Homeowners Friendly Society Group

annual report & accounts

for the year ended 31 December 2005

engage
Mutual Assurance

society information

engage Mutual Assurance is a trading name of Homeowners Friendly Society Limited.

registered office

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websites: www.engagemutual.com
www.theukgroup.com

Registered and Incorporated under the Friendly Societies Act 1992

Registered No: 964F

Authorised and regulated by the Financial Services Authority

board of directors

Raymond F Pierce BA FRSA

David G Hargrave BCom MSc FIA

Andrew S Haigh BSc

Kevin D Chidwick BSc FCCA MBA
(resigned 26 August 2005)

Rt. Hon. Lord Clark of Windermere BA MSc PhD

Penelope J Hemming

W Graham Henderson B Comm CA FRSA
(appointed 23 February 2006)

C Christopher F Lazenby BSc(Eng) CEng MBCS

Peter W Mason BSc Hons. FIA
(appointed 9 December 2005)

Christina M McComb BA Hons. MBA
(appointed 11 May 2005)

Gordon A Murison MBE (retired 12 May 2005)

secretary

Andrew J Horsley MSI FCIS

actuarial function holder

Trevor M Batten FIA

auditors

KPMG Audit Plc
Registered Auditor

solicitors

Addleshaw Goddard

bankers

Barclays Bank Plc

board committees

audit

Peter W Mason
(appointed as Chairman 1January 2006)

Rt. Hon. Lord Clark of Windermere

David G Hargrave
(resigned as Chairman 31 December 2005)

Christina M McComb

finance & risk

David G Hargrave (Chairman)
Trevor M Batten
Graham Henderson
Peter W Mason

nominations

Raymond F Pierce (Chairman)
Andrew S Haigh
David G Hargrave

remuneration

Christina M McComb
(appointed as Chairman 9 December 2005)
Rt. Hon. Lord Clark of Windermere

Penelope J Hemming

Raymond F Pierce
(resigned as Chairman 9 December 2005)

our mission is

to enable people to protect their welfare.

We will do this by providing our customers with accessible, simple, value for money protection and savings products.

contents

your board of directors

Ray Pierce *BA FRSA (60)* *Chairman*

Ray joined the Board, and was appointed Chairman, in 1999. He has extensive experience in the financial services industry, in both general management and strategic marketing roles. Ray was a Director of Guardian Royal Exchange Plc and has also held senior positions at The Mortgage Corporation and American Express. He is Chairman of Crown Sports Plc, Chairman of Sense International, an international development charity and Chairman of Elevation Events Plc. Ray is also Vice Chairman of Thinc Destini Plc, a Director of Guinness Flight Venture Capital Trust Plc and Chairman of the Board of Trustees of the National Motor Museum.

David Hargrave *BCom MSc FIA (55)* *Vice Chairman*

David joined the Homeowners Board in 1981 and was re-appointed as Vice Chairman in 2004 having served in this position during 1998/1999. David is an Actuary and in 1995 formed David Hargrave Limited, an independent company specialising in project-based financial consultancy. He is also the independent trustee of a number of pension funds.

Andrew Haigh *BSc (43)* *Chief Executive*

Andrew became Chief Executive of Homeowners in March 2002. He joined the Society in 1998 and was appointed to the Board as Sales and Marketing Director in 1999. He is a marketing professional with over 21 years' experience. Prior to joining Homeowners, Andrew held senior positions with NCR Corporation and National & Provincial Building Society. His early career was with Barclays Bank, British Airways and Volvo. He is also a member of the Executive Committee of the Association of Friendly Societies.

Rt. Hon. Lord Clark of Windermere *BA MSc PhD (66)* *Non-Executive Director*

Lord Clark joined Homeowners as a consultant in 1982 and became a Director in 1989. He left to join the Cabinet in 1997 as Chancellor of the Duchy of Lancaster being responsible for, amongst other things, the machinery of government, including IT. Lord Clark, who rejoined the Homeowners Board in 1999, was MP for South Shields from 1979 until his elevation to the House of Lords in July 2001. He is currently Chairman of the Forestry Commission, and a Non-Executive Director of Thales Plc and Carlisle United Football Club Limited.

Penny Hemming *(58)* *Non-Executive Director*

Penny joined the Homeowners Board in October 2004 having served as CBI Regional Director for Yorkshire and the Humber since 1995, giving her a wide understanding of all issues confronting businesses today. She also spent 16 years in the city as a stockbroker and currency broker. Penny is a Trustee of Eureka, the Museum for Children, a member of the Advisory Board of the University of Bradford School of Management and was appointed a Deputy Lieutenant of West Yorkshire in 2000.

Graham Henderson *B Comm CA FRSA (51)* *Finance Director*

Graham joined the Board in February 2006 as Finance Director. He is a Chartered Accountant with over 20 years' experience in senior financial roles in financial services companies. His last role was as Programme Director responsible for the implementation of new reporting regulations for the life and pensions operations of Abbey Plc. He has operated as Finance Director and Head of Finance at Britannia Life and at Royal Life and has extensive experience of change management, corporate finance and business planning.

Chris Lazenby *BSc(Eng) CEng MBCS (55)* *Operations Director*

Chris joined Homeowners in August 2003 and was appointed to the Board as Operations Director in January 2004. He has extensive experience of leading business-wide change having been responsible for projects as diverse as developing strategy, setting up a customer contact centre, cost reduction and many technology-based initiatives. Chris's previous roles have included Head of Business Improvement in the mutual sector with Britannia Building Society, IT Director for Lunn Poly as well as senior positions at Ladbrokes and Massey Ferguson.

Peter Mason *BSc Hons FIA (55)* *Non-Executive Director*

Peter joined the Board in December 2005. He is a Fellow of the Institute of Actuaries with over 30 years' experience of Financial Services businesses. He is Investment Director and Actuary at the Neville James Group, an investment management company, and holds Non-Executive Directorships at Countrywide Plc and Chesnara Plc.

Christina McComb *BA Hons MBA (49)* *Non-Executive Director*

Christina joined the Board in May 2005. She has extensive experience of investing in and developing smaller companies, including 14 years working at 3i where she was responsible for 3i's investment portfolio in London and the South East and latterly 3i's UK technology portfolio. She is currently a Director of the Shareholder Executive, a department based within the DTI which manages the Government's financial and shareholder interests in a number of public-owned enterprises. Christina is also a Non-Executive Director of Partnerships-UK and a member of the Investors Advisory Board of the London Technology Fund. She is a Governor of Richmond Upon Thames College, a leading tertiary college in south-west London.

chairman's report for the year ended 31 December 2005

Of particular importance to many customers last year was the continued rise of the stock market, which resulted in considerable improvement in maturity values for many unit linked savings plans as equities returned to levels of early 1998. We hope for continued growth this year and a consequent further improvement in investment returns.

As well as bringing the welcome improvement in stock market growth, 2005 also proved to be a very significant year in the Society's development. After several years of preparation and consultation, Child Trust Funds became a reality and I am delighted to report that your Society played one of the leading roles in their success during the year.

We have supported the concept of the Child Trust Fund since it was first raised, and have been keen to approach it in a manner which would be as inclusive as possible and would encourage more young parents to save regularly. We believe we have made good progress towards this goal as research undertaken last year suggested that twice as many of our Child Trust Fund customers were making regular payments into their Child Trust Fund, compared to the experience of other providers.

