Direct Line Insurance Group plc
Preliminary results for the year ended 31 December 2016

7 March 2017

Financial highlights

- Gross written premium for Ongoing operations[1,2] up 3.9% to £3,274.1m (2015: £3,152.4m), driven by growth in Motor and Home own-brand in-force policies (up 4.3%)
- 2016 results reflect the one-off impact of using the new Ogden discount rate of minus 0.75%. Operating profit from Ongoing operations of £403.5m (pre-Ogden discount rate reduction[3]: £578.6m; 2015: £520.7m) and profit before tax of £353.0m (pre-Ogden[3]: £570.3m; 2015: £507.5m). Return on tangible equity[1, 2] of 14.2%, (pre-Ogden[3]: 20.2%; 2015: 18.5%)
- Combined operating ratio[1] from Ongoing operations of 97.7% (pre-Ogden[3]: 91.8%; 2015: 94.0%) increased as a result of the reduction in the Ogden discount rate, partially offset by improved current-year underwriting performance and favourable weather claims. Adjusted for normal weather and before the Ogden discount rate change, the combined operating ratio was 93.5%, towards the lower end of the target range of 93% to 95%
- 5.4% increase in final dividend per share to 9.7 pence per share, (2015: 9.2 pence). Total dividends per share for 2016, including special interim dividend of 10.0 pence per share paid in September 2016 following the approval of the Group's partial internal model, of 24.6 pence per share (2015: 50.1 pence)
- The Group's estimated Solvency II capital coverage ratio[4] post dividend is 165%, above the middle of the Group's risk appetite range of 140% – 180% (pre-dividend: 174%)

Strategic and operational highlights

- Direct Line Motor and Home new business growth at the highest annual level since IPO, demonstrating the success of the investment in brand, proposition and customer service
- Total costs for Ongoing operations of £923.7m broadly flat year on year before non-cash impairment charge of £39.3m, after absorbing £24.1m Flood Re levy and supporting growth in Motor and Home own brands
- Extended Home and Private Insurance partnership with RBS for a further three years, and implemented faster and easier sales journeys using cloud-based technology making connectivity and future change easier
- Invested in innovation, including partnership with PSA Peugeot Citroën for telematics extended for 4 more years, introducer role developed with Tesla, and MOVE_UK project brought into data collection stage
- Received approval from the Prudential Regulation Authority to use the Group's Solvency II partial internal model

Paul Geddes, CEO of Direct Line Group, commented

"2016 was a successful year for Direct Line Group and I'm proud of the strong own brand growth achieved in a switching market, proving our competitiveness in all our key categories and channels. This positions us well in a market disrupted by the reduction in the discount rate, and allows us to target a 93-95% combined operating ratio in 2017. We will continue to target improved efficiency and invest in customer and technology trends affecting our markets."

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Notes:
1. See glossary on page 42 for definitions.
2. See appendix A – Alternative performance measures on page 43 for reconciliation to financial statement line items.
3. See appendix B – Proforma results on page 46 which presents the Group's results excluding the recent impact of the Ogden discount rate reduction.
4. Estimates based on the Group's Solvency II partial internal model for 31 December 2016 and 30 June 2016.

Forward-looking statements disclaimer

Certain information contained in this document, including any information as to the Group's strategy, plans or future financial or operating performance, constitutes "forward-looking statements". These forward-looking statements may be identified by the use of forward-looking terminology, including the terms "aims", "anticipates", "aspire", "believes", "continue", "could", "estimates", "expects", "guidance", "intends", "may", "mission", "outlook", "plans", "predicts", "projects", "seeks", "should", "strategy", "targets" or "will" or, in each case, their negative or other variations or comparable terminology, or by discussions of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. They appear in a number of places throughout this document and include statements regarding the intentions, beliefs or current expectations of the Directors concerning, among other things: the Group's results of operations, financial condition, prospects, growth, strategies and the industry in which the Group operates. Examples of forward-looking statements include financial targets which are contained in this document specifically with respect to return on tangible equity, risk-based capital coverage ratio, the Group's combined operating ratio, prior-year reserve releases, cost reduction, investment income yield, net realised and unrealised gains, results from the run-off segment, restructuring and other one-off costs, and risk appetite range. By their nature, all forward-looking statements involve risk and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future or are beyond the Group's control.

Forward-looking statements are not guarantees of future performance. The Group's actual results of operations, financial condition and the development of the business sector in which the Group operates may differ materially from those suggested by the forward-looking statements contained in this document, for example directly or indirectly as a result of, but not limited to, UK domestic and global economic business conditions, the result of the referendum on the UK's withdrawal from the European Union, market-related risks such as fluctuations in interest rates and exchange rates, the policies and actions of regulatory authorities (including changes related to capital and solvency requirements or the Ogden discount rate), the impact of competition, currency changes, inflation and deflation, the timing impact and other uncertainties of future acquisitions, disposals, joint ventures or combinations within relevant industries, as well as the impact of tax and other legislation and other regulation in the jurisdictions in which the Group and its affiliates operate. In addition, even if the Group's actual results of operations, financial condition and the development of the business sector in which the Group operates are consistent with the forward-looking statements contained in this document, those results or developments may not be indicative of results or developments in subsequent periods.

The forward-looking statements contained in this document reflect knowledge and information available as of the date of preparation of this document. The Group and the Directors expressly disclaim any obligations or undertaking to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise, unless required to do so by applicable law or regulation. Nothing in this document should be construed as a profit forecast.

Inside Information

Prior to publication, this document contained inside information for the purposes of Article 7 of the European Union Regulation 596/2014.

Financial summary

	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Ongoing operations:				
In-force policies (thousands)			15,806	16,068
Gross written premium	1,661.0	1,600.4	3,274.1	3,152.4
Net earned premium	1,520.7	1,480.3	3,000.6	2,920.8
Underwriting (loss) / profit	(84.1)	22.0	70.1	175.2
Instalment and other operating income	86.9	78.0	165.3	150.8
Investment return	77.1	84.9	168.1	194.7
Operating profit – Ongoing operations	79.9	184.9	403.5	520.7
Run-off	3.0	34.8	26.6	73.1
Restructuring and other one-off costs	(9.6)	(8.3)	(39.9)	(48.7)
Operating profit	73.3	211.4	390.2	545.1
Finance costs	(18.8)	(18.9)	(37.2)	(37.6)
Profit before tax	54.5	192.5	353.0	507.5
Tax	(11.6)	(39.9)	(74.2)	(108.3)
Profit from discontinued operations, net of tax	–	–	–	181.2
Profit after tax	42.9	152.6	278.8	580.4
Of which Ongoing operations	48.8	132.4	293.0	385.3
Key metrics – Ongoing operations				
Loss ratio – prior to reduction in Ogden discount rate[1]	56.7%	64.6%	55.0%	59.5%
Loss ratio – reduction in Ogden discount rate	11.5%	-	5.9%	-
Commission ratio[1]	12.0%	10.3%	11.5%	10.9%
Expense ratio[1] including Flood Re levy	25.3%	23.6%	25.3%	23.6%
Combined operating ratio[1]	105.5%	98.5%	97.7%	94.0%
Adjusted diluted earnings per share [2] (pence)			21.2	26.6
Return on tangible equity[2]			14.2%	18.5%
Key metrics				
Investment income yield[2]			2.5%	2.4%
Investment return[2]			2.6%	2.9%
Basic earnings per share [2] (pence)			20.4	27.9
Return on equity			10.8%	21.3%
Dividend per share – interim (pence)			4.9	4.6
– final interim (pence)			9.7	9.2
– regular (pence)			14.6	13.8
– first special interim[3] (pence)			10.0	27.5
– second special interim (pence)			-	8.8
– total (pence)			24.6	50.1
Net asset value per share (pence)			184.7	192.2
Tangible net asset value per share (pence)			147.4	153.8

	FY 2016	HY 2016
Capital coverage[4] – estimated	165%	184%

Notes:
1. A reduction in the ratio represents an improvement and positive change as a proportion of net earned premium, while an increase in the ratio represents a deterioration and negative change.
2. See glossary on page 42 for definitions and appendix A – Alternative performance measures on page 43 for reconciliation to financial statement line items.
3. The special interim dividend paid on 24 July 2015 of 27.5 pence per share, following the sale of the Group's former Italian and German operations.
4. See note 4 on page 1 and adjusted for dividends.
5. See appendix B – Proforma results on page 46 which presents the Group's results excluding the recent impact of the Ogden discount rate reduction.

Business update

Overview

Direct Line Group (the "**Group**") had a successful 2016, absorbing a reduction in the discount rate applicable to personal injury lump sum damages awards to minus 0.75% (the "**Ogden discount rate**") and the Flood Re levy, while at the same time investing in the business and making progress on implementing its strategy. The Group's investment in its direct brands, competitiveness on price comparison websites ("**PCWs**") and partnership capabilities are bearing fruit.

On 27 February 2017, the Lord Chancellor announced a reduction in the Ogden discount rate to minus 0.75% from 20 March 2017, and that a consultation would be launched across the industry before Easter 2017 to consider options for reform. The Ogden discount rate is used to calculate lump sum settlements of bodily injury claims, including awards for recurring costs such as loss of earnings and ongoing medical care. The Group has previously held a provision in claims reserves for the risk of a change in the Ogden discount rate to 1.5%, compared to the previous actual rate of 2.5%. As a result of the announcement, the Group has increased this provision for the estimated impact of moving to a minus 0.75% Ogden discount rate, for all business earned up to 31 December 2016. The Group continues to hold a significant margin above the actuarial best estimate and after this adjustment, the Group's overall reserving strength has been maintained as a result of reflecting the Ogden discount rate change to minus 0.75%.

As a result of the recent reduction in the Ogden discount rate, operating profit from Ongoing operations for 2016 has reduced by £175.1 million; the combined operating ratio ("**COR**") from Ongoing operations has increased by 5.9 percentage points, mostly relating to 2015 and prior years business, with minimal impact of 0.4 percentage points relating to the 2016 accident year; profit before tax has reduced by £217.3 million; and return on tangible equity has reduced by 6.0 percentage points. Appendix B presents the Group's results excluding the one-off impact of the recent Ogden discount rate reduction.

Operating profit from Ongoing operations was £403.5 million (pre-Ogden: £578.6 million; 2015: £520.7 million) and Group profit before tax was £353.0 million, (pre-Ogden: £570.3 million; 2015: £507.5 million). The COR for Ongoing operations was 97.7% (pre-Ogden: 91.8%; 2015: 94.0%), which benefited from lower weather losses (£18 million compared to £90 million in 2015), partially offset by a £39.3 million non-cash impairment charge to intangible assets and £24.1 million Flood Re levy (2015: £nil). The current-year attritional loss ratio improved to 69.2% (pre-Ogden: 68.8%; 2015: 69.4%) as a result of improvements in Motor and Commercial. Prior-year reserve releases from Ongoing operations were lower at £266.7 million (pre-Ogden £429.6 million; 2015: £378.9 million).

The Motor division grew in-force polices 4.5% in the year and improved its current-year attritional loss ratio by 0.9 percentage points after the impact of the recent change to the Ogden discount rate. Overall claims inflation was at the top of long-term expectations driven by slightly higher than expected damage costs.

In Home, the Group was also able to grow its own brand in-force policies by 2.3% in 2016, although this was more than offset by the continuing fall in in-force policies in the partnership channel. Strong propositions, such as the introduction of 3 hour emergency plumbing services for Home Plus customers this year and improved competitiveness on PCWs helped drive the growth in own brand policies. Claims inflation was also slightly above long-term expectations.

The Commercial business grew its Direct Line for Business in-force policies by 6.4% and continued to demonstrate the attractiveness of the Direct Line brand in this customer segment. Meanwhile the broker business, under the NIG brand, made further progress in underwriting performance while also stabilising its in-force policies.

Total costs from Ongoing operations remained flat compared to 2015 before £39.3 million of non-cash impairment of intangible assets as the Group supported the growth in its own brands policies and also absorbed £24.1 million of additional costs in relation to the Flood Re levy. The non-cash impairment related to ongoing IT projects which aim to enhance the Group's digital offering, customer experience and operational efficiency.

Investment income was in line with expectations at 2.5% income yield with net realised and unrealised gains of £3.6 million, lower than prior year mainly due to lower unrealised investment property gains of £4.1 million (2015: £24.2 million).

Strategic priorities

The Group's strategy is to make insurance much easier and better value for our customers. This strategy is set out across three pillars: to be a great retailer; to be a smart and efficient manufacturer; and to lead and disrupt the market. These pillars are supported by the key enablers of data and technology, culture and capability and capital and risk management.

During the year, the Group delivered a number of initiatives which benefited customers in 2016 while building capability for the future.

Great retailer

The differentiation of the Group's brands remained a key focus in 2016. For Direct Line, the Group has built strong foundations since the 'reboot' of the brand just over two years ago, introducing a succession of effectively marketed product enhancements. This year a three-hour emergency plumbing service was added for Home Plus customers. Strong marketing and branding is key to clearly articulating these enhancements to customers so they want to deal directly with the Group. The success of marketing to drive Direct Line growth was recognised when the Group won the Gold IPA award for marketing effectiveness.

The strength of the Direct Line brand is not limited to the personal lines sector. With more small businesses looking for reliable and easy to use direct insurance, Direct Line for Business continued to grow strongly in the year, highlighting the value of this brand asset.

The Group's effectiveness on PCWs via the Churchill and Privilege brands has also increased, particularly in Home as the customer journey has been improved. This contributed to strong new sales growth through this channel.

The Churchill brand was strengthened with the launch of a 'Lollipoppers' campaign and new Lollipop men and women have been recruited nationwide. The Churchill Motor free rescue campaign was re-launched, differentiating this brand and leveraging the Group's Rescue capabilities at the same time.

The Green Flag brand continued to perform well. Green Flag's app was enhanced with Green Flag 'Alert Me' and 'Rescue Me', providing the capability for rescue customers to monitor the health of their car and to improve their rescue experience.

Smart and efficient manufacturer

The Group's underlying costs (excluding higher non-cash impairment of intangible assets than in recent years) were stable compared to 2015, having absorbed the £24.1 million Flood Re levy and still supporting 4.3% in-force policy growth in Motor and Home own brands. Excluding the impairment, H2 2016 costs were lower than H2 2015, primarily due to lower claims handling expenses.

In Partnerships, the Home and Private Insurance arrangement with RBS was extended for a further three years and the Travel insurance contract with Nationwide Building Society was extended until the end of 2018.

