(6,905)		(5,064)	
			236,595		203,721
Change in the unearned premiums					
- gross amount	3	8,145		(7,032)	
- reinsurers' share	3	(3)		16	
			8,142		(7,016)
Net insurance premium revenue	3		**244,737**		**196,705**
Financial income	5		**6,705**		**5,042**
Claims paid					
- gross amount		(96,436)		(62,577)	
- reinsurers' share		749		62	
		(95,687)		(62,515)	
Change in the provision for claims					
- gross amount		(6,918)		(11,532)	
- reinsurers' share		-		-	
		(6,918)		(11,532)	
Net policyholder claims and benefits incurred	3		**(102,605)**		**(74,047)**
Change in equalisation provision			-		(2,337)
Investment expenses and charges			(90)		(64)
Net operating expenses	3 , 4		(142,009)		(118,756)
Profit before income tax			**6,738**		**6,543**
Income tax expense	7		(2,022)		(2,850)
Profit for the year			**4,716**		**3,693**

All recognised gains and losses have been included in the income statement. All operations of the Company continued throughout both periods and no operations were discontinued.

The notes on pages 10 to 19 form an integral part of these financial statements.

Statement of total recognised income and expense

	Notes	2005	2004
		£000	£000
Profit for the year		4,716	3,693
Total recognised income and expense for the year		4,716	3,693
IFRS Transitional adjustment as at 1 January 2005	1(g)	2,368	-
Change in fair value of financial assets available for sale		(8)	-
Prior year adjustment	4(b)	-	1,229
Total recognised gains and losses for the year		7,076	4,922

Movements in shareholders' funds are shown in note 16.

The notes on pages 10 to 19 form an integral part of these financial statements.

HAMILTON INSURANCE COMPANY LIMITED

Balance sheet

As at 31 December

	Notes	2005	2004
		£000	£000
Assets			
Intangible assets			
Deferred acquisition costs	11	28,661	37,001
Financial assets	8	147,045	127,744
Reinsurance assets			
Unearned premiums		301	303
Reinsurance recoverables		25	-
Other reinsurance debtors		1,890	978
		2,216	1,281
Insurance and other receivables			
Debtors arising from direct insurance operations	9	15,430	22,471
Other debtors	10	62	-
Accrued interest		1,466	1,019
		16,958	23,490
Cash and cash equivalents			
Cash at bank and in hand	12	-	1,174
Total assets		194,880	190,690

The notes on pages 10 to 19 form an integral part of these financial statements.

HAMILTON INSURANCE COMPANY LIMITED

Balance sheet (continued)

As at 31 December

	Notes	2005	2004
		£000	£000
Liabilities			
Insurance contract provisions			
Unearned premiums	18	77,741	85,886
Claims provisions	18	39,261	32,425
Equalisation provisions	18	-	3,382
		117,002	121,693
Insurance, other payables and deferred income			
Creditors arising out of direct insurance operations	13	16,300	14,695
Creditors arising out of reinsurance operations		-	1,461
		16,300	16,156
Deferred tax liabilities	15	2,004	-
Income taxes			
Other creditors including taxation	14	1,089	1,495
Cash and cash equivalents			
Bank overdraft	12	63	-
Total liabilities		**136,458**	**139,344**
Net assets		**58,422**	**51,346**
Shareholders equity			
Called up share capital	17	23,212	23,212
Share premium account	16	93	93
Profit and loss account	16	30,441	28,041
Equalisation reserve	16	4,684	-
Fair value reserve	16	(8)	-
Total shareholders equity		**58,422**	**51,346**

The financial statements on pages 5 to 19 were approved by the board of directors on 13 February 2006 and signed on its behalf by the directors listed below.

S G Boyle Chairman

S J Young Managing Director

The notes on pages 10 to 19 form an integral part of these financial statements.

HAMILTON INSURANCE COMPANY LIMITED

__Cash flow statement__

For the year ended 31 December

	Notes	2005	2005	2004	2004
Cash flows from operating activities		**£000**	**£000**	**£000**	**£000**
Profit before income tax			6,738		6,543
Adjustments for:					
Investment income		(6,630)		(4,903)	
Unrealised (gains)/losses on financial assets		6		(139)	
Change in deferred acquisition cost asset		8,340		(7,753)	
			1,716		(12,795)
Increase in financial assets		(13,132)		(16,633)	
Increase in reinsurance assets		(935)		(843)	
(Increase)/decrease in insurance and other receivables		6,978		(10,220)	
Increase in insurance, other payables and deferred income		1,606		10,123	
Decrease in reinsurance liabilities		(1,461)		(2,084)	
Increase/(decrease) in other liabilities and provisions		(1,311)		20,260	
			(8,255)		603
Income taxes paid			(1,436)		(3,697)
Net cash from operating activities			**(1,237)**		**(9,346)**
Cash flow from financing activities					
Proceeds from the issue of share capital			-		10,000
Net cash flow from financing activities			-		**10,000**
Net increase in cash and cash equivalents			**(1,237)**		**654**
Cash and cash equivalents at 1 January	1(h),12		1,174		520
Cash and cash equivalents at 31 December	1(h),12		**(63)**		**1,174**

The Company classifies the net acquisition of financial assets as operating cash flows as they are funds from the net cash flows associated with insurance contracts.