As explained in last year's Annual Report, we launched our new trading identity, **engage** Mutual Assurance, in April 2005. Our new name has given the organisation a contemporary look and feel while retaining our traditional mutual values and welfare orientation.

We have also made changes to the names of our subsidiary companies to feature the new **engage** identity. This enables us to make best use of the new name, while avoiding complex or confusing caveats or footnotes in our literature to explain the different relationships between new trading styles and old company names. The first of these was the OEIC manager – which is used to provide the Child Trust Fund and our equity ISA product – which is now called **engage** Mutual Funds Limited.

The more significant decision will be whether to change the name of the Society itself. To date, the **engage** trading style has been a huge success and provides an excellent base on which to develop the Society further. We would like to see how this year unfolds, but our current thinking is that it would be appropriate to change the name of the Society next year. If we do decide to go ahead, we will communicate our plans and seek your support in the normal way by putting forward a formal resolution for member approval.

With so much change happening in the organisation and the industry at large, it would be all too easy to become focused on the present, day to day issues of running the organisation and lose sight of our long term strategy. I am pleased to be able to inform members that we have addressed the significant opportunities presented in the last 12 months in the context of where we need to take the organisation in the long term. In his Business Review, the Chief Executive outlines how we have made the most of the opportunity to build new strategic partnerships, build awareness of our new name and develop the internet as one of the most important channels by which we communicate with people.

Some of the main responsibilities of your Board are, of course, to carefully review strategy, progress and the changing risks that the organisation faces. We continue to develop both the membership of the Board and the reporting and control processes to ensure that these responsibilities are delivered effectively.

In my report last year, I referred to the Myners Review on "The Governance of

Life Mutuals" and the likely proposals for improvement in governance processes. These proposals have now crystallised into formal guidance which was developed by a joint Committee from the two trade bodies, the Association of Friendly Societies and the Association of Mutual Insurers. The Society is a member of both organisations and plays an active role on the Committee. We support the changes and have already implemented a number of detailed improvements to our own processes, although we were pleased to note that in the majority of cases we already met the proposed standard. You can read about some of the changes in the Corporate Governance Section of the Annual Report.

We were pleased to welcome two new Non-Executive Directors to the Society in the course of 2005. Christina McComb joined the Board in May. Christina is a Director of the Shareholder Executive within the Cabinet Office, prior to which she had a long association with the venture capital group 3i. She has much experience in the workings of government and the problems and challenges faced by growing organisations.

Peter Mason was appointed to the Board in December, having had earlier involvement as an independent member of the Finance & Risk Committee. He is an Actuary and brings a wealth of experience of life company financial operations. Peter took on the Chairmanship of the Audit Committee on 1 January 2006.

Graham Henderson joined the Board in February 2006 for an eighteen month fixed term in the Finance Director role, having worked with us on an interim basis since October 2005. Graham is a qualified Chartered Accountant and has extensive experience gained in senior roles in the life insurance industry, which has already been put to very good effect. We look forward to working with Graham in the months to come.

Two members of the Board stepped down in 2005.

Kevin Chidwick, Finance Director, left the Society in August to pursue other interests. We thank Kevin for his contribution and wish him well for the future.

Gordon Murison retired as a Non-Executive Director in May 2005. Gordon had given tremendous service, over 27 years, to the Board of the former UK Civil Service Benefit Society which transferred its engagements to us in 2003. He remained on the Board of the merged organisation to ensure a smooth transition and to provide continuity in the representation of the UK members at Board level. On behalf of all members we thank Gordon for his service over so many years and in particular for the support and advice he offered to make the integration of the Societies such an effective process. We wish Gordon an enjoyable retirement.

I closed my report last year with the expectation that 2005 would be important for us. That certainly proved to be the case. I have no doubt that 2006 will be just as important, as we seek to make the very most of the excellent progress we made last year.

The Board, Management and Staff of the Society continue to focus on building a successful future for the organisation and delivering good value and excellent service for all our customers. We thank you for your support.

R.F. Pierce

Ray Pierce
Chairman
23 February 2006

chief executive's business review

for the year ended 31 December 2005

As always, our priority last year was to continue to provide customers with a good value, high quality service for their savings and protection needs. In what proved to be a very eventful year, we were successful in that aim and were able to deliver our products to a far wider audience than ever before. The number of new policies processed in the year rose by three and a half times the number for 2004 to nearly 80,000 and our customer base grew by 24%.

a new look and a new name

2005 was our first year of operations under our new trading style of **engage** Mutual Assurance. We are proud of the success we have been able to make of Child Trust Fund (CTF), through our subsidiary **engage** Mutual Funds Limited, and the impressive list of new distribution partners we attracted. These results were underpinned by our new trading style, which provided a far more contemporary and relevant foundation on which to build awareness and new customer relationships.

The new style was launched to customers with the AGM Notice of Meeting for 2005 and the first annual statements under the new brand were issued in January 2006.

Part of the challenge we faced in launching the new identity was how to make people aware of our new name. We were delighted to secure a sponsorship arrangement with the Rugby Football League which has provided extensive exposure in both broadcast and print media as title sponsors of the **engage** Super League. The sponsorship coverage we received last year was independently assessed and was estimated to have an equivalent media value worth significantly more than the cost of the sponsorship. We look forward to another successful year as sponsors in 2006 and have extended the relationship to cover the 2007 and 2008 seasons. We further reinforced awareness of **engage**, with the sponsorship of the **engage** International Open, a World Bowls Tour event held in November 2005. These initiatives have served to raise awareness and the profile of the organisation amongst our customer base, and have supported our sales and marketing activity during 2005.

results and key performance indicators for 2005

In my 2004 report, I aimed to provide customers with more information about the progress of the Society. We have developed this report further to meet new requirements for reporting under an amendment (Section 71A) to the Friendly Societies Act.

The change of trading style from Homeowners to **engage** Mutual Assurance in April 2005 provided the ideal platform from which to launch our CTF campaign. The CTF is the Government's initiative to provide every child born after 1 September 2002 with a savings account. The Government provides a voucher for either £250 or, for lower income families, £500 to pay into the CTF at birth and a further top up will be provided at age 7. Families and friends can add up to £1200 a year to the CTF, tax free. The CTF was launched in April 2005 when more than 2.7 million vouchers were distributed. The initial wave of vouchers included babies born between September 2002 and January 2005, and now goes to the child benefit claimant of all new born children in the UK.

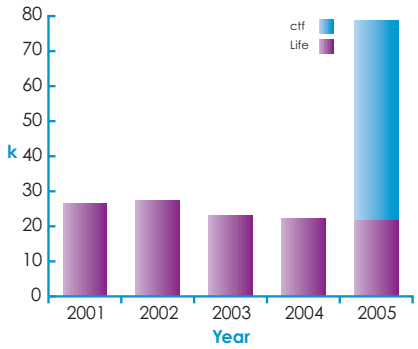
In order to ensure that no child is excluded, parents who do not choose a CTF within twelve months of receiving their voucher will have their CTF allocated to one of a number of registered providers. **engage** will be one of the providers registered to receive government allocated CTFs.