The Group agreed an extension of its Home and Motor insurance partnership with Prudential for a further two years. As part of this, policies will be renewed under the Prudential brand until 2019. The Group also launched its first affinity partnership scheme to offer access to Churchill-branded Home and Motor policies for Prudential Group customers who do not currently have such insurance with the Group. This partnership demonstrates the Group's ability to deliver tailored propositions to meet the needs of partners and their customers.

The Group increased the number of accident repair centres it owns to 18 in 2016, strengthening its ability to control indemnity spend and improve customer experience.

Lead and disrupt the market

The Group continued to build on its strong market position by identifying and investing in market developments that it believes can contribute to future growth.

The Group has extended its motor insurance partnership with PSA Finance UK (part of the Peugeot Citroën Group) for a further four years. The partnership has found success by packaging insurance with car finance to create innovative mobility solutions for consumers, particularly young or inexperienced drivers through the use of telematics in the Peugeot Just Add Fuel and Citroën Simplydrive offers. Extending the partnership allows the Group to create propositions based on the technology fitted to the car.

The Group is working with Tesla to understand the role advanced technology and driving aids can play in enhancing road safety and therefore insurance. In 2017 Tesla became an introducer Appointed Representative to be able to refer customers to Direct Line to insure their Tesla.

In 2016, the Group joined a partnership called MOVE_UK with the UK government, technology providers and car manufacturers to accelerate the development, market readiness and deployment of Automated Driving Systems ("ADS"). With ADS systems observing and recording in the background while MOVE_UK vehicles are driven normally, this is a unique opportunity to learn how ADS technology would respond in real life situations.

In Commercial, the Group continued to be recognised for its leading capabilities in eTrade and direct Commercial insurance, both of which are expected to continue to grow.

Key enablers

Alongside the strategic pillars, the Group's ongoing areas of focus include developing future capability and managing the risks associated with IT systems' stability and cyber security. Technology remains at the heart of the Group's operations and the focus is on upgrading the Group's IT systems and capabilities, aimed at improving the digital offering, customer experience and operational efficiency. While progress has been made in each of the three areas, implementation and integration of a range of new IT systems is inherently complex and challenging. The Group remains focused on adopting the right capabilities and will take the time necessary to do so.

The Group has made progress improving the performance of the core infrastructure during the year, supporting its people in performing their roles more effectively.

During the year the Group continued to invest in employees' skills to improve effectiveness and customer experiences. The Group is committed to broadening the diversity of its talent pool and this year signed up to the Women in Finance Charter, seeking to increase the number of women in senior roles in the organisation. In addition, a new graduate scheme and apprentice recruitment drive were launched to build a stronger organic talent pool.

The Group also launched a major new training programme for its people, designed to help flex their approaches to improve engagement with customers. Not only has this strengthened front office staff skills, as they handle customers in often difficult situations, but it has also strengthened the way people interact with one another. This has in turn helped the engagement rate to continue to improve through the year from an already improved level in 2015.

During 2016, the Group received approval from the Prudential Regulation Authority ("**PRA**") to use the Partial Internal Model ("**PIM**"), successfully concluding a multi-year project. The model is at the centre of the Group's risk management framework and is now used to report its Solvency II capital coverage.

The Group has used the PIM to establish a capital risk appetite target range which provides additional security over the regulatory solvency capital requirement (**"SCR"**).

The Group was well prepared for the UK's referendum on leaving the EU and has actively managed the impacts from the subsequent volatile financial markets. The Group is a UK-based business underwriting risk within the UK, and the day-to-day operations remain largely unaffected. The Group continues to monitor the consequences of the devaluation of Sterling and uncertain financial markets.

Dividends and capital management

The Board is proposing a final dividend of 9.7 pence per share, an increase of 5.4%, making a total regular dividend for 2016 of 14.6 pence per share. This represents 5.8% growth over the 2015 regular dividend and is in line with the Group's aim to grow the regular dividend annually in real terms.

The Board has considered the risk appetite range of the Group under its Solvency II PIM and considers that the appropriate range, which should enable it to meet its operational, regulatory and rating agency requirements, is 140% to 180% of its SCR.

After deducting the final dividend, the Group's estimated Solvency II capital coverage ratio was 165%.

Regulatory update

On 27 February 2017, the Lord Chancellor announced a reduction in the Ogden discount rate to minus 0.75% with effect from 20 March 2017, which has led to an increase in the amount of claims reserves necessary to be held by the Group, specifically those that are settled as lump sums by the Courts. This follows a consultation process instigated by the Ministry of Justice some years ago in connection with the rate to be applied to personal injury lump sum damages awards in settling such claims. The Group is committed to ensuring claimants receive appropriate compensation and has made appropriate provision in its claims reserves for the ruling, which will apply to all open unsettled claims. The Lord Chancellor's announcement referred to a consultation to consider options for reform concerning the discount rate and accordingly has left open the possibility of further changes to the process by which the rate is set, and therefore to the rate itself. The Group welcomes the consultation to consider options for reform, with a view to achieving a better and fairer framework for claimants and defendants.

On 23 February 2017, the Government announced measures to reduce the volume and cost of soft tissue damage 'whiplash' claims and stated its expectation that this will see a reduction in motor insurance premiums by £40 on average. The measures include a fixed tariff for payment of injuries up to 24 months in duration. Further measures detailed in the paper are still being considered. The Government is keen to introduce all changes to whiplash claims as a package in late 2018. The Group has been calling for reform in this area for some time and continues to work with Government and industry bodies on how the reforms should be implemented.

On 16 January 2017 the Financial Services Compensation Scheme announced that it would raise a supplementary levy of £63 million on general insurers to compensate policyholders of the Enterprise and Gable Insurance companies. The Group's share of the levy, approximately £5 million for 2017, will be charged to operating expenses in Q1 2017.

From 1 April 2016, Flood Re, the Government and industry-backed scheme to provide affordable home insurance to households at high risk of flooding, became operational. The Group has supported Flood Re's formation and was ready to cede chosen risks to Flood Re on its inception.

Outlook

The Group's markets were highly competitive and faced a number of significant government policy and regulatory changes during 2016 and in early 2017. In the face of these challenges, the Group demonstrated both its resilience and its appeal to customers by growing its own brands policies while maintaining overall margins, which has continued into early 2017. The Group does not expect any material residual impact on 2017 profit as a result of adopting the reduction in the Ogden discount rate to minus 0.75%.

The Group aims to reduce its expense ratio during 2017, absorbing its investment in future capability. The Group also aims to deliver a lower commission ratio during 2017, normalised for major weather events; this will in part reflect changes in its distribution channel mix. Over the longer term, the Group aims to achieve further reductions in both the expense and commission ratios.

For 2017, the Group targets achieving a COR in the range of 93% to 95% for Ongoing operations, assuming a normal annual level of claims from major weather events and no further change to the Ogden discount rate. In addition, the Group reiterates its ongoing target of achieving at least a 15% return on tangible equity ("**RoTE**").

Finance review

Performance

Operating profit – Ongoing operations

	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Underwriting profit / (loss)	(84.1)	22.0	70.1	175.2
Instalment and other operating income	86.9	78.0	165.3	150.8
Investment return	77.1	84.9	168.1	194.7
Operating profit	79.9	184.9	403.5	520.7

In 2016, operating profit from Ongoing operations was £403.5 million (pre-Ogden: £578.6 million; 2015: £520.7 million) primarily due to a lower underwriting result as the Group has reflected an increase in its claims reserves for the recent reduction in the Ogden discount rate, and lower investment returns. The underwriting profit was £70.1 million, (2015: £175.2 million), principally due to the recent reduction in the Ogden discount rate, which led to lower prior-year reserve releases from Ongoing operations of £266.7 million (2015: £378.9 million). This was partially offset by lower claims costs from major weather events. Expenses include higher non-cash impairments than in previous years of £39.3 million and the Flood Re levy of £24.1 million. Investment return was lower primarily due to a reduction in unrealised property gains.

Operating profit from Ongoing operations for the second half of 2016 was £79.9 million (pre-Ogden: £255.0 million; 2015: £184.9 million). The decrease in operating profit was driven by the recent reduction in the Ogden discount rate and a lower investment return, partially offset by lower claims costs from major weather events and an increase in instalment and other operating income.

In-force policies and gross written premium

In-force policies – Ongoing operations (thousands)

As at	31 Dec 2016	30 Sep 2016	30 Jun 2016	31 Mar 2016	31 Dec 2015
Own brands	3,642	3,607	3,541	3,487	3,459
Partnerships	231	233	238	244	248
Motor total	3,873	3,840	3,779	3,731	3,707
Own brands	1,759	1,751	1,743	1,729	1,719
Partnerships	1,619	1,638	1,660	1,677	1,699
Home total	3,378	3,389	3,403	3,406	3,418
Of which Nationwide and Sainsbury's	719	723	724	724	719
Rescue	3,646	3,621	3,670	3,805	3,932
Other personal lines	4,234	4,219	4,224	4,275	4,356
Rescue and other personal lines	7,880	7,840	7,894	8,080	8,288
Direct Line for Business	433	428	424	419	407
NIG and other	242	239	236	234	248
Commercial	675	667	660	653	655
Total	15,806	15,736	15,736	15,870	16,068

Total in-force policies for Ongoing operations during 2016 reduced by 1.6% to 15.8 million (31 December 2015: 16.1 million). The fall primarily related to lower partner volumes in Home and Rescue and other personal lines. Motor in-force policies grew by 4.5% and Commercial by 3.1% across the period. Own brands in-force policies in 2016 grew by 4.3% including a 5.3% increase in Motor.

Gross written premium – Ongoing operations

	Q4 2016 £m	Q4 2015 £m	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Own brands	333.3	308.9	734.4	672.3	1,428.7	1,307.5
Partnerships	24.0	24.6	54.4	51.1	110.4	99.2
Motor total	357.3	333.5	788.8	723.4	1,539.1	1,406.7
Own brands	100.1	99.9	213.1	214.5	404.7	408.4
Partnerships	105.2	112.8	218.1	234.0	429.7	457.9
Home total	205.3	212.7	431.2	448.5	834.4	866.3
Of which Nationwide and Sainsbury's	54.1	56.3	110.5	114.6	215.5	221.2
Rescue	34.9	36.2	81.2	82.7	163.1	163.3
Other personal lines	60.2	57.2	121.9	116.6	237.7	230.8
Rescue and other personal lines	95.1	93.4	203.1	199.3	400.8	394.1
Direct Line for Business	27.1	24.7	56.6	52.8	109.6	101.8
NIG and other	93.3	91.6	181.3	176. 4	390.2	383.5
Commercial	120.4	116.3	237.9	229.2	499.8	485.3
Total	778.1	755.9	1,661.0	1,600.4	3,274.1	3,152.4

Gross written premium of £3,274.1million increased by 3.9% compared with 2015 (£3,152.4 million) primarily related to an increase in Motor own brands.

Motor

Motor in-force policies increased by 4.5% during 2016, driven primarily by own brands. Overall, Motor gross written premium increased by 9.4% in comparison to 2015.

The market experienced high levels of shopping during 2016. The Direct Line brand was able to use this environment to continue to improve its competitive position, resulting in strong new business growth. The comparatively high level of persistency and attractive customer base allowed the Group to reinvest some of that value back into propositions and price competitiveness.

Motor average written premiums[1] increased by 6.3% in 2016 compared with an average increase of 5.2% in 2015. As demonstrated by the improving current year loss ratio, the Group was able to continue to write business at attractive margins, as a result of successful pricing and a slightly improved risk mix. Claims inflation remained at the top of the Group's long-term expectation of 3%-5%, driven by higher damage costs.

Home

In-force policies for Home own brands increased by 2.3% to 1.8 million over 2016, while partner in-force policies reduced by 4.7%. Gross written premium was 3.7% lower than in 2015 primarily due to partnerships which were 6.2% lower, while own brands experienced a smaller reduction of 0.9%. In Q4 2016, Home own brands gross written premium grew year on year to £100.1 million (Q4 2015: £99.9 million).

Following a prolonged period of significant deflation, the home market showed signs of some stability during the second half of 2016. Home's average written premium[2] decreased by 3.9% in 2016 compared with 3.6% in 2015, primarily due to changes to tenure and distribution channel mix, including higher sales through the PCW channel. Home market new business premiums improved during the year after years of premium deflation. New business pricing for the Group's Home own brands was sufficiently competitive to allow the Home division to continue to grow own brands through web and aggregator channels.

Note:

1. Average incepted written premiums excluding IPT for total Motor for year to date 31 December 2016
2. Average incepted written premiums excluding IPT for Home own brands for year to date 31 December 2016

The Group's partnership with Nationwide Building Society was due to terminate in June 2017. These plans are currently being reviewed which may result in the migration moving to the second half of 2017, whilst the Group works with Nationwide to ensure a smooth transition for customers. If this is the case, the Group will continue to earn premiums written in the second half of 2017 through to the second half of 2018.

Rescue and other personal lines

Gross written premium for Rescue and other personal lines grew by 1.7% compared with 2015. Rescue gross written premium remained broadly stable compared with 2015. Green Flag performed well, supported by competitive propositions. Gross written premium for other personal lines grew by 3.0% compared to 2015. The reduction in in-force policies for other personal lines of 2.8% across 2016 primarily reflects lower packaged bank account volumes.

Commercial

Commercial in-force policy growth across 2016 was achieved by increased sales through Direct Line for Business and NIG. By 31 December 2016, there were more than 433,000 Direct Line for Business in-force policies. Commercial gross written premium increased by 3.0% to £499.8 million compared to 2015, reflecting growth in Commercial direct, particularly landlord and van products. Gross written premium for NIG and other increased by 1.7% compared to 2015, in part reflecting premium rate increases.

Underwriting profit – Ongoing operations

	H2 2016	H2 2015	FY 2016	FY 2015
Underwriting profit / (loss) (£ million)	**(84.1)**	22.0	**70.1**	175.2
Loss ratio	**68.2%**	64.6%	**60.9%**	59.5%
Commission ratio	**12.0%**	10.3%	**11.5%**	10.9%
Expense ratio	**25.3%**	23.6%	**25.3%**	23.6%
COR	**105.5%**	98.5%	**97.7%**	94.0%

The COR for Ongoing operations of 97.7% (2015: 94.0%), was 3.7 percentage points higher year on year primarily as a result of the recent Ogden discount rate reduction, partially offset by lower weather losses. The loss ratio was 60.9% (pre-Ogden: 55.0%; 2015: 59.5%) which was higher by 1.4 percentage points compared to 2015. The commission ratio increased by 0.6 percentage points and the expense ratio by 1.7 percentage points. Excluding the impact of the recent reduction in the Ogden discount rate, the COR for Ongoing operations improved to 91.8% in 2016.