Notes to the financial statements

1 Significant accounting policies

Hamilton Insurance Company Limited was incorporated on 2 August 1982. The Company is domiciled in England and Wales and its registered office is shown on page 1.

(a) Statement of compliance

For all periods up to and including year ended 31 December 2004, the Company prepared its financial statements in accordance with UK Generally Accepted Accounting Principles UK GAAP in accordance with historic cost convention, as modified to include the revaluation of investments, the ABI SORP - Accounting for Insurance Business, and the provisions of Section 255 of, and Schedule 9A to the UK Companies Act 1985. From 1 January 2005, the Company prepared its financial statements in accordance with International Financial Reporting Standards ("IFRSs") and interpretations thereof issued by the International Accounting Standards Board IASB and its predecessor body as well as interpretations issued by the International Financial Interpretations Committee ("IFRIC") and those parts of the UK Companies Act 1985. They are prepared on a going concern basis.

An explanation of how the transition to IFRSs has affected the reported financial position and financial performance is provided below in 1 (c) and note 22.

(b) Basis of preparation

The financial statements are presented in Great British Pounds which is the Company's functional and presentation currency, rounded to the nearest thousand. They are prepared on the historical cost basis except that the financial assets classified as available for sale are stated at fair value.

The preparation of financial information requires the use of estimates and assumptions about future conditions. Use of available information and application of judgement are inherent in the information of estimates. Actual results in the future may differ from those reported.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimates are revised if the revision affects only that year, or the year of revision and future years if the revisions affect both current and future years. Judgements made by management in application of IFRSs that have a significant effect on the financial statements and estimates with significant risks of material adjustments in the next year are discussed in note 2 below.

The accounting policies set out below have been applied consistently to all years presented in these financial statements and in preparing the opening IFRSs balance sheet as at 1 January 2005 for the purposes of the transition to IFRSs.

(c) Change in accounting policy

The Company has adopted IFRS 4 'Insurance Contracts' ("IFRS 4"), IAS 32 'Financial Instruments: Disclosure and Presentation' ("IAS 32"), and IAS 39 'Financial Instruments: Recognition and Measurement' ("IAS 39") with effect from 1 January 2005. In preparing these financial statements, the Company has elected to take advantage of certain transitional provisions within IFRS 1 'First Time Adoption of International Financial Reporting Standards' which offer exemptions from presenting comparative information or applying IFRSs retrospectively. The most significant of these provisions is the exemption from presenting comparative information in accordance with IAS 32, IAS 39 and IFRS 4. Comparative information for financial instruments and insurance contracts has been prepared on the basis of the Company's previous accounting standards. A summary of the main changes to the comparative information to comply with IAS 39 and IFRS 4 as noted in 1(e) and 1(g), is set out below.

Reconciliation of equity		**Previous GAAP 1 January 2004 £000**	**Effect of transition to IFRSs £000**	**IFRSs 1 January 2004 £000**	**Previous GAAP 31 December 2004 £000**	**Effect of transition to IFRSs £000**	**IFRSs 31 December 2004 £000**
Total assets	1(e)	149,545	-	149,545	190,690	-	190,690
Technical provisions	1(g)	(101,431)	1,045	(100,386)	(121,693)	3,382	(118,311)
Other creditors	1(g)	(10,461)	(313)	(10,774)	(17,651)	(1,014)	(18,665)
Total liabilities		(111,892)	732	(111,160)	(139,344)	2,368	(136,976)
Net assets		37,653	732	38,385	51,346	2,368	53,714
Shareholders equity							
Called up share capital		13,212	-	13,212	23,212	-	23,212
Share premium account		93	-	93	93	-	93
Profit and loss account	1(g), 1(e)	24,348	-	24,348	28,041	-	28,041
Equalisation reserve	1(g)	-	732	732		2,368	2,368
		37,653	732	38,385	51,346	2,368	53,714

IFRS 4 does not permit the recognition of equalisation provisions. Accordingly, the profit and loss account reserve as at 1 January 2005 was credited with £2.4 million relating to a previously recognised equalisation provision to comply with IFRS 4. Of the £2.4 million, £1.6 million after tax related to 2004 and was included in the previously reported income statement for that year. In preparing its opening IFRSs balance sheet, the Company has adjusted amounts reported previously in financial statements prepared in accordance with its old basis of accounting (previous GAAP).

The IASB issued IFRS 7 'Financial Instruments Disclosures' ("IFRS 7") in August 2005. The accounting standard supersedes IAS 30 and replaces certain disclosure requirements of IAS 32. The standard is required to be applied for periods on or after 1 January 2007. The Company has applied the standard for the period beginning 1 January 2005. This standard was endorsed by the EU on 11 January 2006.