We ended 2005 as one of the leading providers of CTFs. Our success in CTF was the result of more than three years' preparation. In addition to extensive research and involvement in the consultation process, we developed operating systems and procedures to ensure the smooth and efficient administration of these new accounts.

We provide CTFs direct to the public through our website, **www.engagemutual.com** and also through a range of high quality partners who provide additional access for distribution. Early research suggests that we have been particularly successful in internet distribution of CTFs and we believe we are the leading provider of web based equity stakeholder CTF accounts, with over 60% of all applicants using the internet.

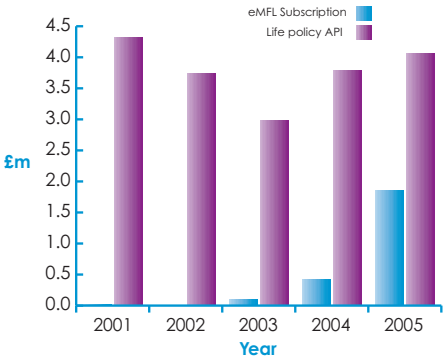
The positive impact of CTF on new business volumes has been significant, as shown in the chart below.

new business volume



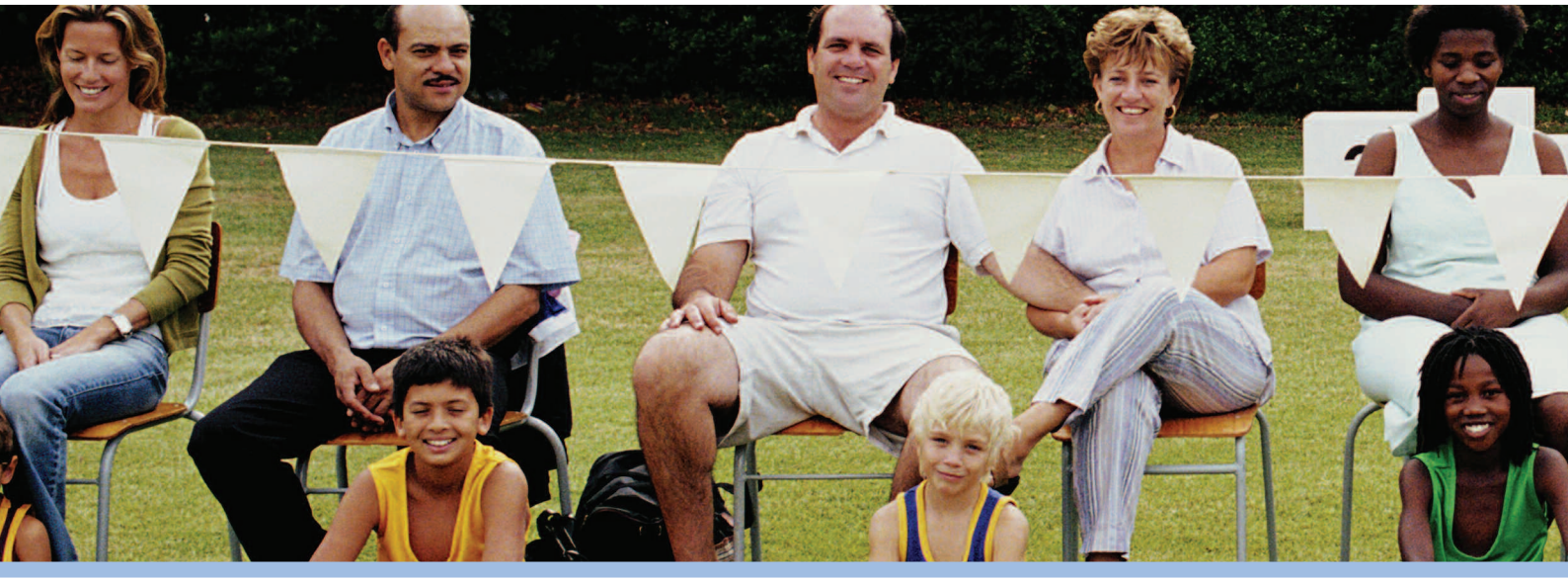
We do not wish to become reliant on CTF as our sole source of new business and have been working to maintain sales in our traditional life assurance products such as the Over 50s plan, Tax Exempt Savings Plan and With Profits policies. Our life based new business volume remained stable with only a very slight decrease in volume and a slight increase in the level of new business premiums in 2005.

new business performance



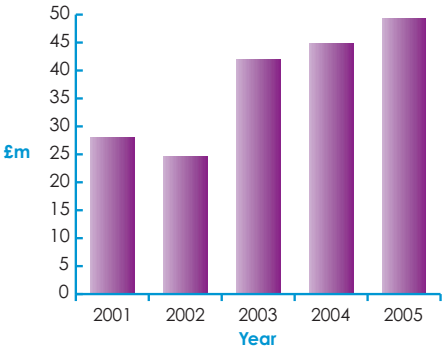
For life assurance policies we show new regular premiums and one tenth of the new single premiums for the year. Under normal financial reporting conventions we would show the OEIC investment sales in terms of the total premiums received, however for ease of comparison, we have adopted the same convention as for life policies in this chart. The total figure for new OEIC subscriptions was in excess of £18m for the year.

chief executive's business review (cont.)



The Group continues to be financially robust. The Fund For Future Appropriations (FFA) has continued to increase as shown on our Balance Sheet on page 30.

fund for future appropriations (FFA)

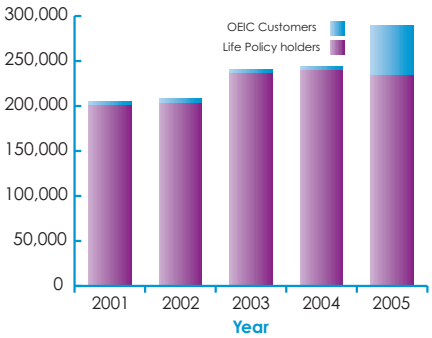


The FFA is a measure of the Group's surplus assets over liabilities, using accounting conventions for life companies. The improved position reflects a strengthening of the With Profits sub fund, with a proportion of these assets being required for future terminal bonuses.

Continued investment in long-term, low charge business such as the CTF is likely to result in a reduction in the FFA as with this type of product, it takes several years to recover the initial costs, or 'strain', of selling and setting up an account. Managing our financial strain will be an important feature of our activities in the coming years as we seek to grow the organisation and maintain a satisfactory level of capital by keeping costs under control.

The success of the CTF has brought many new customers to **engage** as can be seen in the chart below. It should be noted that we always aim to offer all our customers the same standard of value and service, regardless of which type of policy they hold or which subsidiary provides their product.

group customers



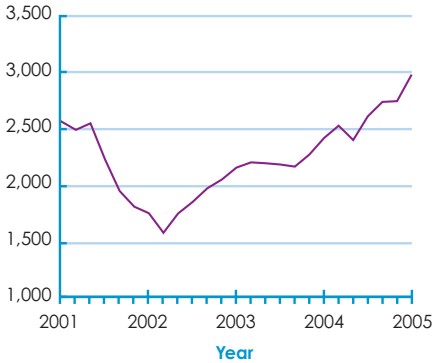
It was a successful year for the With Profits sub fund and the UK brands. We have continued to promote the UK Civil Service Benefit Society brand following the transfer of engagements in 2003, and we launched the UK Armed Forces Benefit Society brand in 2004 to support our activities with NAAFI Financial. We saw good new business growth in 2005 from new and existing customers with maturing polices.