At the start of the year, the Group set 2016 COR guidance for Ongoing operations in the range of 93% to 95%. This assumed a normal level of claims from major weather events. On this basis and excluding the recent Ogden discount rate reduction, the Group achieved a normalised COR of 93.5% which is towards the lower end of the Group's target range. This also includes a non-cash intangible asset impairment charge of £39.3 million.

Within the loss ratio, the current-year attritional loss ratio improved by 0.2 percentage points to 69.2% (pre-Ogden: 68.8%; 2015: 69.4%) with improvements in Motor and Commercial offset by a deterioration in Home and Rescue and other personal lines.

The increase in the commission ratio of 0.6 percentage points to 11.5% primarily reflected higher payments to partners, particularly in Home, following lower claims costs as a result of prior-year reserve releases and major weather events.

The Group's expense ratio increased to 25.3%, predominantly due to higher non-cash intangible asset impairments of £39.3 million and the Flood Re levy of £24.1 million. Excluding the impairment charge and Flood Re levy, the expense ratio would have been 23.2%.

Loss ratio analysis by division – Ongoing operations

	Notes	Motor £m	Home £m	Rescue and other personal lines £m	Commercial[1] £m	Total Ongoing £m
For the year ended 31 December 2016						
Net insurance claims	3	1,001.7	332.0	243.0	250.5	1,827.2
Prior-year reserve releases	18	123.5	75.9	17.5	49.8	266.7
Major weather events		n/a	(18.0)	n/a	n/a	(18.0)
Attritional net insurance claims		1,125.2	389.9	260.5	300.3	2,075.9
Net earned premium	3	1,337.1	816.3	394.4	452.8	3,000.6
Loss ratio - current-year attritional		84.1%	47.8%	66.0%	66.3%	69.2%
Loss ratio - prior-year reserve releases		(9.2%)	(9.3%)	(4.4%)	(11.0%)	(8.9%)
Loss ratio - major weather events – Home[2]		n/a	2.2%	n/a	n/a	0.6%
Loss ratio - reported	3	74.9%	40.7%	61.6%	55.3%	60.9%
Commission ratio	3	3.2%	22.6%	7.2%	19.5%	11.5%
Expense ratio	3	28.2%	21.7%	24.5%	23.9%	25.3%
COR	3	106.3%	85.0%	93.3%	98.7%	97.7%
For the year ended 31 December 2015						
Net insurance claims	3	794.8	435.1	231.6	275.8	1,737.3
Prior-year reserve releases	18	266.8	41.9	13.6	56.6	378.9
Major weather events		n/a	(90.0)	n/a	n/a	(90.0)
Attritional net insurance claims		1,061.6	387.0	245.2	332.4	2,026.2
Net earned premium	3	1,249.3	845.0	386.4	440.1	2,920.8
Loss ratio - current-year attritional		85.0%	45.8%	63.5%	75.5%	69.4%
Loss ratio - prior-year reserve releases		(21.4%)	(5.0%)	(3.6%)	(12.8%)	(13.0%)
Loss ratio - major weather events – Home[2]		n/a	10.7%	n/a	n/a	3.1%
Loss ratio - reported	3	63.6%	51.5%	59.9%	62.7%	59.5%
Commission ratio	3	2.6%	20.9%	6.4%	19.6%	10.9%
Expense ratio	3	26.2%	19.8%	24.9%	22.2%	23.6%
COR	3	92.4%	92.2%	91.2%	104.5%	94.0%

Notes:

1. Commercial attritional loss ratio includes weather claims costs.
2. Home claims for major weather events, including inland and coastal flooding and storms.

The movement in the current-year attritional loss ratio is a key indicator of underlying accident year performance as it excludes prior-year reserve movements and claims from major weather events. The Group's current-year attritional loss ratio improved by 0.2 percentage points to 69.2% in 2016 (2015: 69.4%) with improvements in Motor and Commercial partially offset by a deterioration in Home and Rescue and other personal lines. Excluding the impact of the recent reduction in the Ogden discount rate, the current-year attritional loss ratio for Ongoing operations improved to 68.8% in 2016.

By division, the COR improved in Home and Commercial, mainly as a result of benign weather compared to 2015. The COR deteriorated in Motor due to the recent Ogden discount rate change and an intangible asset impairment charge of £39.3 million.

Motor

The COR for the Motor division was 106.3% (2015: 92.4%), including an 11.2 percentage points one-off increase due to the recent reduction in the Ogden discount rate. Prior-year reserve releases were significantly lower at £123.5 million (2015: £266.8 million), including a £139.8 million charge in respect of the recent Ogden discount rate change. The expense ratio increased due to higher non-cash intangible asset impairments of £39.3 million. The commission ratio remained broadly stable compared to 2015.

The current-year attritional loss ratio improved by 0.9 percentage points to 84.1% (2015: 85.0%). Excluding the impact of the recent reduction in the Ogden discount rate, the current-year attritional loss ratio for Motor was 83.3%, an improvement of 1.7 percentage points compared to 2015. Growth in average premiums, coupled with improving claims trends in large bodily injury, were partially offset by higher than expected damage inflation and the Group's investment in new business growth. Operating profit was £149.1 million, lower than 2015 primarily as a result of a one-off charge due to the reduction in the Ogden discount rate of £150.3 million and higher intangible asset impairments of £39.3 million.

Home

In Home, the COR improved by 7.2 percentage points primarily as a result of a lower loss ratio, which was 10.8 percentage points lower than 2015. The impact of major weather events in 2016 was approximately £18 million (2015: £90 million) and was lower than the normal annual level of claims costs expected from major weather events of approximately £70 million. Prior-year reserve releases, which included favourable development from the storms in late 2015, were higher than last year at £75.9 million (2015: £41.9 million).

The current-year attritional loss ratio, excluding claims costs from major weather events, was 2.0 percentage points higher than 2015. This was predominantly driven by a greater proportion of new business sales compared to 2015 and an increase in claims inflation.

Rescue and other personal lines

The COR for Rescue and other personal lines was 2.1 percentage points higher than 2016 at 93.3% (2015: 91.2%). The Rescue COR was 83.4% (2015: 82.3%) with a higher loss ratio reflecting changes in business mix and investment in the network. The commission ratio of 7.2% was 0.8 percentage points higher than 2015, reflecting higher partner profit share, while the expense ratio was stable compared to 2015.

Commercial

The Commercial COR of 98.7% was 5.8 percentage points lower compared to 2015. This benefited from lower weather-related claims costs, which were offset by the impact of the recent Ogden discount rate change.

Operating profit was therefore £41.8 million, an increase of £21.0 million compared to 2015. The reduction due to the recent change in the Ogden discount rate was £24.7 million, of which £23.1 million relates to 2015 and prior accident years. The current-year attritional loss ratio was 9.2 percentage points lower than 2015 due to lower weather-related claims costs and over 1 percentage point of underlying improvement due to better pricing and risk selection.

Total costs – Ongoing operations

	Notes	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Staff costs		197.4	203.9	406.5	407.5
Other operating expenses		132.9	131.0	277.8	261.3
Marketing		50.0	59.2	112.6	117.8
Depreciation		15.1	15.8	30.1	30.7
Amortisation and impairment of other intangible assets		66.7	36.5	96.7	67.4
Total costs		462.1	446.4	923.7	884.7
Operating expenses	10	384.7	349.4	759.3	689.1
Claims handling expenses	8	77.4	97.0	164.4	195.6
Total costs		462.1	446.4	923.7	884.7

Total costs for Ongoing operations were £923.7 million (2015: £884.7 million), after non-cash intangible asset impairments of £39.3 million and the Flood Re levy of £24.1 million. The impairments are in respect of intangible assets previously capitalised on the balance sheet and primarily relate to ongoing IT projects which aim to enhance the Group's digital offering, customer experience and operational efficiency. Consequently, the Group's expense ratio increased to 25.3% (2015: 23.6%). Excluding the impairment charge and Flood Re levy the expense ratio would have been 23.2%. The reduction in claims handling expenses was largely due to lower staff costs and other operating costs being allocated to claims and a reduction in claims handling provision.

Costs in the second half of 2016 were higher than in the second half of 2015. Excluding the non-cash impairment, costs were lower in the second half of 2016, primarily due to lower claims handling expenses.

Instalment and other operating income – Ongoing operations

	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Instalment income	55.7	51.7	107.1	100.1
Other operating income:				
Vehicle replacement referral income	7.3	6.7	14.1	12.5
Revenue from vehicle recovery and repair services[1]	9.9	7.9	19.3	15.5
Other income	14.0	11.7	24.8	22.7
Other operating income	31.2	26.3	58.2	50.7
Total	86.9	78.0	165.3	150.8

Instalment and other operating income from Ongoing operations of £165.3 million increased 9.6% on the prior year (2015: £150.8 million). Instalment income increased by £7.0 million compared to 2015, primarily as a result of higher Motor volumes. Other operating income increased £7.5 million in 2016 to £58.2 million (2015: £50.7 million).

Investment return – Ongoing operations

	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Investment income	81.8	82.6	164.5	165.6
Net realised and unrealised gains / (losses)	(4.7)	2.3	3.6	29.1
Total investment return	77.1	84.9	168.1	194.7

The total investment return for Ongoing operations decreased to £168.1 million compared to £194.7 million in 2015. The decrease is primarily as a result of lower net realised and unrealised gains. Investment income remained broadly stable at £164.5 million compared with 2015, despite lower average assets under management of £6,581.0 million (2015: £6,818.7 million) and a reduction of 25 basis points by the Bank of England in the UK base rate during the year. These downward factors were partially offset by portfolio actions.

Net realised and unrealised gains for Ongoing operations of £3.6 million were significantly lower than the comparative period (2015: £29.1 million) primarily due to lower unrealised property gains, which were £4.1 million for the year (2015: £24.2 million).

Investment yields

	FY 2016	FY 2015
Investment income yield[2]	2.5%	2.4%
Investment return[2]	2.6%	2.9%

The investment income yield in 2016 was 2.5%, an increase on the yield achieved in 2015. Actions to diversify the portfolio including investment in commercial real estate loans, subordinated financial debt and global credit, have helped offset yield pressure from low UK interest rates. The Group currently forecasts an investment income yield of 2.4% for 2017 on the basis of current market conditions given the continuing low interest rate environment.

Notes:

1. Vehicle recovery includes post-accident and pay-on-use recovery. Repair services constitute the provision of non-insurance related repairs services.
2. See glossary on page 42 for definition.

Investment holdings and yields – total Group

As at	31 Dec 2016 £m	30 Jun 2016 £m	31 Dec 2015 £m
Investment-grade credit[1]	3,888.3	3,704.8	4,060.0
High yield	409.9	358.9	327.4
Investment-grade private placements	85.1	60.0	13.5
Credit	**4,383.3**	4,123.7	4,400.9
Securitised credit[1,2]	–	317.5	350.8
Sovereign	341.2	456.6	442.7
Total debt securities	**4,724.5**	4,897.8	5,194.4
Infrastructure debt	337.0	342.7	329.6
Commercial real estate loans	79.7	17.7	–
Cash and cash equivalents[3]	1,110.8	989.7	947.3
Investment property	329.0	348.6	347.4
Total Group	**6,581.0**	6,596.5	6,818.7

At 31 December 2016, total investment holdings of £6,581.0 million were 3.5% lower than at 31 December 2015, reflecting dividends paid offset by operating cash flows. Total debt securities were £4,724.5 million (31 December 2015: £5,194.4 million), of which 6.1% were rated as 'AAA' and a further 63.8% were rated as 'AA' or 'A'. The average duration at 31 December 2016 of total debt securities was 2.3 years (31 December 2015: 2.3 years).

As part of the on-going review of investment strategy a decision was taken to exit securitised credit during Q3 2016. In addition the Group sold two investment properties during 2016.

At 31 December 2016, total unrealised gains, net of tax, on available-for-sale ("**AFS**") investments were £92.1 million (31 December 2015: £5.4 million).

In 2016, the Group delivered a robust investment result against a background of increased financial market uncertainties and further yield compression for much of the year. Investment in three new mandates commenced with two fully funded to benchmark holdings (subordinated financial debt and global credit). The commercial real estate loans mandate is expected to be fully funded to its benchmark holding by the end of 2017.

Derivatives are permitted only for risk mitigation and efficient portfolio management within the investment portfolio. Derivatives used include interest rate swaps, for example to hedge exposure to US Dollar interest rate movements, and forward currency contracts to hedge assets denominated in foreign currency back to Sterling. Separately, interest rate swaps have also been used to change the interest rate liability on the Group's debt issuance to a floating rate basis.

Operating profit / (loss) – Ongoing operations

	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Motor	(19.7)	157.0	149.1	338.0
Home	65.2	5.5	166.7	109.9
Rescue and other personal lines	22.5	25.6	45.9	52.0
Commercial	11.9	(3.2)	41.8	20.8
Total Ongoing	**79.9**	184.9	**403.5**	520.7

All divisions were profitable in 2016, with Home and Commercial reporting significant improvements in operating profit compared to 2015. This was partially offset by a decrease in Motor, due to the recent reduction in the Ogden discount rate and a higher level of intangible asset impairments, and in Rescue and other personal lines.

Notes:

1. Asset allocation at 31 December 2016 includes investment portfolio derivatives, which have been netted and have a mark-to-market liability value of £5.8m included in investment-grade credit (31 December 2015: mark-to-market liability value of £45.7m, of which £40.4m included in investment-grade credit and £5.3m in securitised credit). This excludes non-investment derivatives that have been used to hedge interest on subordinated debt, operational cash flows and the disposal of the International division in 2015.
2. Securitised credit was disposed of during 2016.
3. Net of bank overdrafts, includes cash at bank and in hand and money market funds with no notice period for withdrawal (31 December 2015: also included money market funds with maturities greater than three months).

Reconciliation of operating profit

	H2 2016 £m	H2 2015 £m	FY 2016 £m	FY 2015 £m
Operating profit – Ongoing operations	79.9	184.9	403.5	520.7
Run-off	3.0	34.8	26.6	73.1
Restructuring and other one-off costs	(9.6)	(8.3)	(39.9)	(48.7)
Operating profit	73.3	211.4	390.2	545.1
Finance costs	(18.8)	(18.9)	(37.2)	(37.6)
Profit before tax	54.5	192.5	353.0	507.5
Tax	(11.6)	(39.9)	(74.2)	(108.3)
Profit from discontinued operations, net of tax	–	–	–	181.2
Profit after tax	42.9	152.6	278.8	580.4

Run-off
The Run-off segment generated a profit of £26.6 million in 2016 (pre-Ogden: £68.8 million; 2015: £73.1 million). The reduction in the result followed lower prior-year reserve releases from large bodily injury claims in comparison to the previous year, primarily as a result of the recent reduction in the Ogden discount rate.