1 Significant accounting policies (continued)

(c) Change in accounting policy (continued)

Reconciliation of profit for 2004		**Previous GAAP 31 December 2004**	**Effect of transition to IFRSs**	**IFRSs 31 December 2004**
		£000	**£000**	**£000**
Profit before equalisation provision		8,880	-	8,880
Change in equalisation provision	1(g)	(2,337)	2,337	-
Profit before income tax		6,543	2,337	8,880
Income tax expense	1(g)	(2,850)	(701)	(3,551)
Profit after income tax		3,693	1,636	5,329

As at 1 January 2005 and throughout 2005, the Company classified its financial assets and liabilities under IAS 39 as mentioned in note 1(e). The Company's investment securities are classified as assets-for-sale ("AFS") and stated at fair value, with any resultant gain or loss being directly recognised in equity, except for impairment losses. The fair value of listed investments are their quoted bid prices at the balance sheet date. The fair value of unlisted investments are their bid prices as quoted by external brokers at the balance sheet date. Where these investments are interest-bearing with fixed maturity dates, interest is calculated using the effective interest rate method and recognised in the income statement. The financial impact as a result of this change in the accounting policy was not material and no adjustments were made to the opening balance sheet as at 1 January 2005.

(d) Annual basis

The technical result for accident and health, payment or credit protection, and property damage is determined on an annual basis whereby the incurred cost of claims, commission and related expenses are charged against the earned proportion of premiums, net of reinsurance as follows:

(i) Premiums

Written premiums are recognised when the premium is due for payment.

Premium income is earned over the life of each contract, using rules appropriate to the type of each insurance contract and taking account of the effect of reinsurance agreements.

Provision for unearned premiums is made to provide for periods of risk extending beyond the year end. Unearned premiums are calculated on a basis appropriate to the contract. The most significant contract sold by the Company is a policy providing benefits that can last for up to five years; unearned premiums for this contract are calculated on a basis known as the Rule of 45 (the simple average of a Rule of 78 unearned premiums reserve and a pro-rata reserve). Unearned premiums for most other contracts are calculated on a pro-rata basis. Premiums are stated net of insurance premium tax.

Outwards reinsurance premiums are recognised as a deduction from income in accordance with the pattern of reinsurance service received. A portion of the outward reinsurance premiums are treated as prepayments.

(ii) Acquisition costs

Acquisition costs comprise commissions paid or payable to HFC Bank Limited and third parties. Such costs which are incurred during the financial year but which relate to a subsequent period are deferred to the extent that they are recoverable from future margins.

The Company writes certain monthly policies sold by external brokers and HFC Bank Limited that generally remain in force for a period considerably in excess of one month. The acquisition costs payable under these contracts are recoverable either under the indemnity arrangements in place with external brokers or the profit share arrangements in place with HFC Bank Limited. The directors consider that the company's financial statements would not show a true and fair view if these acquisition costs were deferred on a basis compatible with that used for unearned premiums. Instead the acquisition costs associated with those policies sold by external brokers have been deferred over the related indemnity period and those associated with policies sold by HFC Bank Limited over a prudent estimate of persistency.

This treatment is a departure from Schedule 9A of the Companies Act 1985. If the directors were to adopt the requirements of Schedule 9A, the financial statements would not have stated a deferred acquisition cost ("DAC") asset for these monthly premiums. By adopting the policy as stated in the financial statements, a DAC asset of £5.2 million (2004: £18.9 million) and a current debit in the income statement of £13.7 million (2004: credit of £7.0 million) have been recognised. The overall pre-tax impact of adopting the accounting treatment per Schedule 9A of the Companies Act 1985 would have been an increase in current profits of £13.7 million (2004: decrease of £7.0 million). The increase in profit for 2005 of £13.7 million (2004: decrease of £7.0 million) would have resulted in an increase in the current year tax charge of £4.1 million (2004: decrease of £2.1 million).

(iii) Claims

Claims outstanding includes provision for claims incurred but not reported and related claims handling expenses. The provision is assessed using historic claims experience and, for the major classes of business, a termination rate method in which future claims payments are projected using historic claims data. Reinsurance recoveries are assessed in a manner similar to the assessment of claims outstanding.

Claims incurred comprises claims paid in the year and changes in provisions for claims outstanding, together with any adjustments to claims from previous years.

1 Significant accounting policies (continued)

(e) Financial assets and liabilities

For all periods up to and including year ended 31 December 2004, unquoted financial assets such as cash deposits were shown on the balance sheet at cost and all quoted investments were held at market value. Gross investment income was accounted for on an accruals basis. Realised gains and losses on financial assets or liabilities at fair value through income are calculated as the difference between net sales proceeds and the value placed on those investments at the last balance sheet date.