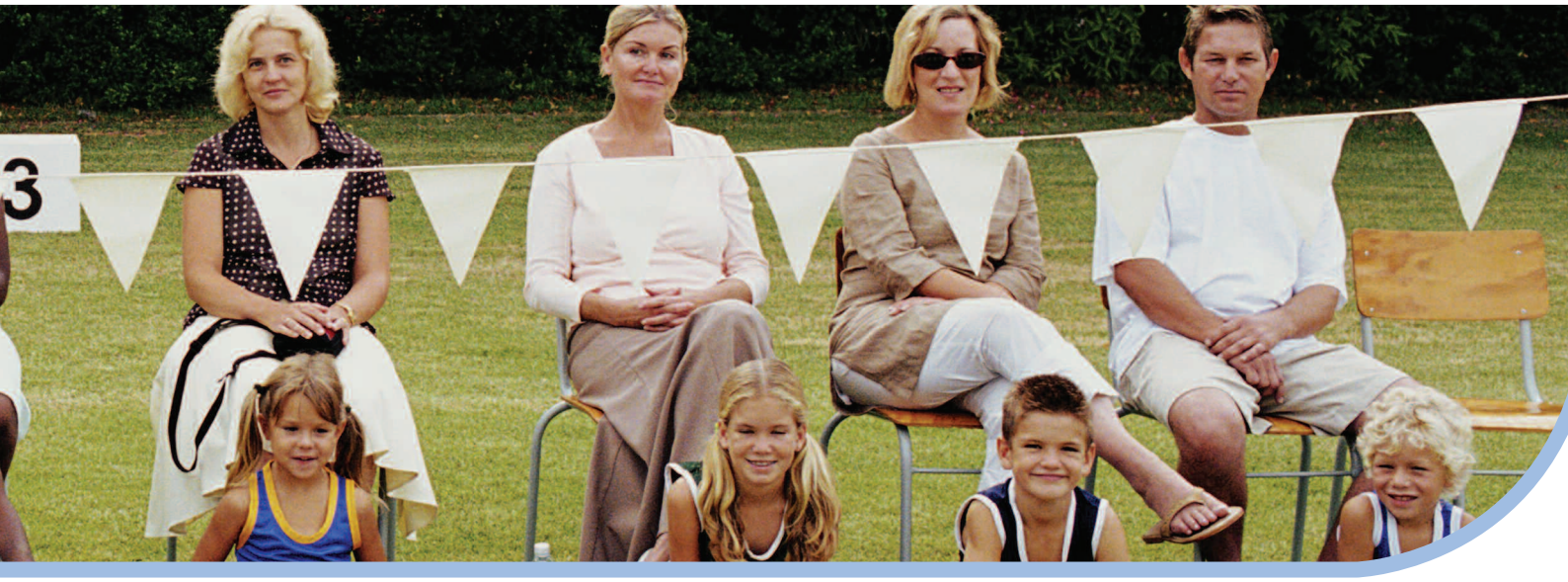
investment performance

In general, 2005 proved to be a very stable environment for UK based savings and investments.

It proved a successful period for the UK stock market and by the end of the year the FTSE All Share index had risen by more than 18%, predominantly driven by energy companies benefiting from higher oil prices and significant returns for those companies who serve the rapidly growing Chinese economy.

FTSE All Share index





Stock market based investments should be regarded with a medium to long-term time frame, i.e. five to ten years. As customers you should also be aware that the value of stock market based investments can fall or rise and in some circumstances investors may not get back all they have invested.

The Bank of England kept base rates unchanged at 4.75% until August 2005, when economic indicators led them to lower rates to 4.50%, this being the only movement during the year.

Many **engage** customers have their policies invested in deposits. The average tax-free return for our deposit-based policies in 2005 rose to 4.85% before charges.

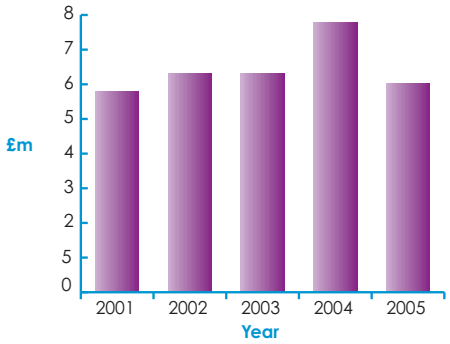
achieving our long term objectives

The long term goals for the Society continue to focus on an increase in the scale of our operations and sustaining that scale with an increased flow of new business. In that way, we will be able to achieve a cost of operation that enables us to deliver simple, good value savings and protection products to a growing customer base.

It is pleasing to note that in a year when we completely rebranded our operations and attracted three and a half times the volume of new business in the previous year, our operating expenses remained within our planned budgets.

Keeping control of expenses will continue to be a priority as we invest to grow the organisation and build an increasingly efficient operating model and continued quality service for customers.

society administrative expenses



increase in scale

Organic growth through initiatives such as CTF is one aspect of our long term plans. Another is to achieve growth through third party administration and transfer of engagement. We are proud of the successful transfer of the UK Civil Service Benefit Society in 2003 and, two years on, we can clearly demonstrate how we upheld the principles of the transfer to the overall benefit of the combined membership of both organisations. The UK brand continues to thrive and is an important part of our continued operations. We are keen to build on that success and maintain an open dialogue with other Societies who may have an interest in pursuing a similar initiative.

We have maintained a strong relationship with Pension Annuity Friendly Society, who demutualised last year and changed their name to Partnership Assurance and for whom we provide administration services through our subsidiary **engage** Mutual Administration Limited. Again, we are always keen to speak to organisations who are interested in pursuing a similar initiative.

our products

We aim to offer our customers a range of products rather than specialise in just one specific type of product. CTF has been a welcome addition to our range and upholds our principles of simple, good value product design. But we do not just provide for children, our product range includes unit linked and with profits savings plans, term assurance, guaranteed acceptance Over 50s Life Insurance, OEICs and equity ISAs. In 2006 we will look to further enhance our savings products to all generations to make them relevant, ensuring that all our customers have access to the best service and value we can provide in protecting their families' welfare.

new business partnerships

Our most significant new partner in 2005 was ASDA. Through ASDA we are able to reach millions of potential customers each week in over 300 stores across the country. We have quickly developed a strong working relationship with ASDA which has made them an important national distributor of the Child Trust Fund. We look forward to developing the relationship further in 2006.

We have a tradition of building effective distribution relationships with third parties. Our partnership with NAAFI Financial has enabled us to offer a range of savings and investment products to young soldiers who perhaps would not save otherwise. It has also filled an important gap in CTF distribution, making the CTF readily accessible to members of the Armed Forces.