Restructuring and other one-off costs
Restructuring and other one-off costs for 2016 of £39.9 million (2015: £48.7 million) primarily reflected costs associated with the exit of the Group's Bristol property and relocating to a smaller site. Over the four-year period 2015 to 2018, the Group expects cumulative restructuring and other one-off costs to be substantially offset by the operating profit from the Run-off segment.

Finance costs
Finance costs remained stable at £37.2 million (2015: £37.6 million).

Taxation
The effective tax rate in 2016 was 21.0% (2015: 21.3%), which was higher than the standard UK corporation tax rate of 20.0% (2015: 20.25%), primarily due to disallowable expenses. Based on current information, the Group expects the effective tax rate to be broadly in line with the UK standard rate.

Discontinued operations
On 29 May 2015, the Group completed the sale of its International division, which comprised its Italian and German operations, to Mapfre, S.A. Accordingly, this division is treated as discontinued operations. The gain on disposal of £167.1 million is included in profit after tax from discontinued operations of £181.2 million in 2015. Operating profit for 2015 includes £29.9 million of realised net gains on divisional AFS investments reclassified through the income statement on disposal. Further details on discontinued operations are presented in note 4 to the consolidated financial statements, see page 30.

Profit for the year and return on tangible equity
Profit for the year was £278.8 million (pre-Ogden: £452.6 million; 2015: £580.4 million), following the one-off gain on disposal of the Group's International division in 2015 and lower underwriting profit as a result of the recent reduction in the Ogden discount rate, partially offset by an improvement in the underlying underwriting performance in 2016.

RoTE was 14.2% due to lower profit after tax primarily as a result of the recent reduction in the Ogden discount rate (pre-Ogden: 20.2%; 2015: 18.5%).

The Group reiterates its ongoing target of achieving at least a 15% RoTE. Following a review of the approach to the Group's Executive Remuneration policy, the Remuneration Committee is proposing that the level of RoTE required for the March 2017 long-term incentive plan awards to vest be increased from the current range of 14.5% to 17.5% to a range of 15.0% to 18.0%. This will ensure that awards will only vest in full if significant value has been delivered to shareholders.

Earnings per share
Basic earnings per share was 20.4 pence (2015: 27.9 pence) reflecting the decrease in profit after tax.

Adjusted diluted earnings per share[1] from Ongoing operations was 21.2 pence (2015: 26.6 pence) reflecting the decrease in operating profit.

Note:

1. See glossary on page 42 for definitions and appendix A – Alternative performance measures on page 43 for reconciliation to financial statement line items.

Dividends

The Board is proposing a final dividend of 9.7 pence per share making a total regular dividend for 2016 of 14.6 pence per share. This represents 5.8% growth over the 2015 regular dividend and is in line with the Group's aim to grow the regular dividend annually in real terms. The final dividend will be paid on 18 May 2017 to shareholders on the register on 17 March 2017. The ex-dividend date will be 16 March 2017.

Net asset value

As at	Notes	31 Dec 2016 £m	30 Jun 2016 £m	31 Dec 2015 £m
Net assets	13	2,521.5	2,668.8	2,630.0
Goodwill and other intangible assets	13	(508.9)	(541.4)	(524.8)
Tangible net assets	13	2,012.6	2,127.4	2,105.2
Closing number of Ordinary Shares		1,365.1	1,368.2	1,368.7
Net asset value per share (pence)	13	184.7	195.1	192.2
Tangible net asset value per share (pence)	13	147.4	155.5	153.8

The net asset value at 31 December 2016 was £2,521.5 million (31 December 2015: £2,630.0 million) with a tangible net asset value of £2,012.6 million (31 December 2015: £2,105.2 million). The decrease since the beginning of the year reflected the payment of dividends, offset by the profit in 2016 and an increase in AFS investments reserve.

Financial management

Reserving

Financial management includes the central aspect of estimating claims reserves. Uncertainty is an inherent part of insurance, and requires judgement when assessing claims liabilities.

The Group considers the class of business, the length of time to notify a claim, the validity of the claim against a policy, and the claim value. Claims reserves could settle at a range of outcomes, and settlement certainty increases over time. However, for bodily injury claims, the uncertainty is greater due to the length of time taken to settle these claims. Annuity payments for injured parties also increase this uncertainty.

The Group seeks to adopt a conservative approach to assessing liabilities, as evidenced by the favourable development of historical claims reserves. Reserves are based on management's best estimate, which includes a prudent margin that exceeds the internal actuarial best estimate. This margin is made in reference to various actuarial scenario assessments and reserve distribution percentiles, and considers other short and long-term risks not reflected in the actuarial inputs, as well as management's view on the risks and improvements in relation to the actuarial best estimate.

Following the Lord Chancellor's announcement on 27 February 2017 of a reduction in the Ogden discount rate to minus 0.75%, the Group has assessed its liabilities in light of the reduction in the rate. The Ogden discount rate primarily affects the value of large bodily injury claims in the Motor, Commercial and Run-off divisions, and as a result also impacts reinsurance recoveries and the propensity for claims to settle as periodical payment orders. As a result, the Group has made provision within its claims reserves for a reduction in the Ogden discount rate to minus 0.75%. The impact of this on the income statement for the year ended 31 December 2016 is shown in Appendix B on page 46 and has reduced operating profit from Ongoing operations by £175.1 million and profit before tax by £217.3 million.

The Group's prior-year reserves releases were £290.1 million (2015: £449.3 million) after £205.2 million of strengthening due to the recent reduction in the Ogden discount rate. Excluding the change in the Ogden discount rate, the releases have arisen as a result of good experience in large bodily injury claims and periodic payment orders ("**PPOs**"). Home prior-year reserve releases increased to £75.9 million (2015: £41.9 million) with the increase coming mainly from favourable development on the December 2015 weather events.

Prior to the recent reduction in the Ogden discount rate, the Group established claims reserves at an assumed Ogden discount rate of 1.5%, compared with the rate then in force of 2.5%. This differential resulted in lower current-year profits, with a small and diminishing prior-year reserve release in the Group's reported profits as claims settled. The Group will now hold claims reserves at the new Ogden discount rate pending the outcome of the consultation and so the timing difference between current and prior-year profit recognition will no longer exist. The net impact of this change in approach on current year profit is expected to be small.

Following the Group's normal actuarial review process, the Group reduced its margin during 2016 due to improved claims experience, particularly in large bodily injury claims, not yet recognised in the actuarial best estimate. The Group continues to hold a significant margin above the actuarial best estimate and its overall reserving strength has been maintained following the recent reduction in the Ogden discount rate.

Looking forward, the Group expects to continue to set its initial management best estimate for future accident years conservatively. Over time, the proportion of the Group's underwriting profit attributable to current year is expected to increase, including due to targeted improvements in the expense and commission ratio. Assuming current claims trends continue, the contribution from prior-year reserve releases is expected to remain significant, albeit it is expected to reduce over time.

Claims reserves net of reinsurance

As at	31 Dec 2016 £m	31 Dec 2015 £m
Motor	2,084.2	2,125.9
Home	298.1	387.7
Rescue and other personal lines	72.8	79.3
Commercial	607.0	627.3
Total Ongoing	3,062.1	3,220.2
Run-off	326.2	382.4
Total Group	3,388.3	3,602.6

Sensitivity analysis –the discount rate used in relation to PPOs and changes in assumed Ogden discount rate

The table below provides a sensitivity analysis of the potential impact of a change in a single factor with all other assumptions left unchanged. Other potential risks beyond the ones described could have an additional financial impact on the Group.

	Increase / (decrease) in profit before tax and equity[3] at 31 December	
	2016 £m	2015 £m
PPOs[1]		
Impact of an increase in the discount rate used in the calculation of present values of 100 basis points	68.2	76.0
Impact of a decrease in the discount rate used in the calculation of present values of 100 basis points	(97.9)	(109.4)
Ogden[2] as at 31 December 2016		
Impact of the Group reserving at a discount rate of 0% compared to minus 0.75% at 31 December 2016	102.1	–
Impact of the Group reserving at a discount rate of minus 1.5% compared to minus 0.75% at 31 December 2016	(156.4)	–
Ogden as at 31 December 2015		
Impact of the Group reserving at a discount rate of 2.5% compared to 1.5% at 31 December 2015	–	131.9
Impact of the Group reserving at a discount rate of 0.5% compared to 1.5% at 31 December 2015	–	(190.0)

Notes:

1. The sensitivities relating to an increase or decrease in the real discount rate used for PPOs illustrate a movement in the time value of money from the assumed level of 0.0%.
2. As at 31 December 2016 the Group has reserved at a discount rate of minus 0.75% (2015: 1.5%). With effect from 20 March 2017, the Ogden discount rate will be minus 0.75% (2015: 2.5%).
3. These sensitivities exclude the impact of taxation.
4. These sensitivities reflect one-off impacts at 31 December and should not be interpreted as a prediction.

Capital management

Capital management policy

The Group seeks to manage its capital efficiently, maintaining an appropriate level of capitalisation and solvency, while aiming to grow its regular dividend annually in real terms.

As has been its practice, where the Board believes the Group has capital which is expected to be surplus to the Group's requirements for a prolonged period, it would intend to return the excess to shareholders.

In future, the Board has decided that, in the normal course of events, it will consider whether or not it is appropriate to pay a special dividend only once a year, alongside the full year results. In doing this, the Group will harmonise its major capital management decisions with its planning process and its full-year earnings.

Solvency II

Solvency II is the new solvency framework implemented on 1 January 2016 as the capital adequacy regime for the European insurance industry. It established a set of EU-wide capital requirements and risk management standards with the aim of increasing protection for policyholders. The Group is regulated by the PRA on both a Group basis and, for the Group's principal underwriter, U K Insurance Limited ("**UKI**"), on a solo basis.

At 1 January 2016, the Group (including UKI) assessed its capital requirements using the standard formula. UKI had its internal economic capital model approved for use by the PRA in June 2016, and this now forms part of a Group-wide PIM, which has been in use from the same date.

The Board has considered the risk appetite range of the Group under its Solvency II PIM and considers that the appropriate range, which should enable it to meet its operational, regulatory and rating agency requirements, is 140% to 180% of its SCR.

In its preliminary results, the Group has estimated its Solvency II own funds, SCR and Solvency II capital coverage ratio as at 31 December 2016. The Group will formally submit its final Solvency II Solvency Financial Condition Report ("**SFCR**") in May 2017 to the PRA, and expects to continue to update the assumptions and implement model changes until then. Therefore, the final estimates may differ from those presented in these preliminary results.

Solvency ratio sensitivity analysis

The following table shows the Group's solvency ratio sensitivities estimated based on assessed impact of scenarios as at 31 December 2016.

Scenario	Impact on solvency ratio
Motor premium rate reduction of 10%	(14 pts)
One-off catastrophe loss equivalent to the1990 storm	(9 pts)
One-off catastrophe loss based on extensive flooding of the River Thames	(9 pts)
100bps increase in credit spreads	(8 pts)
100bps decrease in interest rates	(7pts)

Capital position

At 31 December 2016, the Group held a Solvency II capital surplus of approximately £0.92 billion above its regulatory capital requirements. This was equivalent to an estimated capital coverage ratio of 165%, post-dividend. Excluding the impact of the recent reduction in the Ogden discount rate to minus 0.75%, the capital coverage ratio would have been approximately 189% post-dividend. Other than the effects of the Ogden discount rate change, which increased the SCR by £0.08 billion, the SCR remained largely stable in the second half of 2016, since the Group was approved to use its PIM. In the first half of 2016, the Group's SCR fell from £1.68 billion to £1.37 billion, largely as a result of the transition from the standard formula to the PIM. The SCR calculation fully recognises the new Ogden discount rate of minus 0.75%, but does not take into account any implications of uncertainty around the future rate. The Group's capital coverage is as follows:

As at	31 Dec 2016	30 Jun 2016
Solvency capital requirement (£ billion)	1.42	1.37
Capital surplus above solvency capital requirement (£ billion)	0.92	1.14
Capital coverage ratio post-dividend	165%	184%

The following table splits the Group's own funds by tier on a Solvency II basis.

As at	31 Dec 2016 £bn	30 Jun 2016 £bn
Tier 1 capital before foreseeable dividends	1.81	2.04
Foreseeable dividends	(0.13)	(0.20)
Tier 1 capital	1.68	1.84
Tier 2 capital	0.62	0.60
Tier 3 capital	0.04	0.07
Own funds	2.34	2.51

Tier 1 capital after foreseeable dividends represents approximately 72% of own funds and 118% of the Group's estimated SCR. Tier 2 capital relates solely to the Group's subordinated debt issued in 2012, which has a market value of £0.62 billion. The Group also recognises a deferred tax asset of £0.04 billon as Tier 3 capital. Therefore, the Group's Tier 2 and 3 capital is within the limits established by Solvency II of up to 50% of the SCR in Tier 2 and 3 combined, and 15% for Tier 3 alone.

Reconciliation of IFRS shareholders' equity to Solvency II own funds

As at	31 Dec 2016 £bn	30 Jun 2016 £bn
Shareholders' equity	2.52	2.67
Goodwill and intangible assets	(0.51)	(0.54)
Change in valuation of technical provisions	(0.04)	0.11
Other asset and liability adjustments	(0.16)	(0.20)
Foreseeable dividends	(0.13)	(0.20)
Tier 1 capital	1.68	1.84
Tier 2 capital	0.62	0.60
Tier 3 capital	0.04	0.07
Own funds	2.34	2.51

Movement in own funds

	2016 £bn
Own funds as at 1 January 2016	2.47
Change in risk margin from Group standard formula basis to Group PIM at 1 January 2016	(0.09)
Ogden discount rate impact	(0.19)
Mark to market movement	0.12
Capital generation	0.49
Capital expenditure	(0.12)
Capital distribution	(0.34)
Own funds as at 31 December 2016	2.34

During 2016, the Group's own funds reduced from £2.47 billion to £2.34 billion. The Group generated £0.49 billion of Solvency II capital, excluding the effects of the Ogden discount rate change, offset by £0.12 billion of capital expenditure and capital distribution of £0.34 billion, including the 2016 interim and final ordinary dividends and special interim dividends. Mark to market gains, as lower interest rates and credit spread tightening increased the value of the bond portfolio, were offset by a change in the basis of the risk margin calculation following approval of the Group's PIM.

Leverage

The Group's financial leverage continues to be conservative. During 2016, the leverage increased from 16.5% to 17.6% due primarily to the increase in value of the subordinated guaranteed dated notes and a reduction in shareholders' equity, following the recent one-off charge following the reduction in the Ogden discount rate.