As at 1 January 2005 and throughout 2005, financial assets and liabilities are classified into the following categories, depending on the purpose for which they were acquired:

(i) Financial assets and liabilities at fair value through income

A financial asset or liability is classified into this category at inception if acquired principally for the purpose of selling in the short term, if it forms part of a portfolio of financial assets in which there is evidence of short term profit taking, or if so designated by management.

(ii) Loans and receivables

Loans and other receivables are non-derivative financial assets with fixed determinable payments that are not quoted in an active market, other than those that the Company intends to sell in the near term, those that the Company upon initial recognition designates as at fair value through income, available for sale or where the Company may not recover substantially all of its initial investment.

(iii) Available-for-sale ("AFS")

AFS financial assets and liabilities are non-derivative financial assets or liabilities that are either designated in this category or are not classified in any of the other categories.

The Company has classified all of its investment securities as AFS financial assets. Financial assets classified as AFS financial assets are stated at fair value, with any resultant unrealised gain or loss being directly recognised in equity. When investment securities classified as AFS are sold or impaired, the accumulated fair value adjustments are included in the income statement as net realised gains and losses. Where these investments are interest-bearing with fixed maturity dates, interest is calculated using the effective interest rate method and recognised in the income statement.

Realised gains and losses on financial assets at fair value through income are calculated as the difference between net sales proceeds and the value placed on those investments at the last balance sheet date. Unrealised gains and losses on financial assets at fair value through income represent the difference between their valuation at the balance sheet date and their valuation at the last balance sheet date.

Purchases of financial assets are recognised on trade date, which is when the Company commits to purchase the assets. The fair value of listed investments are their quoted bid prices at the balance sheet date. The fair value of unlisted investments are their bid prices as quoted by external brokers at the balance sheet date. The carrying amounts of the Company's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the carrying value is reduced to the estimated recoverable amount by means of a charge to the income statement.

(f) Taxation

Income tax on profit comprises current taxation and deferred taxation. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case the related income tax is also recognised in equity.

Current taxation is the amount estimated to be payable or recoverable as a result of the application of the rules for the taxation of general insurance companies to the items included in income statement together with any necessary prior period adjustments.

Deferred tax is provided in full, using the balance sheet liability method, providing for temporary differences between carrying amounts of assets and liabilities for financial reporting purposes, and the amounts used for taxation purposes. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax assets and liabilities are not discounted.

(g) Equalisation reserve

For all periods up to and including year ended 31 December 2004, the Company maintained an equalisation provision in accordance with the Financial Services and Markets Act 2000 in respect of the property class of business written by the Company in order to reduce the impact of possible future claims volatility. It is calculated in accordance with the rules contained within PRU 7.5 of the Integrated Prudential Sourcebook for Insurers. The movement in the equalisation provision is recognised in the income statement previously known as the profit and loss account, and the provision was recognised as a liability on the balance sheet.

IFRS 4 does not permit the recognition of equalisation provisions. Accordingly, the profit and loss reserve as at 1 January 2005, as reported in last year's financial statements was credited with £2.4 million relating to a previously recognised equalisation provision. A separate non-distributable reserve within shareholders funds has been established for the same purpose and calculated under the existing rules noted above. Of the £2.4 million, £1.6 million after tax related to 2004 and was included in the previously reported income statement for that year. The comparative figures in these financial statements have not been adjusted.

(h) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Company's cash management are included as a cash and cash equivalents for the purposes of the statement of cash flows.

Notes to the financial statements (continued)

2 Risk management

The primary insurance activity carried out by the Company is the insurance against the risk of loss from persons that are directly subject to the risk. Such risks may relate to property, accident and health and financial perils that may arise from an insurable event. The Company is exposed to uncertainty surrounding timing and severity of claims under contract. The Company also has exposure to market risks through its insurance and investment activities.

The Company manages its insurance risks through underwriting limits, approval procedures for transactions that involve new products or that exceed set limits, pricing guidelines and management of reinsurance and monitoring of emerging issues. The Company uses internal risk measurement models to assess and monitor insurance risk exposures.

(a) Underwriting strategy

The Company's underwriting strategy seeks diversity to ensure a balanced portfolio and is based on a large portfolio of similar risks over a number of years and as such it is believed that this reduces the variability of the outcomes.

The Company's underwriting strategy is prepared by senior management and included in the annual operating plan ("AOP") which establishes the classes of business and products to be written both through HFC Bank Limited and external brokers. The Company's management monitors actual underwriting results against the AOP to ensure adherence, and to investigate significant variances on a monthly basis.

(b) Reinsurance strategy

The Company reinsures a portion of the risks it underwrites in order to control its exposure to losses and protect capital resources as it deems appropriate. The Company buys non-proportional reinsurance cover with approved external reinsurers to reduce the net exposure to the Company. The Company monitors the financial conditions of reinsurers on an ongoing basis and reviews its reinsurance arrangements periodically. The Company's net cost of buying reinsurance is £6.1 million (2004: £5 million).