We also welcomed a dozen building societies, including Yorkshire, Skipton, Leeds, Scarborough and Darlington, together with a number of friendly societies. In 2006 we are very pleased to have been appointed to provide CTFs to customers of Legal & General and will look to develop a successful relationship with our most recent partner, Debenhams, whilst looking to add new partners during the year.

engage products are now available through more channels and outlets than ever before.

social and environmental issues

The very nature of our organisation means that we do not have a significant environmental impact in the way that industrial companies do. However, we take our responsibilities seriously and have, for example, introduced a recycling scheme within the business. Within our basic mission of encouraging people to save, we acknowledge the fact that the organisation can have a significant social impact. We are keen to develop initiatives which enable us to serve the less well off and last year, for example, we developed a project with housing associations to provide CTF literature to their tenants, many of whom would not have been approached by other financial organisations.

We support local welfare oriented charities and encourage our staff to do the same. We seek feedback from staff across many issues in the workplace and completed a benchmark survey in 2005 against which I will be able to report progress next year.

customer feedback

We always welcome customer feedback, particularly if it helps identify a weakness or strength in our service that we can seek to improve, or where there is good news, do more of. Market Research has been a useful technique through which we have understood customers' product and service requirements. It also played an essential role in helping us to make the right choices in our recent change of trading style.

We have now decided to add more structure to our feedback processes and have established a customer panel which will be consulted on issues such as changes to service or product design. We are keen to hear from any customer who wishes to be available for such consultation, either through the Customer Panel page on our website **www.engagemutual.com** or by writing to the Company Secretary at the Society's address.

outlook for 2006

Our main challenge will be to continue to grow so that we achieve the efficiencies required to run the organisation effectively, while managing our capital and expenses carefully to preserve our long term stability. A great deal was achieved in 2005 towards that goal and we expect 2006 to be a year when the benefits of that hard work will really become evident. We have an increasingly strong brand, excellent distribution partners and a relevant, good value product range. We will continue to work hard in 2006 to ensure we provide customers with the value and quality of financial services products that they require and expect from us.

thanks

We made great progress last year but it would not have been possible without the commitment of the staff and the continued loyalty of our customers. Thank you all. We look forward to a very successful 2006.

Andrew Haigh
Chief Executive
23 February 2006

directors' report for the year ended 31 December 2005

The Directors present their annual report, together with the financial statements and Auditor's report for the year ended 31 December 2005.

business objectives

The mission of **engage** is to enable people to protect their welfare. We will do this by providing our customers with accessible, simple, value for money protection and savings products.

Our major subsidiaries are playing an increasingly important role in meeting the mission:

- **engage** Mutual Funds Limited is the provider of our stakeholder Child Trust Fund, along with our equity ISA product. Homeowners Investment Fund Managers Limited changed its name to **engage** Mutual Funds Limited on 25 January 2006.
- **engage** Mutual Administration Limited, our administration services subsidiary, provides services to other organisations, creating an income which can be used to offset our operating expenses. The subsidiary also employs all of the staff of **engage**. Homeowners Financial Administration Limited resolved to change its name to **engage** Mutual Administration Limited on 23 February 2006.

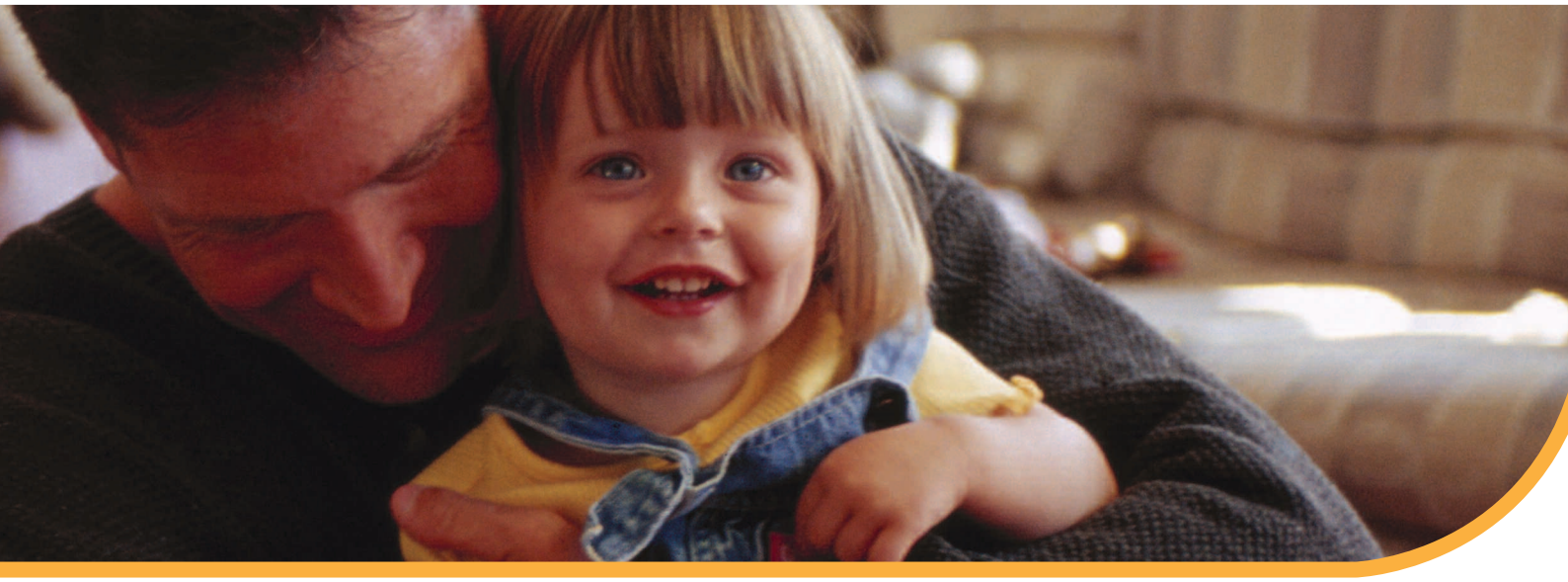
The role of the subsidiaries and the impact on the finances of the Society is such that we present consolidated accounts for the Group.

The Board is committed to the ongoing development of **engage** as a leading Friendly Society, delivering a range of good value, welfare products to a wide audience through direct, worksite and partnership distribution.

The Directors are of the opinion that all activities performed during the year by the Society and its subsidiaries have been carried out within their respective powers.

development of business

Key business developments and the future outlook for the business of the Society and its subsidiaries are detailed in the Chief Executive's Business Review on pages 8 to 13.



board of directors

A list of Directors who held office during the year appears within the 'society information' on page 2.

Christina McComb was appointed as a Director on 11 May 2005 and Peter Mason on 9 December 2005 and, being eligible, offer themselves for election to the Board of Directors. Gordon Murison retired on 12 May 2005. The Board wishes to acknowledge his contribution, in particular, for the successful transition of the ex UK Civil Service Benefit Society (UKCSBS) business into the Society. Kevin Chidwick resigned on 26 August 2005. Graham Henderson was appointed as Finance Director on 23 February 2006.

Lord Clark and Andrew Haigh retire in accordance with the Society's rules and the Friendly Societies Act 1992 and, being eligible, offer themselves for re-election.

As at the year end, no Director of the Society had any interest in the shares of the Society's subsidiary companies.

The Society maintains Directors' and Officers' Insurance for the Board of Directors in respect of their duties as members of the Board.

statement of solvency

As at 31 December 2005, the Society's capital resources for each class of relevant business exceeded the minimum capital resources requirements prescribed by the Financial Services Authority's "Integrated Prudential Sourcebook".

membership

Membership of the Society as at 31 December 2005 stood at 234,015 (2004: 239,056).

complaints policy

We aim to deliver the highest possible level of service to our customers. If any customer believes that we have failed in this aim, they have recourse to our complaints procedures.