As at	31 Dec 2016 £m	30 Jun 2016 £m	31 Dec 2015 £m
Shareholders' equity	2,521.5	2,668.8	2,630.0
Financial debt – subordinated guaranteed dated notes	539.6	551.2	521.1
Total capital employed	3,061.1	3,220.0	3,151.1
Financial-leverage ratio[1]	17.6%	17.1%	16.5%

Credit ratings

Standard & Poor's and Moody's Investors Service provide insurance financial-strength ratings for UKI. UKI is currently rated 'A' (strong) with a stable outlook by Standard & Poor's, and 'A2' (good) with a stable outlook by Moody's.

Note:

1. Total financial debt as a percentage of total capital employed.

Principal risks and uncertainties

The Group assesses robustly its principal risks. Principal risks are defined as having a residual risk impact of £40 million or more on profit before tax or net asset value on a one-in-200 years basis, accounting for customer, financial and reputational impacts. The Group believes that the risk profile remains broadly unchanged over the last year.

Principal risks	Owner	Management and mitigation examples
Insurance risk The risk of loss due to fluctuations in the timings, amount, frequency and severity of an insured event relative to the expectations at the time of underwriting. Insurance risk includes reserve, underwriting, distribution, pricing and reinsurance risks.	Chief Financial Officer, Managing Directors of Personal Lines and Commercial	• The Group estimates the technical reserves using various actuarial and statistical techniques. Management's best estimate of total reserves is set at not less than the actuarial best estimate • Third parties review the Group's reserves • Underwriting guidelines are set for all transacted business and pricing refined by analysing comprehensive data • Catastrophe and motor excess of loss reinsurance limits the Group's exposure to events and large losses • The Group invests in enhanced external data to analyse and mitigate exposures • The Group has set reserves using the latest data and trends. In particular, the recent decision to reduce the Ogden discount rate has been reflected in the estimate of reserves
Market risk The risk of loss resulting from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments. Market risk includes spread, interest rate and property risks.	Chief Financial Officer	• The Group manages and controls the risks in its investment portfolio through: – an investment strategy approved by the Board – diversification of the types of assets, limits on the amount of illiquid investments, and tight control of individual credit exposures – risk-reduction techniques are used, such as hedging foreign currency exposures with forward contracts and hedging exposure to US interest rates with swap contracts
Credit risk The risk of loss resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors to which the Group is exposed. Credit risk includes counterparty default and concentration risks.	Chief Financial Officer	• Credit limits are set for each counterparty and credit exposures are actively monitored • The Group only purchases reinsurance from reinsurers with at least an 'A-' rating
Operational risk The risk of loss due to inadequate or failed internal processes, people, systems or from external events. Operational risk includes information security, IT and business continuity, partnership contractual obligations, change, financial reporting, model and technology and infrastructure risks.	Specific members of the Executive	• The Group has appropriate operational processes and systems, including detection systems for fraudulent claims • The Group is working to improve the performance of its IT systems, while focusing on developing future systems capability. With significant change underway, the Group is continuing to monitor risks associated with IT systems' stability, cyber security and the internal control environment • The Group's risk management system is designed to enable the capture of risk information in a robust and consistent way • The Group monitors the performance of outsourced and offshored activities
Regulatory and conduct risk The risks leading to reputational damage, regulatory or legal censure, fines or prosecutions and other types of non-budgeted operational risk losses associated with the Group's conduct and activities. Regulatory and conduct risk includes compliance risk.	Chief Financial Officer and Managing Director, Personal Lines	• The Group maintains a constructive and open relationship with regulators • Specific risk management tools and resources are used to help manage exposure to regulatory risk • Risk-based monitoring is designed to ensure effective use of resources • The Group has a strong culture of considering customers' perspectives; delivering the right outcomes for customers is central to how it operates • Robust customer conduct risk management is intended to minimise the Group's exposure
Strategic risk The risk of direct or indirect adverse impact on the earnings, capital, or value of the business resulting from the strategies not being optimally chosen, implemented or adapted to changing conditions. Strategic risk includes strategy formulation and implementation risks.	Chief Executive Officer	• The Group has a plan and targets, against which performance is agreed, monitored and managed • An annual strategy and five-year planning process is run which considers Group performance, competitor positioning and strategic opportunities • Emerging risks are identified and managed using an established governance process and forums

The Group considers brand, reputational and political risk within the drivers of other risk types such as regulatory and conduct, operational, and strategic risks.

Emerging risks

The Group's definition of emerging risk is newly developing or changing risks that are often difficult to quantify, but may materially affect the business. Emerging risks are further defined as highly uncertain risks that are external to the business.

The Group records emerging risks within an Emerging Risk Register. These are reported to the Risk Management Committee and Board Risk Committee for review, challenge, approval, and feed into the Board's strategic planning process. The Group's emerging risks processes aim to:

- Achieve 'first mover advantage' by recognising risks and associated opportunities early
- Reduce the uncertainty and volatility of the Group's results
- Manage emerging risks proactively

The Group considers its main emerging risks to be:

Technological change in driving habits reduces consumer need for motor insurance

New car technologies, such as crash-prevention technologies and driverless cars, could significantly affect the size and nature of the insurance market, and the role of insurers. In addition to our partnership with the Government on Automated Driving Systems – MOVE_UK - the Group continues to consider new motor technologies as part of its pricing and underwriting approach.

Changes to traditional insurance business models

New market entrants and changes in consumer expectations could result in significant changes to the structure of the general insurance market, and require the Group to update its business model. The Group's strategy, aligned to its mission to make insurance much easier and better value for its customers, is positioned to take advantage of changes in technology and customer behaviours.

UK economy

The UK could enter a prolonged period of reduced growth following its referendum vote to leave European Union membership, potentially reducing insurance sales and the value of the Group's investment portfolio. Equally, the uncertainty surrounding the nature and outcome of the Article 50 negotiations could have various implications. In addition, whilst operations are based mainly in the UK, the Group has monitored and will continue to monitor actual and potential implications including: changes to the value of Sterling which impact claims and non-claims supplier costs; volatility in currency exposures and hedging costs; inflation; recruitment and retention of our people; potential changes to direct and indirect tax; and the impact on the Group's capital position.

Climate change

Climate change could increase the frequency of severe weather events in the UK, and particularly, flooding claims costs. The Group continue to monitor changes in claims experience and consider weather trends as part of its pricing and underwriting processes.

Potential future changes to the Ogden discount rate

The Ogden discount rate has recently been reduced to minus 0.75%, with an imminent consultation announced to consider the methodology for setting this discount rate and, therefore, potentially leading to further changes to the rate itself. The Group is monitoring the development of the consultation and analysing the implications on claims costs and the solvency capital requirement.

Consolidated income statement

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
Gross earned premium	5	3,202.8	3,110.1
Reinsurance premium	5	(202.2)	(189.2)
Net earned premium	5	3,000.6	2,920.9
Investment return	6	171.5	198.1
Instalment income		107.1	100.1
Other operating income	7	58.2	50.7
Total income		3,337.4	3,269.8
Insurance claims	8	(2,179.0)	(1,829.3)
Insurance claims recoverable from reinsurers	8	375.2	162.4
Net insurance claims	8	(1,803.8)	(1,666.9)
Commission expenses	9	(344.0)	(319.3)
Operating expenses	10	(799.4)	(738.5)
Total expenses		(1,143.4)	(1,057.8)
Operating profit		390.2	545.1
Finance costs	11	(37.2)	(37.6)
Profit before tax		353.0	507.5
Tax charge		(74.2)	(108.3)
Profit from continuing operations, net of tax		278.8	399.2
Profit from discontinued operations, net of tax	4A	–	181.2
Profit for the year attributable to owners of the Company		278.8	580.4
Earnings per share:			
Continuing operations:			
Basic (pence)	12	20.4	27.9
Diluted (pence)	12	20.2	27.6
Continuing and discontinued operations:			
Basic (pence)	12	20.4	40.6
Diluted (pence)	12	20.2	40.1

Consolidated statement of comprehensive income

For the year ended 31 December 2016

	2016 £m	2015 £m
Profit for the year	278.8	580.4
Other comprehensive income / (loss)		
Items that will not be reclassified subsequently to the income statement:		
Actuarial (loss) / gain on defined benefit pension scheme	(4.4)	6.7
Tax relating to items that will not be reclassified	0.7	(1.6)
	(3.7)	5.1
Items that may be reclassified subsequently to the income statement:		
Exchange differences on translation of foreign operations	0.1	14.4
Cash flow hedges	1.4	(1.4)
Fair value gain / (loss) on AFS investments	119.6	(100.5)
Less: realised net gains on AFS investments included in income statement	(15.3)	(44.3)
Tax relating to items that may be reclassified	(17.6)	34.6
	88.2	(97.2)
Other comprehensive income / (loss) for the year net of tax	84.5	(92.1)
Total comprehensive income for the year attributable to owners of the Company	363.3	488.3

Consolidated balance sheet

As at 31 December 2016

	Notes	2016 £m	2015 £m
Assets			
Goodwill and other intangible assets		508.9	524.8
Property, plant and equipment		180.9	186.3
Investment property		329.0	347.4
Reinsurance assets	14	1,371.8	1,011.4
Current tax assets		0.1	0.1
Deferred acquisition costs		203.1	203.8
Insurance and other receivables		988.3	955.8
Prepayments, accrued income and other assets		131.0	110.9
Derivative financial instruments		79.7	19.6
Retirement benefit asset		12.0	13.1
Financial investments	15	5,147.0	5,614.6
Cash and cash equivalents	16	1,166.1	963.7
Assets held for sale		3.8	5.1
Total assets		10,121.7	9,956.6
Equity		2,521.5	2,630.0
Liabilities			
Subordinated liabilities		539.6	521.1
Insurance liabilities	18	4,666.6	4,524.5
Unearned premium reserve	19	1,547.9	1,476.6
Borrowings	16	55.3	61.3
Derivative financial instruments		45.1	46.4
Trade and other payables including insurance payables		699.2	656.5
Deferred tax liabilities		46.0	29.9
Current tax liabilities		0.5	10.3
Total liabilities		7,600.2	7,326.6
Total equity and liabilities		10,121.7	9,956.6

Consolidated statement of changes in equity

For the year ended 31 December 2016

	Share capital £m	Employee trust shares £m	Capital reserves £m	AFS revaluation reserve £m	Non-distributable reserve £m	Foreign exchange translation reserve £m	Retained earnings £m	Total shareholders' equity £m
Balance at 1 January 2015	150.0	(13.6)	1,450.0	115.6	124.9	(13.1)	996.7	2,810.5
Profit for the year	–	–	–	–	–	–	580.4	580.4
Other comprehensive loss	–	–	–	(110.2)	–	13.0	5.1	(92.1)
Dividends	–	–	–	–	–	–	(666.0)	(666.0)
Transfer to non-distributable reserve	–	–	–	–	28.0	–	(28.0)	–
Shares acquired by employee trusts	–	(17.8)	–	–	–	–	–	(17.8)
Credit to equity for equity-settled share-based payments	–	–	–	–	–	–	12.1	12.1
Shares distributed by employee trusts	–	11.0	–	–	–	–	(11.0)	–
Tax on share-based payments	–	–	–	–	–	–	2.9	2.9
Balance at 31 December 2015	150.0	(20.4)	1,450.0	5.4	152.9	(0.1)	892.2	2,630.0
Profit for the year	–	–	–	–	–	–	278.8	278.8
Other comprehensive income	–	–	–	86.7	–	1.5	(3.7)	84.5
Dividends	–	–	–	–	–	–	(450.6)	(450.6)
Transfer from non-distributable reserve	–	–	–	–	(152.9)	–	152.9	–
Shares acquired by employee trusts	–	(39.5)	–	–	–	–	–	(39.5)
Credit to equity for equity-settled share-based payments	–	–	–	–	–	–	16.8	16.8
Shares distributed by employee trusts	–	25.6	–	–	–	–	(25.6)	–
Tax on share-based payments	–	–	–	–	–	–	1.5	1.5
Balance at 31 December 2016	150.0	(34.3)	1,450.0	92.1	–	1.4	862.3	2,521.5

Consolidated cash flow statement

For the year ended 31 December 2016

	Note	2016 £m	2015 £m
Net cash generated from operating activities before investment of insurance assets		35.0	42.1
Cash generated from investment of insurance assets		827.4	503.1
Net cash generated from operating activities		862.4	545.2
Cash flows from investing activities			
Purchases of property, plant and equipment		(49.9)	(67.9)
Purchases of intangible assets		(80.8)	(75.5)
Proceeds on disposals of assets held for sale		5.1	7.1
Net cash flows from disposal of subsidiary		–	327.1
Net cash (used by) / generated from investing activities		(125.6)	190.8
Cash flows from financing activities			
Dividends paid		(450.6)	(666.0)
Finance costs		(38.3)	(38.2)
Purchase of employee trust shares		(39.5)	(17.8)
Net cash used by financing activities		(528.4)	(722.0)
Net increase in cash and cash equivalents		208.4	14.0
Cash and cash equivalents at the beginning of the year		902.4	898.2
Effect of foreign exchange rate changes		–	(9.8)
Cash and cash equivalents at the end of the year	16	1,110.8	902.4

Notes to the consolidated financial statements

1. Accounting policies

Basis of preparation

The financial information included in this preliminary announcement has been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards ("IFRS"). However, this announcement does not itself contain sufficient information to comply with IFRS.

The financial information set out in this preliminary results announcement does not constitute the statutory accounts for the year ended 31 December 2016. The financial information is derived from the statutory accounts, which comply with IFRS, within the Group's Annual Report & Accounts. These accounts were signed on 6 March 2017 and are expected to be published in March 2017 and delivered to the Registrar of Companies following the Annual General Meeting to be held on 11 May 2017. The independent auditor's report on the Group accounts for the year ended 31 December 2016 was signed on 6 March 2017, is unqualified, does not draw attention to any matters by way of emphasis and does not include a statement under S498(2) or (3) of the Companies Act 2006.

Going concern

The directors are satisfied that the Group had sufficient resources to continue in operation for the foreseeable future, a period of not less than 12 months from the date of this report. Accordingly, they continue to adopt the going concern basis in preparing the consolidated financial statements.

Adoption of new and revised standards

The Group has adopted the following new amendments to IFRSs and International Accounting Standards ("IASs") that became effective for the Group for the first time during 2016, however these have had no impact on the consolidated financial statements, performance and / or disclosure.