(c) Management of risks

Insurance risk
The Company writes primarily payment protection insurance ("PPI") and domestic property insurance products. PPI products protects the policyholder against having to make loan or credit card repayments for a period of time if they are diagnosed as sick have an accident or made unemployed. Property insurance indemnifies, subject to any limits or excesses, the policyholder against loss or damage to their own material property. The Company charges premiums to policyholders. The event giving rise to a claim for these products usually occurs suddenly and the cause is easily determinable. The claim will thus be notified promptly and can be settled without delay. The key risks with property insurance products are underwriting and claims risk (including the variable incidence of natural disasters). The Company is also exposed to the risk of dishonest actions by policyholders.

Underwriting risk is the risk that the Company does not charge premiums appropriate for the insurance risks it insures. The risk on any policy will vary according to many factors such as location, safety measures in place and age of property for property insurance and average loan value for PPI. The pricing and provision assumptions are based on both historic internal information and experience. These assumptions are reviewed on a periodic basis. The Company's management reviews monthly underwriting performance against plan on a monthly basis.

Claims inducing perils such as storms, floods, subsidence, fires, explosions and rising crime levels and infectious diseases may occur on a regional basis. The Company's business is widely distributed throughout the UK and Irish Republic through the use of external brokers and the HFC Bank distribution. The greatest likelihood of significant losses to the Company arise from catastrophe events such as flood damage, storms and the state of the economy. The Company uses excess of loss reinsurance cover to minimise its exposure to these events.

Market risk
The Company's investment portfolio is managed by HSBC Investment (UK) Limited ("HIUK") using an approach that balances quality, diversification, asset/liability management, liquidity and investment return. The aim of the investment process is to optimise the net of taxes, risk-adjusted investment income and risk-adjusted total return, whilst ensuring that the assets and liabilities are managed on a cash flow and duration basis. The Company's investment committee establishes the investment guidelines/limits for approval by the board of directors and monitors investment performance and adherence to these guidelines on a regular basis.

The Company's exposure to market risk for changes in interest rates is concentrated in its investment portfolio and is considered minimal.

Credit risks
The Company's portfolio of debt securities and to a lesser extent short-term and other investments are subject to credit risk. The Company manages this risk through establishing strict investment guidelines and counterparty limits which are reviewed on a regular basis. The Company's policy is to invest in debt securities that are A-1 or better rated. HIUK uses counterparty limits approved by the Board, adherence to these limits and investment guidelines are monitored on a monthly basis. At the balance sheet date there were no significant concentrations of credit risk. The Company is also exposed to credit risk through its reinsurance arrangements, where an amount recoverable under the reinsurance contract may not be paid. The total exposure under reinsurance contracts is £2.2 million as at 31 December 2005 (2004: £1.3 million). The Company's policy is to use reinsurers that are rated A - or better.

Liquidity risk
The Company has to meet daily calls on cash resources, notably from claims arising from insurance contracts. There is therefore a risk that cash will not be available to settle liabilities when due. The Company manages risk by setting minimum limits on the proportion of assets that are held as cash and readily realisable assets that will be available to settle these liabilities as well as short-term borrowing facilities to cover for unusually high levels of claims.

Notes to the financial statements (continued)

2 Risk management (continued)

(c) Management of risks (continued)

Claims reserves

Outstanding claims provision includes provisions for reported claims, claims incurred but not reported (also known as 'IBNR') and related claims handling expenses. The provision for PPI products are assessed using historic claims experience and a termination rate method in which future claims payments and expected duration of claims are projected using historic claims data. For domestic property reserves are set using historic claims experience and individual case estimates. IBNR reserves are calculated using triangulation methods based on past experience. Reinsurance recoveries are assessed in a manner similar to the assessment of claims outstanding.

Both PPI and property insurance business are generally considered to be 'short tail' lines, as it takes a relatively short period of time to finalise and settle claims for a given accident year. As a result, the Company has not disclosed claims development information.

The assumptions that have the greatest effect on the measurement of insurance contract provisions are the average cost of property claims, and expected duration of PPI claims. These are used for assessing the IBNR and case estimates for 2004 and 2005 accidents. For 2005, the expected duration of a PPI claim from inception is between 5-7 months depending on type of claim. The average cost of property claims depends on the type of loss. For a typical claim the average cost is around £1,100, for certain larger types of claim this can range up to £31,000.

An analysis of sensitivity around various scenarios for general insurance business provides an indication of the adequacy of the Company's estimation process. The Company believes that the liability for claims reported in the balance sheet is adequate. However, it recognises that the process of estimation is based upon certain variables and assumptions which could differ when claims arise.

The table represented below demonstrates the sensitivity of insured liability estimates to particular movements in assumptions used in the estimation process.