We have documented procedures for the handling and recording of complaints. We deal with all complaints with due care, ensuring that they are thoroughly investigated. The Board of Directors regularly reviews the number and type of complaints received to monitor that complaints are properly dealt with and corrective action has been taken to prevent recurrence.

Senior management deals with serious complaints. In the unlikely event that a complaint cannot be resolved to the customer's satisfaction, the customer will be made aware of the option to appeal to the Financial Ombudsman Service.

employees

The average number of Directors and staff employed by the Group, in each week of the year, totalled 192. The aggregate remuneration paid to Directors and staff employed by the Group, during the year, amounted to £5,161,000. All of the staff are employed by our third party administration subsidiary, **engage** Mutual Administration Limited.

The Society's management meets employee representatives regularly to discuss a wide range of topics, through its staff forum. Communication with and between all employees is subject to regular review and includes staff satisfaction surveys, team briefings and informal meetings with the Chief Executive.

engage has an equal opportunities policy for recruitment and is committed to the ongoing development of its staff. The Society has been officially recognised as an 'Investor in People' since 2001.

pensions arrangements

We are committed to assisting our staff to make adequate provision for their retirement, and to this end the accounts show a small surplus on our defined benefit scheme. This scheme closed to new members on 29 March 2001. The Directors are working with the trustees to seek to manage the pension scheme investment policy to ensure that the scheme remains in a position to meet its obligations going forward in a manner which should not place a material financial strain on the Society.

For employees joining the Society since April 2001 we have a defined contribution arrangement in place whereby the Society matches the employee's contributions with a maximum corporate contribution of 10% of salary.

charitable donations

In 2005 we donated £9,191 to charities, which included donations to local charities, St Michael's Hospice and Martin House Hospice as well as donations to SCOPE, British Heart Foundation, Children in Need and the Breast Cancer and Tsunami Appeals. We met all the costs of maintaining the grounds that we share with our local Hospice.

Our staff fully support charities and have donated £1,589 to Children in Need, Cancer Research, SCOPE and the Breast Cancer Appeal as well as donations to local charities, St Michael's Hospice, Martin House Hospice, Harrogate Hospital and the Jake Burgess Appeal.

More recently, **engage** has been officially recognised as having one of the country's most successful Give as You Earn schemes and was awarded the Payroll Giving Gold Award. This honour recognised the number of our employees who had enrolled on the scheme and was presented to the Society in February 2006.

re-appointment of auditors

A resolution to re-appoint KPMG Audit Plc as Auditor will be proposed at the forthcoming Annual General Meeting. Auditors are rotated at least once every seven years with a full review process being conducted every three years.

By Order of the Board
Andrew Horsley
Secretary
23 February 2006

corporate governance report

The Board is accountable to the Society's members for the operation of the Society and regards good corporate governance as being fundamental to this responsibility. It has been the Society's policy to follow the principles of the Combined Code on Corporate Governance matters for a number of years. As a result, the Board has welcomed the recommendations of the Myners Review and the introduction of the Annotated Combined Code. The Board is firmly of the view that, to comply with best practice in corporate governance, it should aim to adhere to the principles and provisions of the Combined Code on Corporate Governance annotated by the Association of Mutual Insurers and the Association of Friendly Societies to cover mutual insurers ("the Code").

It will be our policy to observe the Code wherever appropriate for an organisation of our size, status and aspiration or to clearly explain why we feel any deviation from the Code is acceptable or necessary. The Board considers that it complies with all aspects of the Code unless the contrary is stated within this Report.

The Board applies principles of good governance by adopting the following procedures:

- the Board meets a minimum of six times a year for Board meetings and, in addition, meets at least twice a year for a detailed review of the Society's strategy;
- the Board's principal role is to focus on the Society's strategy and ensure that the necessary resources are in place for the Group to meet its objectives and that financial control and risk management procedures are robust. In particular, its role is to provide general direction to the organisation and to safeguard the interests of members;
- the Board maintains a schedule of retained powers relating to approval of the strategic aims of the Group as well as approval of policies and matters which must be approved by the Board under legislation and the Society's rules;
- to ensure that the Board functions effectively, all Directors receive accurate, timely and clear information and it is the responsibility of the Chairman to ensure that this is periodically reviewed;
- the Chairman also ensures that, on appointment, Non-Executive Directors receive a comprehensive tailored induction programme on the Group's business and regulatory environment. All Non-Executive Directors update their skills, knowledge and familiarity with the Group through meetings with the Executive of the Society and its employees and relevant external courses. Individual training requirements for Non-Executives are discussed during the performance evaluation process;
- the Board has access to independent professional advice at the Society's expense, where they judge it necessary to discharge their responsibilities as Directors;
- all Directors have access to the advice and services of the Group Secretary who is responsible for ensuring the Board procedures are complied with and advising the Board, through the Chairman, on governance matters;
- the Board currently consists of three Executive Directors and six Non-Executive Directors. The size and composition of the Board is kept under review to ensure that there is adequate succession planning for Executive and Non-Executive Directors and that there are sufficient skills and experience represented on the Board for the direction of the Group's activities. The Board is of the opinion that the composition of the Board is appropriate for the business.

attendance of directors at board and committee meetings

Board Meetings	Ray Pierce	David Hargrave	Andrew Haigh	Kevin Chidwick	Lord Clark	Penny Hemming	Chris Lazenby	Peter Mason	Christina McComb	Gordon Murison
HFS (12)	12	12	12	7 of 7	11	11	11	1 of 1	6 of 8	5 of 5
eMFL* (6)	6	4 of 4	6	5 of 5	4 of 4	3 of 4	6	N/A	3 of 4	N/A
HMSL (1)	1	1	1	1	1	N/A	1	N/A	N/A	1
eMAL** (1)	1	1	1	1	1	N/A	1	N/A	N/A	1
eMSL*** (1)	1	1	1	1	1	N/A	1	N/A	N/A	1
Committee Meetings										
Audit (4)	N/A	4	N/A	N/A	4	2 of 2	N/A	1 of 1	1 of 1	2 of 2
Finance & Risk (6)	N/A	6	N/A	3 of 3	N/A	N/A	N/A	6	N/A	N/A
Nominations (2)	2	1 of 1	2	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Remuneration (3)	3	N/A	N/A	N/A	3	0 of 1	N/A	N/A	1 of 1	2 of 2

* Homeowners Investment Fund Managers Limited changed its name to **engage** Mutual Funds Limited (eMFL) on 25 January 2006.
** Homeowners Financial Administration Limited resolved to change its name to **engage** Mutual Administration Limited (eMAL) on 23 February 2006.
*** UK Friendly Insurance Services Limited resolved to change its name to **engage** Mutual Services Limited (eMSL) on 23 February 2006.

non-executive directors

In the opinion of the Board, each Non-Executive Director, including the Chairman, is independent in character and judgement. The Vice Chairman, David Hargrave has served the Society since his first election by members in 1982. Lord Clark has served the Society, as a Non-Executive Director, from 1989 until he left to join the Cabinet in 1997. Lord Clark re-joined the Board in 1999. The Board is unanimously of the view that David Hargrave's and Lord Clark's knowledge and experience remain invaluable to the Society and that the independence of their judgement will not be prejudiced by a continuation of their period in office.