Amendments to IFRS 10 'Consolidated Financial Statements', IFRS 12 'Disclosure of Interests in Other Entities' and IAS 28 'Investments in Associates and Joint Ventures' – Investment Entities: Applying the Consolidation Exception - the amendments address issues that have arisen in applying the investment entities exception under IFRS 10.

IFRS 11 (amended) 'Joint Arrangements' Accounting for Acquisitions of Interests in Joint Operations - the amendments require an entity to apply the principles of IFRS 3 Business Combinations when it acquires an interest in a joint operation which constitutes a 'business' as defined by IFRS 3.

IAS 1 (amended) 'Presentation of Financial Statements' Disclosure Initiative - the amendments are intended to assist entities in applying judgement when meeting the presentation and disclosure requirements in IFRS, providing clarity to the materiality requirement in IAS 1, that specific line items in the income statement, other comprehensive income and balance sheet may be disaggregated. The amendments clarify that an entity's share of the other comprehensive income of associates and joint ventures accounted using the equity method should be presented separately from those arising from the Group. The amendment also addresses that entities have flexibility as to the order in which they present the notes to the financial statements.

IAS 16 (amended) 'Property, Plant and Equipment' and IAS 38 (amended) 'Intangible Assets' – Classification of Acceptable Methods of Depreciation and Amortisation - the amendments state that revenue-based amortisation models are explicitly prohibited for property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets.

IAS 27 (amended) 'Separate Financial Statements', Equity Method in Separate Financial Statements - the amendments allow an entity to use the equity method for its investments in subsidiaries, joint ventures and associates in its separate financial statements.

Annual Improvements 2012-2014 Cycle - these improvements include:

IFRS 5 (amended) 'Non-Current Assets Held for Sale and Discontinued Operations' - assets are generally disposed of either through sale or through a distribution to owners. The amendment clarifies that changing from one disposal method to another is a continuation of the original plan of disposal.

IFRS 7 (amended) 'Financial Instruments: Disclosures' - provides additional guidance to clarify whether a servicing contract that includes a fee can constitute continuing involvement in a financial asset for the purpose of the disclosures required in relation to transferred assets.

IAS 19 (amended) 'Employee Benefits' - a further amendment has been made to IAS 19 to clarify that the high quality corporate bonds used to estimate the discount rate for post-employment benefits should be issued in the same currency as the benefits to be paid.

2. Critical accounting estimates and judgements

Full details of critical accounting estimates and judgements used in applying the Group's accounting policies are outlined on pages 118 to 120 of the Annual Reports & Accounts 2015. There have been no significant changes to the principles or assumptions of these critical accounting estimates and judgements during the year ended 31 December 2016.

3. Segmental analysis

The table below analyses the Group's revenue and results by reportable segment for the year ended 31 December 2016.

	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	Total Ongoing £m	Run-off £m	Total £m
Gross written premium	1,539.1	834.4	400.8	499.8	3,274.1	–	3,274.1
Gross earned premium	1,461.3	851.0	396.1	494.4	3,202.8	–	3,202.8
Reinsurance premium	(124.2)	(34.7)	(1.7)	(41.6)	(202.2)	–	(202.2)
Net earned premium	1,337.1	816.3	394.4	452.8	3,000.6	–	3,000.6
Investment return	116.9	19.9	3.9	27.4	168.1	3.4	171.5
Instalment income	76.1	23.5	1.9	5.6	107.1	–	107.1
Other operating income	40.9	0.8	13.5	3.0	58.2	–	58.2
Total income	1,571.0	860.5	413.7	488.8	3,334.0	3.4	3,337.4
Insurance claims	(1,297.3)	(332.1)	(243.0)	(297.7)	(2,170.1)	(8.9)	(2,179.0)
Insurance claims recoverable from reinsurers	295.6	0.1	–	47.2	342.9	32.3	375.2
Net insurance claims	(1,001.7)	(332.0)	(243.0)	(250.5)	(1,827.2)	23.4	(1,803.8)
Commission expenses	(42.9)	(184.4)	(28.4)	(88.3)	(344.0)	–	(344.0)
Operating expenses	(377.3)	(177.4)	(96.4)	(108.2)	(759.3)	(0.2)	(759.5)
Total expenses	(420.2)	(361.8)	(124.8)	(196.5)	(1,103.3)	(0.2)	(1,103.5)
Operating profit before restructuring	149.1	166.7	45.9	41.8	403.5	26.6	430.1
Restructuring costs[1]							(39.9)
Operating profit							390.2
Finance costs							(37.2)
Profit before tax							353.0
Underwriting (loss) / profit	(84.8)	122.5	26.6	5.8	70.1		
Loss ratio	74.9%	40.7%	61.6%	55.3%	60.9%		
Commission ratio	3.2%	22.6%	7.2%	19.5%	11.5%		
Expense ratio	28.2%	21.7%	24.5%	23.9%	25.3%		
COR	106.3%	85.0%	93.3%	98.7%	97.7%		

Note:

1. Restructuring costs are costs incurred in respect of the business activities where the Group has a constructive obligation to restructure its activities.

The table below analyses the Group's revenue and results for continuing operations by reportable segment for the year ended 31 December 2015. Discontinued operations are detailed in note 4.

	Motor £m	Home £m	Rescue and other personal lines £m	Commercial £m	Total Ongoing £m	Run-off £m	Continuing operations £m
Gross written premium	1,406.7	866.3	394.1	485.3	3,152.4	0.1	3,152.5
Gross earned premium	1,358.7	880.3	388.0	483.0	3,110.0	0.1	3,110.1
Reinsurance premium	(109.4)	(35.3)	(1.6)	(42.9)	(189.2)	–	(189.2)
Net earned premium	1,249.3	845.0	386.4	440.1	2,920.8	0.1	2,920.9
Investment return	138.9	20.5	3.8	31.5	194.7	3.4	198.1
Instalment income	69.7	23.3	1.7	5.4	100.1	–	100.1
Other operating income	33.9	0.5	12.6	3.7	50.7	–	50.7
Total income	1,491.8	889.3	404.5	480.7	3,266.3	3.5	3,269.8
Insurance claims	(956.7)	(434.8)	(231.6)	(304.5)	(1,927.6)	98.3	(1,829.3)
Insurance claims recoverable from reinsurers	161.9	(0.3)	–	28.7	190.3	(27.9)	162.4
Net insurance claims	(794.8)	(435.1)	(231.6)	(275.8)	(1,737.3)	70.4	(1,666.9)
Commission expenses	(31.9)	(176.7)	(24.5)	(86.1)	(319.2)	(0.1)	(319.3)
Operating expenses	(327.1)	(167.6)	(96.4)	(98.0)	(689.1)	(0.7)	(689.8)
Total expenses	(359.0)	(344.3)	(120.9)	(184.1)	(1,008.3)	(0.8)	(1,009.1)
Operating profit before restructuring and other one-off costs	338.0	109.9	52.0	20.8	520.7	73.1	593.8
Restructuring and other one-off costs[1]							(48.7)
Operating profit							545.1
Finance costs							(37.6)
Profit before tax							507.5
Underwriting profit / (loss)	95.5	65.6	33.9	(19.8)	175.2		
Loss ratio	63.6%	51.5%	59.9%	62.7%	59.5%		
Commission ratio	2.6%	20.9%	6.4%	19.6%	10.9%		
Expense ratio	26.2%	19.8%	24.9%	22.2%	23.6%		
COR	92.4%	92.2%	91.2%	104.5%	94.0%		

Note:

1. Restructuring costs are costs which have been incurred in respect of the business activities where the Group has a constructive obligation to restructure its activities. One-off costs are costs that are non-recurring in nature.

4. Discontinued operations and disposal group

The Group completed the disposal of its Italian and German subsidiaries (represented by Direct Line Insurance S.p.A and Direct Line Versicherung AG respectively) on 29 May 2015, which was treated as discontinued operations, generating a gain on disposal of £167.1 million.

A) Discontinued operations

The following table analyses performance relating to the discontinued operations for the period from 1 January to disposal on 29 May 2015.

	2015 £m
Gross written premium	261.1
Gross earned premium	207.2
Reinsurance premium	(78.8)
Net earned premium	128.4
Investment return[1]	37.1
Instalment income	1.4
Other operating income	0.1
Total income	167.0
Insurance claims	(156.2)
Insurance claims recoverable from reinsurers	60.9
Net insurance claims	(95.3)
Commission expenses	(28.0)
Operating expenses	(10.2)
Total expenses	(38.2)
Operating profit from discontinued operations	33.5
Gain on disposal of discontinued operations	167.1
Profit before tax from discontinued operations	200.6
Tax charge	(19.4)
Profit after tax from discontinued operations	181.2
Underwriting loss	(5.1)
Loss ratio	74.2%
Commission ratio	21.8%
Expense ratio	8.0%
COR	104.0%

Note:

1. Realised net gains on AFS investments included £29.9 million of gains reclassified through the income statement, on disposal of International.

The following table analyses the other comprehensive loss relating to discontinued operations, included in the consolidated statement of comprehensive income for the period from 1 January to disposal on 29 May 2015.

	2015 £m
Items that may be reclassified subsequently to income statement:	
Exchange differences on the translation of foreign operations	14.4
Cash flow hedge	(1.2)
Fair value gain on AFS investments	0.6
Less: realised net gains on AFS investments included in income statement	(31.8)
Tax relating to items that may be reclassified	10.1
Other comprehensive loss for the year net of tax	(7.9)

The following table analyses the cash flows relating to the discontinued operations included in the consolidated cash flow statement for the period 1 January to disposal on 29 May 2015.

	2015 £m
Net cash generated from operating activities	19.1
Net cash used by investing activities	(1.5)
Net cash generated from the disposal of discontinued operations[1]	327.1
Effect of foreign exchange rate changes	(9.8)
Net increase in cash and cash equivalents	334.9

Note:

1. The net cash generated from the disposal of discontinued operations comprises the net cash consideration of £422.5 million less the cash held by the German and Italian subsidiaries at the point of sale of £95.4 million.

B) Disposal group

The following table analyses the gain on disposal of discontinued operations during the year including the assets and liabilities held for sale in the disposal group immediately prior to the disposal on 29 May 2015.

	29 May 2015 £m
Assets	
Intangible assets	5.4
Property, plant and equipment	5.2
Reinsurance assets	171.0
Deferred tax assets	41.9
Current tax assets	–
Deferred acquisition costs	105.5
Insurance and other receivables	152.3
Prepayments and accrued income	3.1
Financial investments	665.5
Cash and cash equivalents	95.4
Total assets	1,245.3
Liabilities	
Insurance liabilities	504.5
Unearned premium reserve	355.0
Trade and other payables including insurance payables	125.3
Deferred tax liabilities	32.0
Current tax liabilities	4.0
Total liabilities	1,020.8
Net assets	224.5
Cash consideration received[1]	438.1
Transaction costs	(15.6)
Net cash consideration	422.5
Net assets disposed	(224.5)
Currency translation reserve reclassified to the income statement	(30.9)
Gain on disposal of discontinued operations	167.1

Note:

1. The Group entered into a foreign currency hedge converting Euro into Sterling in September 2014 for the disposal proceeds. The foreign currency hedge gain of £34.0 million and other sale-related consideration are included in cash consideration received.

5. Net earned premium

	2016 £m	2015[1] £m
Gross earned premium:		
Gross written premium	3,274.1	3,152.5
Movement in unearned premium reserve	(71.3)	(42.4)
	3,202.8	3,110.1
Reinsurance premium:		
Premium payable	(206.2)	(191.7)
Movement in reinsurance unearned premium reserve	4.0	2.5
	(202.2)	(189.2)
Total	3,000.6	2,920.9

Note:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.

6. Investment return

	2016 £m	2015[1] £m
Investment income:		
Interest income from debt securities	136.5	140.1
Cash and cash equivalent interest income	4.2	6.7
Interest income from infrastructure debt	7.8	4.4
Interest income from commercial real estate loans	1.0	–
Interest income	149.5	151.2
Rental income from investment property	18.4	17.9
	167.9	169.1
Net realised gains / (losses):		
AFS debt securities	15.3	12.4
Derivatives	(282.3)	(56.5)
Investment property	1.3	–
	(265.7)	(44.1)
Net unrealised gains:		
Derivatives	265.2	48.9
Investment property	4.1	24.2
	269.3	73.1
Total	171.5	198.1

Note:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.

The table below analyses the realised and unrealised gains and losses on derivative instruments included in investment return.

	Realised 2016 £m	Unrealised 2016 £m	Realised 2015[1] £m	Unrealised 2015[1] £m
Derivative (losses) / gains:				
Foreign exchange forward contracts[2]	(425.7)	19.1	(82.4)	(19.1)
Associated foreign exchange risk	151.0	253.0	44.9	61.9
Net (losses) / gains on foreign exchange forward contracts	(274.7)	272.1	(37.5)	42.8
Interest rate swaps[2]	(16.9)	20.7	(28.7)	1.2
Associated interest rate risk on hedged items	9.3	(27.6)	9.7	4.9
Net (losses) / gains on interest rate derivatives	(7.6)	(6.9)	(19.0)	6.1
Total	(282.3)	265.2	(56.5)	48.9

Notes:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.
2. Foreign exchange forward contracts are at fair value through the income statement and interest rate swaps are designated as hedging instruments.

7. Other operating income

	2016 £m	2015[1] £m
Vehicle replacement referral income	14.1	12.5
Revenue from vehicle recovery and repair services	19.3	15.5
Other income[2]	24.8	22.7
Total	58.2	50.7

Notes:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.
2. Other income includes legal services revenue, salvage income and fee income from insurance intermediary services.

8. Net insurance claims

	Gross	Reinsurance	Net	Gross	Reinsurance	Net
	2016 £m	2016 £m	2016 £m	2015[1] £m	2015[1] £m	2015[1] £m
Current accident year claims paid	1,131.7	–	1,131.7	1,037.0	–	1,037.0
Prior accident year claims paid	905.2	(18.8)	886.4	941.9	(15.9)	926.0
Increase / (decrease) in insurance liabilities	142.1	(356.4)	(214.3)	(149.6)	(146.5)	(296.1)
Total	2,179.0	(375.2)	1,803.8	1,829.3	(162.4)	1,666.9

The table below analyses the claims handling expenses included in the net insurance claims.

	2016 £m	2015[1] £m
Ongoing operations	164.4	195.6
Run-off	1.2	4.8
Total	165.6	200.4

Note:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.

9. Commission expenses

	2016 £m	2015[1] £m
Commission expenses	246.8	253.2
Expenses incurred under profit participations	97.2	66.1
Total	344.0	319.3

Note:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.