	Financial Impacts	
	Profit after tax	**Net Assets**
	2005	**2005**
	£000	**£000**
Interest rates increasing 200 basis points	(474)	474
Interest rates increasing 100 basis points	(239)	239
Interest rates reducing 100 basis points	243	(243)
Interest rates reducing 200 basis points	490	(490)
Failure of major bond provider with 20% recovery	(3,925)	3,925
Claims cost increasing 20%	(4,114)	4,114
Claims cost reducing 20%	4,114	(4,114)

3 Premiums

All premiums are in respect of direct insurance business and are written in the United Kingdom, the Channel Islands and the Republic of Ireland. Business written outside the United Kingdom represents less than 5% of total gross premiums and has therefore not been analysed.

		2005			**2004**	
	Gross	**Reinsurance Ceded**	**Net**	**Gross**	**Reinsurance Ceded**	**Net**
Written premiums				**(restated)**	**(restated)**	**(restated)**
	£000	**£000**	**£000**	**£000**	**£000**	**£000**
Accident and health	10,654	-	10,654	12,438	(248)	12,190
Payment protection	117,171	-	117,171	114,374	(451)	113,923
Property damage	115,675	(6,905)	108,770	81,973	(4,365)	77,608
	243,500	(6,905)	236,595	208,785	(5,064)	203,721
Earned premiums						
Accident and health	10,626	-	10,626	10,250	(248)	10,002
Payment protection	125,399	-	125,399	110,016	(452)	109,565
Property damage	115,620	(6,908)	108,712	81,487	(4,348)	77,139
	251,645	(6,908)	244,737	201,753	(5,048)	196,705
Incurred claims						
Accident and health	2,528	-	2,528	2,280	(77)	2,203
Payment protection	34,593	-	34,593	28,991	-	28,991
Property damage	66,233	(749)	65,484	42,838	15	42,853
	103,354	(749)	102,605	74,109	(62)	74,047
Operating expenses						
Accident and health	4,943	-	4,943	4,685	-	4,685
Payment protection	87,264	-	87,264	76,572	-	76,572
Property damage	49,802	-	49,802	37,499	-	37,499
	142,009	-	142,009	118,756	-	118,756

Notes to the financial statements (continued)

3 Premiums (continued)

	2005 Gross	2005 Reinsurance Ceded	2005 Net	2004 Gross	2004 Reinsurance Ceded	2004 Net
Profit before income tax						
Accident and health	3,434	-	3,434	3,537	(171)	3,366
Payment protection	6,837	-	6,837	7,169	(452)	6,717
Property damage	2,625	(6,158)	(3,533)	823	(4,363)	(3,540)
	12,896	(6,158)	6,738	11,529	(4,986)	6,543

Previously, accident and sickness business classes relating to loans and credit card balances were reported under 'accident and health'. Under the revised FSA risk categories these have been classified as 'payment protection' for 2005. The 2004 comparatives above have also been restated.

4 Net operating expenses

(a) Net operating expenses

	2005 £000	2004 £000
Acquisition cost payable	86,069	78,048
Increase/(decrease) in deferred acquisition costs	8,339	(7,753)
Profit commission payable	42,864	44,654
Administrative expenses	4,737	3,807
	142,009	118,756

(b) Restatement of financial statements for 2003 and prior years

In 2004 the Company identified an error in its accounting for deferred acquisition costs for certain products. This error had resulted in the deferred acquisition cost asset being overstated in the financial statements for the year ended 31 December 2003 and in previous years. The cumulative effect of this error was that profit and loss account reserves carried forward at 31 December 2003, as reported in 2003 year's financial statements, were overstated by £1.2million (£1.8 million before taxation). Of the £1.2 million, £1.1 million after tax arose in 2003 but was not included in the reported profit and loss account for that year.

(c) Employee information

The Company does not employ any staff directly. All staff used by the Company were employed and provided by HFC Bank Limited and HSBC Bank plc for both 2005 and 2004.

(d) Auditors Remuneration

Auditors' remuneration for the current year was borne by the parent company.

5 Financial income

	2005 £000	2004 £000
Floating rate securities		
Floating rate notes	2,023	800
Fixed rate securities		
Commercial paper	701	468
Cash and money market deposits		
Cash deposits	666	2,964
Certificates of deposit	3,138	621
Other	177	189
	6,705	5,042

Floating and fixed rate securities are classified as AFS financial assets.

6 Directors' emoluments

	2005 £000	2004 £000
Aggregate emoluments as directors	254	210
Company pension contributions to money purchase schemes	17	13
	271	223

Retirement benefits are accruing to two directors under a money purchase scheme (2004: two directors). Two directors are due to receive amounts under long-term incentive schemes.

No director exercised share options in the holding company, HSBC Holdings plc, during the year. Directors' emoluments were paid by HFC Bank Limited for both 2005 and 2004.

Highest paid director:	2005	2004
Aggregate emoluments	145	118
Company pension contributions to money purchase scheme	10	8

The highest paid director did not exercise any share options in the ultimate holding company, HSBC Holdings plc, in the year.