The Society does not have a Senior Independent Director, as we regard the appointment of a Senior Independent Director as inappropriate to an organisation of our size and structure.

The Non-Executive Directors meet without the Executive Directors present at least once a year.

chairman and chief executive

The roles of the Chairman and Chief Executive are held by different people and are distinct in their purpose. The Chairman is responsible for leadership of the Board and ensuring that the Board acts effectively.

The Chief Executive has overall responsibility for managing the Society and its subsidiaries and for implementing the strategies and policies agreed by the Board.

performance evaluation

The Group has a formal performance evaluation system for all members of staff including the Executive Directors. The Chief Executive appraises the Executive Directors on their performance and the Chairman undertakes an appraisal of the Chief Executive.

A performance evaluation system for Non-Executive Directors, including the Chairman, has been established. The Chairman meets each Non-Executive Director annually to discuss individual performance. A meeting of the Non-Executive Directors is also held, without the Executive Directors present, to discuss collectively the performance of the Executive Directors.

In 2005 the appraisal of Non-Executive Directors took the format of an appraisal of each individual Director by the Chairman through the completion of a questionnaire. The Chairman reviewed the output of all questionnaires and used this as a basis for an evaluation interview with each Non-Executive Director. This procedure identifies any individual and Board training requirements and provides the evidence for the Board to decide whether to recommend to members that a Director should be re-elected.

appointments to the board

The appointment of new Directors is considered by the Nominations Committee (see page 21) which makes recommendations to the Board. All Directors are subject to election by members at the Annual General Meeting (AGM) following their appointment. In addition, all Directors must receive approval from the Financial Services Authority as an Approved Person in order to fulfil their controlled function as a Director. Under the Society's Rules, Directors have to submit themselves for re-election at least once every three years.

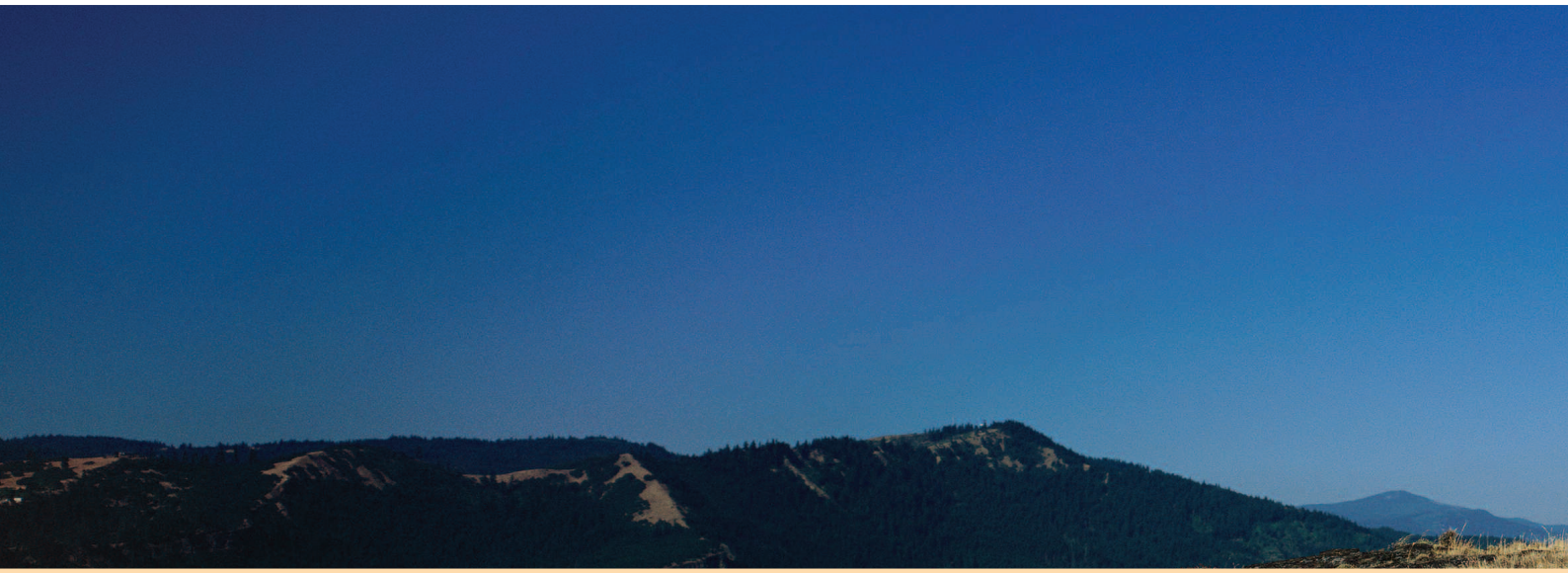
At the AGM to be held in 2006, members will be asked to elect Christina McComb, Peter Mason and Graham Henderson, and re-elect Andrew Haigh and Lord Clark.

Given their particular individual expertise and experience and performance to date, the Board recommends that Christina McComb, Peter Mason and Graham Henderson be put forward for election and Andrew Haigh and Lord Clark be put forward for re-election by members.

The terms and conditions of appointment of Non-Executive Directors are available for inspection at our Head Office and can be viewed by contacting the Secretary.

board committees

The Board has established a number of Committees which have their own terms of reference. Details of the principal Board Committees, including their membership during 2005, are set out overleaf.



audit committee

The Audit Committee consists of four Non-Executive Directors which, with effect from 1 January 2006, falls under the Chairmanship of Peter Mason. Three of the Committee members, Peter Mason, Christina McComb and David Hargrave, have relevant financial sector experience. The other Committee member is Lord Clark. The responsibilities of the Committee are in line with the provisions of the Smith Guidance on Audit Committees. The main function of the Committee is to assist the Board in fulfilling its oversight responsibilities, specifically the ongoing review, monitoring and assessment of:

- the integrity of the financial statements and reviewing significant financial reporting judgements contained in them;
- the effectiveness of systems of internal control and risk management processes;
- the internal and external audit processes;
- compliance with applicable laws and regulations;
- the recommendation to the Board on the appointment, re-appointment and removal of External Auditors.

During 2005 the Committee met four times in the execution of its responsibilities. During the meetings the Committee considered reports on:

- the system of internal control;
- the integrity of financial statements;
- high level risks and associated controls;
- compliance with laws and regulations, including adherence to Money Laundering and Health & Safety regulations; and
- the activities of internal audit and of the External Auditors on the audit.

Reports were provided by the Internal Audit, Risk and Compliance functions and the External Auditors. The Chairman of the Audit Committee meets regularly with the Internal Auditor to discuss issues of internal control.