10. Operating expenses

	Total Ongoing	Restructuring costs	Run-off	Total Group
	2016 £m	2016 £m	2016 £m	2016 £m
Staff costs[1]	269.0	16.0	–	285.0
Other operating expenses[1,2,3]	250.9	23.9	0.2	275.0
Marketing	112.6	–	–	112.6
Amortisation and impairment of other intangible assets	96.7	–	–	96.7
Depreciation	30.1	–	–	30.1
Total	759.3	39.9	0.2	799.4

Notes:

1. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
2. Other operating expenses include IT costs, insurance levies, professional fees and property costs.
3. A property site in Bristol comprising of freehold property and fixtures and fittings was transferred from freehold property to assets held for sale in 2016. The property with a carrying value of £23.5 million was remeasured on transfer to its fair value of £3.8 million resulting in a charge to other operating expenses in Restructuring of £19.7 million.

10. Operating expenses continued

	Total Ongoing	Restructuring and one-off costs	Run-off	Total Group
	2015[1] £m	2015[1] £m	2015[1] £m	2015[1] £m
Staff costs[2]	254.2	18.7	0.4	273.3
Other operating expenses[2,3,4]	219.0	30.0	0.2	249.2
Marketing	117.8	–	0.1	117.9
Amortisation and impairment of other intangible assets	67.4	–	–	67.4
Depreciation	30.7	–	–	30.7
Total	689.1	48.7	0.7	738.5

Notes:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.
2. Staff costs and other operating expenses attributable to claims handling activities are allocated to the cost of insurance claims.
3. Other operating expenses include IT costs, insurance levies, professional fees and property costs.
4. The Pudsey sites were transferred from property, plant and equipment to assets held for sales in 2015. The sites with a carrying value of £22.1 million were remeasured on transfer to their fair value of £5.1 million resulting in a charge to other operating expenses in Restructuring of £17.0 million.

The table below analyses the number of people employed by the Group's operations.

	At 31 December		Average for the year	
	2016	2015[1]	**2016**	2015[1]
Operations	**9,692**	9,531	**9,546**	9,564
Support	**1,285**	1,190	**1,353**	1,257
Total[2]	**10,977**	10,721	**10,899**	10,821

Notes:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.
2. The increase in 2016 headcount relates to the acquisition of additional UK accident repair centres and the recruitment of additional DLG Legal Services Limited employees.

The aggregate remuneration of those employed by the Group's operations comprised:

	2016 £m	2015[1] £m
Wages and salaries	**348.1**	335.4
Social security costs	**38.9**	37.8
Pension costs	**24.4**	23.4
Share-based payments	**16.8**	12.1
Total	**428.2**	408.7

Note:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.

11. Finance costs

	2016 £m	2015[1] £m
Interest expense on subordinated liabilities	**46.3**	46.3
Net interest received on designated hedging instrument[2]	**(8.0)**	(8.0)
Unrealised (gain) / loss on interest rate derivatives[2]	**(19.6)**	4.5
Unrealised loss / (gain) on associated interest rate risk on hedged item[2]	**17.8**	(5.9)
Amortisation of arrangement costs and discount on issue of subordinated liabilities	**0.7**	0.7
Total	**37.2**	37.6

Notes:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations.
2. On 27 April 2012 the Group issued subordinated guaranteed dated notes with a nominal value of £500 million at a fixed rate of 9.25%. On the same date, the Group also entered into a 10-year designated hedging instrument to exchange the fixed rate of interest on the notes for a floating rate of three-month London Interbank offered rate plus a spread of 706 basis points, which increased to 707 basis points with effect from 29 July 2013.

12. Earnings per share

Earnings per share is calculated by dividing earnings attributable to the owners of the Company by the weighted average number of Ordinary Shares during the year.

On 30 June 2015, the Group completed an 11 for 12 share consolidation which had the effect of reducing the number of shares in issue from 1,500 million Ordinary Shares of 10 pence each to 1,375 million new Ordinary Shares of 10 $^{10}/_{11}$ pence each. The weighted average number of Ordinary Shares used in calculating basic and diluted earnings per share for the year ended 31 December 2015 reflects this share consolidation.

Basic

Basic earnings per share is calculated by dividing the earnings attributable to the owners of the Company by the weighted average number of Ordinary Shares for the purposes of basic earnings per share during the period, excluding Ordinary Shares held as employee trust shares.

	2016 £m	2015 £m
Earnings attributable to owners of the Company arising from:		
Continuing operations	278.8	399.2
Discontinued operations	–	181.2
Total Group	278.8	580.4
Weighted average number of Ordinary Shares (millions)	1,368.7	1,431.2
Basic earnings per share (pence):		
Continuing operations	20.4	27.9
Discontinued operations	–	12.7
Total Group	20.4	40.6

Diluted

Diluted earnings per share is calculated by dividing the earnings attributable to the owners of the Company by the weighted average number of Ordinary Shares during the period adjusted for the dilutive potential Ordinary Shares. The Company has share options and contingently issuable shares as categories of dilutive potential Ordinary Shares.

	2016 £m	2015 £m
Earnings attributable to owners of the Company arising from:		
Continuing operations	278.8	399.2
Discontinued operations	–	181.2
Total Group	278.8	580.4
Weighted average number of Ordinary Shares (millions)	1,368.7	1,431.2
Effect of dilutive potential of share options and contingently issuable shares (millions)	13.1	17.8
Weighted average number of Ordinary Shares for the purpose of diluted earnings per share (millions)	1,381.8	1,449.0
Diluted earnings per share (pence):		
Continuing operations	20.2	27.6
Discontinued operations	–	12.5
Total Group	20.2	40.1

13. Net assets per share and return on equity

Net asset value per share is calculated as total shareholders' equity divided by the number of Ordinary Shares at the end of the period excluding shares held by employee share trusts.

Tangible net asset value per share is calculated as total shareholders' equity less goodwill and other intangible assets divided by the number of Ordinary Shares at the end of the period excluding shares held by employee share trusts.

The table below analyses net asset and tangible net asset value per share.

At 31 December	2016 £m	2015 £m
Net assets	2,521.5	2,630.0
Goodwill and other intangible assets	(508.9)	(524.8)
Tangible net assets	2,012.6	2,105.2
Number of Ordinary Shares (millions)	1,375.0	1,375.0
Shares held by employee share trusts (millions)	(9.9)	(6.3)
Closing number of Ordinary Shares (millions)	1,365.1	1,368.7
Net asset value per share (pence)	184.7	192.2
Tangible net asset value per share (pence)	147.4	153.8

Return on equity

The table below details the calculation of return on equity.

	2016 £m	2015 £m
Earnings attributable to owners of the Company arising from:		
Continuing operations	278.8	399.2
Discontinued operations	–	181.2
Total Group	278.8	580.4
Opening shareholders' equity	2,630.0	2,810.5
Closing shareholders' equity	2,521.5	2,630.0
Average shareholders' equity	2,575.8	2,720.2
Return on equity	10.8%	21.3%

14. Reinsurance assets

	2016 £m	2015 £m
Reinsurers' share of general insurance liabilities	1,329.0	975.8
Impairment provision	(50.7)	(53.9)
	1,278.3	921.9
Reinsurers' unearned premium reserve	93.5	89.5
Total	1,371.8	1,011.4

15. Financial investments

	2016 £m	2015 £m
Available-for-sale debt securities		
Corporate	4,183.7	4,182.4
Supranational	98.6	140.1
Local government	21.7	105.3
Sovereign	341.2	442.7
Securitised credit	–	356.1
Total	4,645.2	5,226.6
Held-to-maturity debt securities		
Corporate	85.1	13.5
Total debt securities	4,730.3	5,240.1
Total debt securities		
Fixed interest rate[1]	4,709.6	4,801.6
Floating interest rate	20.7	438.5
Total	4,730.3	5,240.1
Loans and receivables		
Deposits with credit institutions with maturities in excess of three months	–	44.9
Infrastructure debt	337.0	329.6
Commercial real estate loans	79.7	–
Total	5,147.0	5,614.6

Notes:

1. The Group swaps a fixed interest rate for a floating rate of interest on its US Dollar, Euro and a small amount of its Sterling corporate debt securities by entering into interest rate derivatives. The hedged amount at 31 December 2016 was £1,593.6 million (2015: £1,283.3 million).

16. Cash and cash equivalents and borrowings

	2016 £m	2015 £m
Cash at bank and in hand	166.6	131.8
Short-term deposits with credit institutions[1]	999.5	831.9
Cash and cash equivalents	1,166.1	963.7
Bank overdrafts[2]	(55.3)	(61.3)
Cash and bank overdrafts[3]	1,110.8	902.4

Notes:

1. This represents money market funds with no notice period for withdrawal.
2. Bank overdrafts represent short-term timing differences between transactions posted in the records of the Group and transactions flowing through the accounts at the bank.
3. Cash and bank overdrafts is included for the purposes of the consolidated cash flow statement.

The effective interest rate on short-term deposits with credit institutions for the year ended 31 December 2016 was 0.45% (2015: 0.56%) and average maturity was 10 days (2015: 10 days).

17. Share capital

	2016 Number Millions	2015 Number Millions	2016 £m	2015 £m
Issued and fully paid: equity shares				
Ordinary Shares of 10 $^{10}/_{11}$ pence each	1,375	1,375	150.0	150.0

At a General Meeting on 29 June 2015, shareholders approved a share consolidation which completed on 30 June 2015. As a result of the share consolidation, shareholders held 11 new Ordinary Shares of 10 $^{10}/_{11}$ pence each issued by the Company in exchange for every 12 Ordinary Shares of 10 pence each held immediately prior to the share consolidation, which were cancelled by the Company.

18. Insurance liabilities

	2016 £m	2015 £m
Insurance liabilities	4,666.6	4,524.5

Gross insurance liabilities

Accident year	2007 £m	2008 £m	2009 £m	2010 £m	2011 £m	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	Total £m
Estimate of ultimate gross claims costs:											
At end of accident year	4,014.7	3,393.4	3,823.3	3,941.7	2,698.1	2,372.7	2,184.0	2,094.5	2,118.1	2,157.7	
One year later	(44.7)	50.8	121.6	(117.1)	(99.3)	(163.3)	(117.6)	20.7	(30.0)		
Two years later	7.8	51.7	(37.0)	(99.1)	(94.6)	(118.9)	(153.0)	(38.4)			
Three years later	64.8	(36.7)	(14.0)	(50.3)	(89.3)	(49.3)	(21.0)				
Four years later	(5.4)	(16.7)	(101.5)	(105.5)	(60.9)	(9.9)					
Five years later	(12.1)	(55.5)	(38.8)	(57.7)	(21.2)						
Six years later	(24.4)	(45.7)	(80.8)	(25.9)							
Seven years later	(18.8)	(29.9)	(27.3)								
Eight years later	(14.4)	(16.2)									
Nine years later	0.5										
Current estimate of cumulative claims	3,968.0	3,295.2	3,645.5	3,486.1	2,332.8	2,031.3	1,892.4	2,076.8	2,088.1	2,157.7	
Cumulative payments to date	(3,770.5)	(3,178.8)	(3,463.0)	(3,279.1)	(2,134.6)	(1,813.0)	(1,552.7)	(1,451.3)	(1,360.7)	(1,019.4)	
Gross liability recognised in balance sheet	197.5	116.4	182.5	207.0	198.2	218.3	339.7	625.5	727.4	1,138.3	3,950.8
2006 and prior											636.5
Claims handling provision											79.3
Total											4,666.6

Net insurance liabilities

Accident year	2007 £m	2008 £m	2009 £m	2010 £m	2011 £m	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	Total £m
Estimate of ultimate net claims costs:											
At end of accident year	3,970.3	3,334.7	3,790.6	3,902.0	2,644.4	2,271.8	2,093.9	1,971.0	1,926.7	1,922.2	
One year later	(64.3)	52.0	70.0	(125.2)	(131.5)	(146.7)	(123.6)	(29.7)	(67.0)		
Two years later	(14.5)	15.9	(17.4)	(120.4)	(82.1)	(107.8)	(134.4)	(42.0)			
Three years later	32.9	(22.8)	(54.1)	(44.0)	(76.5)	(35.6)	(27.8)				
Four years later	(8.9)	(45.8)	(67.0)	(93.6)	(48.7)	(11.6)					
Five years later	(17.6)	(48.7)	(29.6)	(52.3)	(37.3)						
Six years later	(19.6)	(30.9)	(74.6)	(43.9)							
Seven years later	(16.0)	(24.5)	(38.2)								
Eight years later	(12.5)	(16.2)									
Nine years later	(7.5)										
Current estimate of cumulative claims	3,842.3	3,213.7	3,579.7	3,422.6	2,268.3	1,970.1	1,808.1	1,899.3	1,859.7	1,922.2	
Cumulative payments to date	(3,705.2)	(3,139.0)	(3,429.8)	(3,264.4)	(2,111.2)	(1,800.7)	(1,537.1)	(1,449.7)	(1,358.7)	(1,019.4)	
Net liability recognised in balance sheet	137.1	74.7	149.9	158.2	157.1	169.4	271.0	449.6	501.0	902.8	2,970.8
2006 and prior											338.2
Claims handling provision											79.3
Total											3,388.3

18. Insurance liabilities continued

Movements in gross and net insurance liabilities

	Gross £m	Reinsurance £m	Net £m
Claims reported	2,791.1	(315.3)	2,475.8
Incurred but not reported	1,778.2	(460.2)	1,318.0
Claims handling provision	104.8	–	104.8
At 1 January 2015	4,674.1	(775.5)	3,898.6
Cash paid for claims settled in the year	(1,978.9)	16.0	(1,962.9)
Increase / (decrease) in liabilities:			
Arising from current-year claims	2,307.6	(191.4)	2,116.2
Arising from prior-year claims	(478.3)	29.0	(449.3)
At 31 December 2015	4,524.5	(921.9)	3,602.6
Claims reported	2,732.2	(375.0)	2,357.2
Incurred but not reported	1,697.9	(546.9)	1,151.0
Claims handling provision	94.4	–	94.4
At 31 December 2015	4,524.5	(921.9)	3,602.6
Cash paid for claims settled in the year	(2,036.9)	18.8	(2,018.1)
Increase / (decrease) in liabilities:			
Arising from current-year claims	2,329.3	(235.4)	2,093.9
Arising from prior-year claims	(150.3)	(139.8)	(290.1)
At 31 December 2016	4,666.6	(1,278.3)	3,388.3
Claims reported	2,584.5	(388.3)	2,196.2
Incurred but not reported	2,002.8	(890.0)	1,112.8
Claims handling provision	79.3	–	79.3
At 31 December 2016	4,666.6	(1,278.3)	3,388.3

Movement in prior-year net claims liabilities by operating segment

	2016 £m	2015 £m
Motor	(123.5)	(266.8)
Home	(75.9)	(41.9)
Rescue and other personal lines	(17.5)	(13.6)
Commercial	(49.8)	(56.6)
Total Ongoing	(266.7)	(378.9)
Run-off	(23.4)	(70.4)
Total	(290.1)	(449.3)

19. Unearned premium reserve

Movement in unearned premium reserve

	Gross £m	Reinsurance £m	Net £m
At 1 January 2015	1,434.2	(87.0)	1,347.2
Net movement in the year	42.4	(2.5)	39.9
At 31 December 2015	1,476.6	(89.5)	1,387.1
Net movement in the year	71.3	(4.0)	67.3
At 31 December 2016	1,547.9	(93.5)	1,454.4

20. Related parties

Transactions between the Group's subsidiary undertakings, which are related parties, have been eliminated on consolidation and accordingly are not disclosed.