Notes to the financial statements (continued)

7 **Income tax expense**

	2005	2004
Current tax expenses	**£000**	**£000**
Current year corporation tax at 30% (2004: 30%)	1,030	2,850
Deferred tax expense		
Origination and reversal of temporary differences	992	-
	992	-
Total income tax expense	2,022	2,850
Reconciliation of effective tax rate		
Profit before income tax	6,738	6,543
Taxation at 30% (2004: 30%)	2,022	1,963
Effects of :		
Under provided in prior years	-	826
UK taxation basis of insurance profits	-	61
Total income tax expense	2,022	2,850
Effective tax rate	30%	44%

8 **Financial assets**

	2005	2004
	£000	**£000**
Floating rate securities		
Listed	42,727	31,951
Fixed rate securities		
Unlisted	5,754	29,358
Cash and money market deposits		
Cash deposits	849	29,349
Certificates of deposit	91,706	35,496
Other money market investments	6,009	1,590
	147,045	127,744

Floating and fixed rate securities are classified as AFS financial assets. The amortised cost of investments held was the same as market value (2004: £105.5 million). The maturity value of these investments is £147 million (2004: £127.8 million).

9 **Debtors arising out of direct insurance operations**

	2005	2004
	£000	**£000**
Insurance receivables due from parent company	3,954	4,742
Insurance receivables due from other group companies	252	6,526
Insurance receivables due from third parties	9,567	8,089
Other receivables and prepayments	1,657	3,114
	15,430	22,471

10 **Other debtors**

	2005	2004
	£000	**£000**
Other debtors	62	-
	62	-

11 **Deferred acquisition costs**

	2005	2004
	£000	**£000**
Opening balance	37,001	29,248
Acquisition costs incurred in the year	86,069	78,048
Amortisation charge	(94,409)	(70,295)
Closing balance	28,661	37,001

12 **Cash and cash equivalents**

	2005	2004
	£000	**£000**
Bank and cash balances	3,211	1,311
Bank overdrafts	(3,274)	(137)
	(63)	1,174

HAMILTON INSURANCE COMPANY LIMITED

Notes to the financial statements (continued)

13 *Creditors arising out of direct insurance operations*

	2005 £000	2004 £000
Commission payable to parent company	4,565	2,832
Commission payable to other group companies	185	2,051
Other amounts owed to parent company	149	3,271
Insurance contract payables to other group companies	8,609	3,845
Insurance premium tax	2,712	2,562
Other creditors and accruals	80	134
	16,300	14,695

14 Other creditors including taxation and social security

	2005 £000	2004 £000
Taxation	1,089	1,495

15 Deferred tax liabilities

	2005 £000	2004 £000
Opening shareholders' funds under UK GAAP	-	-
IFRS 4 transitional adjustment see note 1(g)	1,015	-
Opening shareholders' funds after adjustment	1,015	-
Deferred tax expense	992	-
Change in fair value of financial assets available for sale	(3)	-
	2,004	-

Deferred taxation has been provided for in full as follows:

Short term timing differences	2,004	-

16 Reconciliation of shareholders' funds

	Share capital 2005 £000	*Share* premium 2005 £000	*Profit and* loss 2005 £000	*Fair value* reserve 2005 £000	*Equalisation* reserve 2005 £000	*Total* 2005 £000
Opening shareholders' funds under UK GAAP	23,212	93	28,041	-	-	51,346
IFRS 4 transitional adjustment see note 1(g)	-	-	-	-	3,383	3,383
Deferred tax expense					(1,015)	(1,015)
Opening shareholders' funds after adjustment	23,212	93	28,041	-	2,368	53,714
Profit for the year	-	-	4,716	-	-	4,716
Reserve transfer	-	-	(2,316)	-	2,316	-
Change in fair value of financial assets	-	-	-	(8)	-	(8)
Increase in called up share capital	-	-	-	-	-	-
Closing shareholders' funds	23,212	93	30,441	(8)	4,684	58,422

	Share capital 2004 £000	Share premium 2004 £000	Profit and loss 2004 £000	Fair value reserve 2004 £000	Equalisation reserve 2004 £000	Total 2004 £000
Opening shareholders' funds	13,212	93	24,348	-	-	37,653
Retained profit for the year	-	-	3,693	-	-	3,693
Increase in called up share capital	10,000	-	-	-	-	10,000
Closing shareholders' funds	23,212	93	28,041	-	-	51,346

17 Called up share capital

	2005 £000	2004 £000
Authorised:		
50,000,000 Ordinary shares of £1 each	50,000	50,000
Allotted, called up and fully paid:		
23,212,000 (2004: 23,212,000) Ordinary shares of £1 each	23,212	23,212

Notes to the financial statements (continued)

18 Insurance contract provisions

(a) Analysis of movements in claims provisions

	Total claims provisions 2005 £000	Total claims provisions 2004 £000
Opening balance	32,425	21,532
Payments in respect of previous years' claims	(33,117)	(23,277)
Run-off variance in prior years' provisions	2,141	3,431
Claims reserving for current year	101,131	70,432
Claims paid in respect of current year	(63,319)	(39,693)
Closing balance	39,261	32,425

During the period, favourable run-off deviation of £0.6 million was experienced in respect of the property business. There were unfavourable run-off deviations of £2.7 million in respect of accident and health and PPI business. In 2004, there was favourable run-off deviation of £1.5 million in respect of accident and health business and an unfavourable run-off deviation of £4.9 million in respect of payment protection and property business.