Full details of the Group's related party transactions for the year ended 31 December 2015 are included on page 163 of the Annual Report & Accounts 2015.

Corporate information

Direct Line Insurance Group plc is a public limited company registered in England and Wales, number 02280426. The address of the registered office is Churchill Court, Westmoreland Road, Bromley BR1 1DP.

Statutory accounts information

The Annual Report & Accounts 2015 were signed on 29 February 2016 and were delivered to the Registrar of Companies following the Annual General Meeting held on 12 May 2016. The Annual Report & Accounts 2015 is available at: ara2015.directlinegroup.com .

Glossary

Adjusted diluted earnings per share
Adjusted diluted earnings per share is calculated by dividing the adjusted profit after tax of Ongoing operations by the weighted average number of Ordinary Shares during the period adjusted for dilutive potential Ordinary Shares.

Adjusted profit after tax
Profit after tax is adjusted to exclude discontinued operations, the Run-off segment and restructuring and other one-off costs, and is stated after charging tax (using the UK standard tax rate of 20.0%; 2015: 20.25%).

Commission ratio
The ratio of commission expense divided by net earned premium.

Combined operating ratio ("COR")
The combined operating ratio is the sum of the loss, commission and expense ratios. The ratio measures the amount of claims costs, commission and expenses compared to net earned premium generated. A ratio of less than 100% indicates profitable underwriting.

Capital coverage ratio
The ratio of Solvency II own funds to the solvency capital requirement.

Current-year attritional loss ratio
The loss ratio for the current accident year, excluding the movement of claims reserves relating to previous accident years and claims costs relating to major weather events in the Home division.

Earnings per share
The amount of the Group's profit allocated to each Ordinary Share of the Company.

Expense ratio
The ratio of operating expenses divided by net earned premium.

Investment income yield
The annualised income earned from the investment portfolio, recognised through the income statement during the period and divided by the average assets under management. This excludes unrealised and realised gains and losses, impairments and fair-value adjustments. The average assets under management derives from the period's opening and closing balances for the total Group.

Investment return
The income earned from the investment portfolio, including unrealised and realised gains and losses, impairments and fair value adjustments.

Investment return yield
The annualised return earned from the investment portfolio, recognised through the income statement during the period divided by the average assets under management. This includes unrealised and realised gains and losses, impairments and fair-value adjustments. The average assets under management derives from the period's opening and closing balances for the total Group.

Loss ratio
Net insurance claims divided by net earned premium.

Ongoing operations
Ongoing operations comprise the Group's Ongoing divisions: Motor, Home, Rescue and other personal lines, and Commercial. It excludes discontinued operations, the Run-off segment, and restructuring and other one-off costs.

Operating profit
The pre-tax profit that the Group's activities generate, including insurance and investments activity, but excluding finance costs.

Return on tangible equity ("RoTE")
Return on tangible equity is annualised adjusted profit after tax from Ongoing operations divided by the Group's average shareholders' equity less goodwill and other intangible assets.

Solvency II
The capital adequacy regime for the European insurance industry, which became effective on 1 January 2016. It establishes revised capital requirements and risk management standards. It sets out capital requirements , appropriate systems of governance and disclosure requirements.

Total costs
Total costs comprise operating expenses and claims handling expenses for Ongoing operations.

Underwriting result (profit or loss)
The profit or loss from operational activities excluding investment return and other operating income. It is calculated as net earned premium less net insurance claims and total expenses.

Appendix A – Alternative performance measures

The Group has identified Alternative Performance Measures ("APMs") in accordance with the European Securities and Markets Authority's published Guidelines. The Group uses APMs to improve comparability of information between reporting periods and reporting segments, by adjusting for either uncontrollable or one-off costs which impact the IFRS measures, to aid the user of the Annual Report in understanding the activity taking place across the Group. These APMs are contained within the main narrative sections of this document, outside of the financial statements and notes, and may not necessarily have standardised meanings for ease of comparability across peer organisations.

Further information is presented below, defined in the glossary on page 42 and reconciled to the most directly reconcilable line items in the financial statements and notes. Note 3 on page 28 of the consolidated financial statements presents a reconciliation of the Group's business activities on a segmental basis to the statutory income statement including Ongoing operations of the Group. All note references in the table below are to the notes to the consolidated financial statements on pages 27 to 41.

Group APM	Closest equivalent IFRS measure	Definition and / or reconciliation	Rationale for APM
Adjusted diluted earnings per share	Diluted earnings per share	Adjusted diluted earnings per share is defined in the glossary on page 42 and is reconciled on page 44.	This is a representation of the underlying earnings over the number of shares in issue adjusted for potential dilutions from the exercise of options.
Current-year attritional loss ratio	Loss ratio	Current-year attritional loss ratio is defined in the glossary on page 42 and is reconciled to loss ratio (discussed below) on page 11.	Expresses claims performance in the current accident year in relation to net earned premium.
COR	Operating profit	COR is defined in the glossary on page 42. The constituent parts: Operating profit – Ongoing operations is discussed below; and Net earned premium (note 3).	This is a measure of underwriting profitability whereby a ratio of less than 100% represents an underwriting profit and a ratio of more than 100% represents an underwriting loss and excludes non-insurance income.
Investment income yield	Investment income	Investment income yield is defined in the glossary on page 42 and is reconciled on page 45.	Expresses a relationship between the investment return and the associated opening and closing assets net of any associated liabilities.
Loss ratio	Net insurance claims	Loss ratio is defined on page 42 and is reconciled in note 3.	Expresses claims performance in relation to net earned premium.
Investment return yield	Investment return	Investment return yield is defined on page 42 and is reconciled on page 45.	Expresses a relationship between the investment income and the associated opening and closing assets net of any associated liabilities.
Operating profit – Ongoing operations	Operating profit	Operating profit – Ongoing operations is defined as Operating profit (see glossary on page 42) less Operating profit from run-off segment plus restructuring and one-off costs (see note 3) and is reconciled on page 44.	This measure shows the underlying performance (before tax and finance costs) of the business activities without the impact of business that is in run-off and restructuring and one-off expenses.
Profit after tax from Ongoing operations	Profit after tax	Operating profit – Ongoing profit (as above) less Finance costs and Tax at standard rate and is reconciled on page 44.	This measure shows the underlying performance (after tax and finance costs) of the business activities without the impact of business that is in run-off and restructuring and one-off expenses.
RoTE	Return on Equity	RoTE is defined in the glossary on page 42 and is reconciled on page 44.	This shows underlying performance against a measure of equity that is more able to be compared with other companies.
Tangible equity	Equity	Tangible equity is defined as Equity less Intangible assets within the Balance Sheet and is reconciled on page 44.	This shows the equity excluding intangible assets for comparability with companies which have not acquired businesses or capitalised intangible assets.
Tangible net asset per share	Net assets per share	Tangible net asset per share is defined as Tangible equity (as above) expressed as a value per share and is reconciled in note 13 on page 36.	This shows the equity excluding intangible assets per share for comparability with companies which have not acquired businesses or capitalised intangible assets.
Total costs - Ongoing operations	Operating expenses	Total costs – Ongoing operations is defined as Operating expenses adjusted to remove restructuring and Other one-off costs and Operating expenses charged to the run-off segment (reconciled in note 10) plus claims handling expenses incurred in net insurance claims on Ongoing operations (note 8). This is reconciled on page 12.	This represents the total value of operating expenses including those allocated to the insurance claims line as claims handling expenses.

Additionally, the current-year attritional loss ratio within the analysis by division section and total costs have also been identified as alternative performance measures, similarly reconciled to the financial statements and notes, on pages 11 and 12 respectively, and defined in the glossary.

Appendix A – Alternative performance measures

Return on tangible equity ("RoTE")[1]

At	Note[2]	2016 £m	2015 £m
Operating profit	3	390.2	545.1
Add back: restructuring and other one-off costs	3	39.9	48.7
Exclude: operating profit from run-off	3	(26.6)	(73.1)
Operating profit from Ongoing operations	3	403.5	520.7
Finance costs	3	(37.2)	(37.6)
Profit before tax – Ongoing operations		366.3	483.1
Tax charge (using the UK standard tax rate of 20.0% and 20.25% respectively)		(73.3)	(97.8)
Adjusted profit after tax – Ongoing operations		293.0	385.3
Opening shareholders' equity		2,630.0	2,810.5
Opening goodwill and other intangible assets		(524.8)	(517.5)
Opening disposal group equity		–	(241.0)
Opening shareholders' tangible equity		2,105.2	2,052.0
Closing shareholders' equity		2,521.5	2,630.0
Closing goodwill and other intangible assets		(508.9)	(524.8)
Closing shareholders' tangible equity		2,012.6	2,105.2
Average shareholders' tangible equity[3]		2,058.9	2,078.6
Return on tangible equity		14.2%	18.5%

Adjusted diluted earnings per share[1]

At	Note[2]	2016 £m	2015 £m
Adjusted profit after tax for Ongoing operations		293.0	385.3
Weighted average number of Ordinary Shares for the purpose of diluted earnings per share (millions)	12	1,381.8	1,449.0
Adjusted diluted earnings per share (pence)		21.2	26.6

Notes:

1. See glossary on page 42 for definitions
2. See notes to the consolidated financial statements
3. Mean average of opening and closing balances

Appendix A – Alternative performance measures

Investment yields

At	Note	2016 £m	2015[1] £m
Investment income	6	167.9	169.1
Investment return	6	171.5	198.1
Opening investment property		347.4	307.2
Opening financial investments		5,614.6	5,961.2
Opening cash and cash equivalents		963.7	880.4
Opening borrowings		(61.3)	(69.8)
Opening derivatives liability[2]		(45.7)	(27.8)
Opening investment holdings		6,818.7	7,051.2
Closing investment property		329.0	347.4
Closing financial investments	15	5,147.0	5,614.6
Closing cash and cash equivalents	16	1,166.1	963.7
Closing borrowings	16	(55.3)	(61.3)
Closing derivatives liability[2]		(5.8)	(45.7)
Closing investment holdings		6,581.0	6,818.7
Average investment holdings		6,699.9	6,935.0
Investment income yield		2.5%	2.4%
Investment return yield		2.6%	2.9%

Notes:

1. Results for the year ended 31 December 2015 are based on continuing operations and exclude discontinued operations
2. See footnote 1 on page 14.

Appendix B – proforma results

The table below presents the Group's results on a proforma basis for 2016 in order to exclude the impact on the income statement of the reduction in the Ogden discount rate to minus 0.75%, as management believe that this provides a clearer comparison to 2015.

	FY 2016 £m	Proforma FY 2016 £m	FY 2015 £m
Ongoing operations:			
In-force policies (thousands)	15,806	15,806	16,068
Gross written premium	3,274.1	3,274.1	3,152.4
Net earned premium	3,000.6	3,000.6	2,920.8
Underwriting profit	70.1	245.2	175.2
Instalment and other operating income	165.3	165.3	150.8
Investment return	168.1	168.1	194.7
Operating profit – Ongoing operations	403.5	578.6	520.7
Run-off	26.6	68.8	73.1
Restructuring and other one-off costs	(39.9)	(39.9)	(48.7)
Operating profit	390.2	607.5	545.1
Finance costs	(37.2)	(37.2)	(37.6)
Profit before tax	353.0	570.3	507.5
Tax	(74.2)	(117.7)	(108.3)
Profit from discontinued operations, net of tax	–	–	181.2
Profit after tax	278.8	452.6	580.4
Of which Ongoing operations	293.0	433.1	385.3
Key metrics – Ongoing operations			
Loss ratio[1] prior to the reduction in Ogden discount rate	55.0%	55.0%	59.5%
Loss ratio[1] due to reduction in Ogden discount rate	5.9%	–	–
Commission ratio[1]	11.5%	11.5%	10.9%
Expense ratio[1] including Flood Re levy	25.3%	25.3%	23.6%
COR[1]	97.7%	91.8%	94.0%
Adjusted diluted earnings per share (pence)[2]	21.2	31.3	26.6
Return on tangible equity[2]	14.2%	20.2%	18.5%
Key metrics			
Investment income yield[1]	2.5%	2.5%	2.4%
Investment return[1]	2.6%	2.6%	2.9%
Basic earnings per share (pence)[1]	20.4	33.1	27.9
Return on equity	10.8%	17.0%	21.3%
Dividend per share – interim (pence)	4.9	n/a	4.6
– final interim (pence)	9.7	n/a	9.2
– regular (pence)	14.6	n/a	13.8
– first special interim[3] (pence)	10.0	n/a	27.5
– second special interim (pence)	-	n/a	8.8
– total (pence)	24.6	n/a	50.1
Net asset value per share (pence)	184.7	197.4	192.2
Tangible net asset value per share (pence)	147.4	160.2	153.8

	FY 2016	FY 2016	HY 2016
Capital coverage[2,4] – estimated	165%	189%	184%

Notes:

1. A reduction in the ratio represents an improvement and positive change as a proportion of net earned premium, while an increase in the ratio represents a deterioration and negative change.
2. See glossary on page 42 for definitions and appendix A – Alternative performance measures on page 43 for reconciliation to financial statement line items.
3. The special interim dividend paid on 24 July 2015 of 27.5 pence per share, following the sale of the Group's former Italian and German operations.
4. See note 4 on page 1 and adjusted for dividends.

Additional information

We confirm that to the best of our knowledge:

1. the financial statements within the Annual Report & Accounts, from which the financial information within these Preliminary Results have been extracted, are prepared in accordance with International Financial Reporting Standards as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the undertakings included in the consolidation taken as a whole; and
2. the management report within these Preliminary Results includes a fair review of the development and performance of the business and the position of the Group, and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties faced by the Group.

Signed on behalf of the Board

Paul Geddes

Chief Executive Officer

6 March 2017

John Reizenstein

Chief Financial Officer

6 March 2017