(b) Analysis of movements in provisions for unearned premiums

	Unearned premium provision 2005 £000	Unearned premium provision 2004 £000
Opening balance	85,886	78,854
Premiums written in the year	185,323	155,172
Premiums earned in the year	(193,468)	(148,140)
Closing balance	77,741	85,886

(c) Analysis of movements in equalisation provisions

	Equalisation provision 2005 £000	Equalisation provision 2004 £000
Opening balance	3,382	1,045
IFRS 4 transitional adjustment as at 1 January 2005 see note 1(g)	(3,382)	-
Revised opening balance as at 1 January 2005	-	1,045
Reserve movement	-	2,337
Closing balance	-	3,382

19 Derivatives and financial instruments

In respect of income earning financial assets, the following table indicates their effective interest rate at the balance sheet dates and their maturity.

	2005 £000	2005 %
Effective interest rates:		
Debt securities - fixed rate	97,460	4.61
Debt securities - variable rate	42,727	4.74
Cash and money market deposits	6,858	4.58
	147,045	
Maturities:		
Less than on year	108,318	
Between 1 and 2 years	4,851	
Between 2 and 3 years	12,505	
Between 4 and 5 years	3,002	
Over 5 years	18,369	
	147,045	

20 Ultimate parent company

The Company's immediate holding company is HFC Bank Limited. The ultimate holding company and the largest group in which HFC Bank Limited and its subsidiary companies are consolidated is HSBC Holdings plc, which is incorporated in England. The consolidated accounts of HSBC Holdings plc are available to the public and may be obtained from the Company Secretary at the Company's registered office.

Hamilton Insurance Company Limited is registered in England.

21 Related party transactions

The table below provides the balances of transactions the Company has with key management personnel, other group subsidiaries, and its parent company during the period. Key management personnel are those persons considered as having the authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly.

	Other group subsidiaries		**Parent company**	
	2005	**2004**	**2005**	**2004**
	£000	**£000**	**£000**	**£000**
Commissions and acquisition costs payable	10,048	4,089	46,633	49,621
Service charges payable	90	64	4,611	3,636
Year end balances relating to commissions, acquisition costs and service charges	3,060	2,910	4,015	2,977

Key management personnel are deemed to be the directors of the Company. Compensation paid to the key management personnel is disclosed as part of directors' emoluments in note 6. There were no other transactions between the Company and key management personnel during the year.

22 Explanation of transition to IFRSs

As stated in note 1(a), these are the Company's first financial statements prepared in accordance with IFRSs.

The accounting policies set out in note 1 have been applied in preparing the financial statements for the year ended 31 December 2005, the comparative information presented in these financial statements for the year ended 31 December 2004 are the same amounts reported previously in financial statements prepared in accordance with its old basis of accounting (UK GAAP). The 2004 comparatives have not been restated to reflect the change in accounting policies from UK to IFRSs GAAP.

The Company has adopted IFRS 4 and IAS 39 with effect from 1 January 2005. The resulting changes to the IFRSs balance sheet for 31 December 2004 are summarised below.

(a) IFRS 4 'Insurance Contracts'

IFRS 4 does not permit the recognition of equalisation provisions. Accordingly, the profit and loss reserve as at 1 January 2005 was £2.4 million relating to a previously recognised equalisation provision. A separate reserve within shareholders funds has been established for the same purpose. Of the £2.4 million, £1.6 million after tax related to 2004 and was included in the previously reported income statement for that year. In preparing its opening IFRSs balance sheet, the Company has adjusted amounts reported previously in financial statements prepared in accordance with its old basis of accounting (previous GAAP).

(b) IAS 39 'Financial instruments: Recognition and Measurement'

As at 1 January 2005 and throughout 2005, the Company classified its financial assets and liabilities under IAS 39 as mentioned in note 1(e). The Company's investment securities are classified as AFS and stated at fair value, with any resultant gain or loss being directly recognised in equity, except for impairment losses. The fair value listed investments are their quoted bid prices at the balance sheet date. The fair value of unlisted investments are their bid prices as quoted by external brokers at the balance sheet date. Where these investments are interest-bearing with fixed maturity dates, interest is calculated using the effective interest rate method is recognised in the income statement. The financial impact as a result of this change in the accounting policy was not material and no adjustments were made to the opening balance sheet as at 1 January 2005. The comparative figures in these financial statements have not been adjusted as mentioned in note 1(c).