The Committee considers that it has met its responsibilities and performed its duties with appropriate levels of care and expertise during 2005.

finance & risk committee

The Finance & Risk Committee consists of Peter Mason, Graham Henderson, the Finance Director, and Trevor Batten, the Actuarial Function Holder and With Profits Actuary, under the Chairmanship of David Hargrave. The Committee met six times during 2005 to review the Group's financial management in greater detail than is possible at regular Board meetings. In particular, the Board has charged the Committee with providing direction and recommending strategy in the areas of management of the Society's with profit business, management of the Group's investment strategy and monitoring of the Group's investment performance. In September 2005, the purposes of the Committee were expanded to include a review of the principles underlying capital management of the Group, product pricing for all Group products, the expense analysis and FSA returns.

nominations committee

The Nominations Committee consists of the Chairman, the Vice Chairman and the Chief Executive. It meets as appropriate to review the structure, size and composition of the Board and to make recommendations to the Board with regard to any adjustments that are deemed necessary. It is also responsible for identifying and nominating for the approval of the Board, candidates to fill Board vacancies as and when they arise.

We appointed professional recruitment consultants to ensure that vacancies were brought to the attention of as wide an audience as possible. All applicants were independently appraised by external consultants and a short list was drawn up, prior to interview by the Board and appointment.

remuneration committee

The Remuneration Committee currently consists of the Chairman of the Society and three independent Non-Executive Directors, under the Chairmanship of Christina McComb. Christina McComb took over Chairmanship of the Remuneration Committee from the Chairman of the Society on 9 December 2005. The Committee meets as appropriate to determine the policy for executive remuneration. The objective of the Committee is to give Executive Directors encouragement to enhance the Society's performance by ensuring that they are fairly and responsibly rewarded for their individual and collective contributions. Further details of the Committee and the remuneration policy can be found in the Report of the Directors on Remuneration on pages 24 to 25.

Where the Society appoints remuneration consultants, they have no other connection with the Society.

The full terms of reference of the Audit, Finance & Risk, Nominations and Remuneration Committees are available on request from the Group Secretary or by viewing our website at **www.engagemutual.com.**

relations with customers

The customers of the **engage** Group are made up of the Friendly Society's life fund members and non-life customers of its open ended investment subsidiary company. **engage** applies the same principles of value and service to all customers and encourages feedback on any aspect of the Group's activities.

The **engage** Group has recently established a customers' panel, consisting of around 200 customers, who are invited to comment on a variety of issues. It is the intention of the Society that members of the Board will attend meetings of the panel and use this as an opportunity to understand customers' issues and concerns.

All members of the Friendly Society who are eligible to vote are encouraged to exercise their vote at the AGM by sending to them a proxy voting form and pre-paid reply envelope. A separate resolution is proposed on each separate issue including a resolution on the Annual Report and Accounts.

system of internal control

The Board has delegated responsibility for managing the system of internal control to senior management. The Internal Audit function provides independent assurance to the Board on the effectiveness of the system of internal control through the Audit Committee.

The information received and considered by the Committee provided reasonable assurance that during 2005 there were no material breaches of control or regulatory standards and that, overall, the Group maintained an adequate system of internal control.

auditor

The Group has a policy on the use of the External Auditor for non-audit work which is implemented by the Audit Committee. The purpose of the policy is to ensure the continued independence and objectivity of the External Auditor. The External Auditor, KPMG Audit Plc, undertook a number of non-audit assignments during 2005 and these were conducted within the limits set out in the policy and are considered to be consistent with the professional and ethical standards expected of the External Auditor in this regard.

role as an institutional shareholder

The Group has appointed State Street Global Advisers and more recently in 2006 Legal & General Investment Management to undertake its fund management. Both fund managers comply with the principles set out in "The responsibilities of institutional shareholders and agents – statement of principles" published by the Institutional Shareholders Committee.

The Group has requested State Street and Legal & General to consider carefully the explanations given by companies in which they have invested for any departure from the Combined Code and to make reasoned judgements in each case. Our fund managers use the ABI and Research, Recommendations & Electronic Voting (RREV) services to analyse resolutions for compliance with the Combined Code. Where the fund manager does not accept the explanation for any major departure from the Combined Code, the fund manager will enter into dialogue directly with the company in question. Arrangements are currently being made to ensure that the Board is made aware, through the quarterly report of any issues of significance.

Our fund managers have procedures to check that proxy votes have been received. Arrangements are currently being made to ensure that the Board is made aware, through the quarterly report, of the total number of resolutions and the number of company resolutions that the fund manager voted against or abstained.

Our fund managers also attend AGMs of companies in which they have invested, on behalf of the Society, where it is appropriate and practicable to do so.

creditor payment policy

It is the Society's policy to settle invoices in accordance with suppliers' standard terms, unless specifically agreed otherwise in advance.

statement of the directors' responsibilities

The Directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations. Friendly Society law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with UK Accounting Standards. The financial statements are required by law to give a true and fair view of the state of affairs of the Society and of the income and expenditure of the Society for that period. In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Society and enable them to ensure that its Financial Statements comply with the Friendly Societies Act 1992. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Society and to prevent and detect fraud and other irregularities. Under applicable law the Directors are also responsible for preparing a Directors' Report that complies with that law.

report of the directors on remuneration

The composition and responsibilities of the Society's Remuneration Committee are set out on page 3 and 21 respectively. The Remuneration Committee is responsible for the Group's Executive remuneration policy. The objective of the Committee is to give Executive Directors encouragement to enhance the Society's performance by ensuring that they are fairly and responsibly rewarded for their individual contributions. Where possible the Committee seeks to meet the standards set out in the Combined Code applicable to listed companies.

The level of remuneration is set by reference to jobs carrying similar responsibilities in similar organisations. There is a performance-related element within the remuneration, which is linked to the achievement of objectives.

Proper regard is paid to the need to retain good quality, highly motivated staff and the remuneration being paid by competitors of the Society is taken into consideration. In this respect the Committee receives information inter alia from a leading firm of remuneration consultants, Hay, and also receives benchmarking data where required.

the total emoluments of the Directors, comprise:

	salary £'000	bonus £'000	benefits £'000	**sub-total £'000**	pension contributions £'000	**2005 total £'000**	2004 total £'000
Executive Directors							
Andrew Haigh (Chief Executive)	174	40	1	**215**	24	**239**	200
Kevin Chidwick (resigned 26 August 05)	82	-	1	**83**	8	**91**	141
Chris Lazenby	109	9	1	**119**	10	**129**	127
Total	365	49	3	**417**	42	**459**	468

The remuneration of our Non-Executive Directors is recommended by the Chairman and the Chief Executive for the Remuneration Committee to agree annually at the year end. The remuneration is calculated on the basis of an agreed minimum number of days committed to Society business, and is paid at a rate, which has been confirmed as competitive, when compared with other similar sized financial services organisations.

	salary £'000	bonus £'000	benefits £'000	**sub-total £'000**	pension contributions £'000	**2005 total £'000**	2004 total £'000
Non-Executive Directors							
Ray Pierce (Chairman)	60	-	1	**61**	-	**61**	58
Lord Clark of Windermere	26	-	1	**27**	-	**27**	18
David Hargrave	36	-	1	**37**	-	**37**	50
Penny Hemming	24	-	-	**24**	-	**24**	5
Peter Mason (appointed 9 December 05)	1	-	-	**1**	-	**1**	-
Christina McComb (appointed 11 May 05)	14	-	-	**14**	-	**14**	-
Gordon Murison (retired 12 May 05)	10	-	1	**11**	-	**11**	24
Total	171	-	4	**175**	-	**175**	155

service contracts

Andrew Haigh and Chris Lazenby have service contracts with a twelve-month notice period. The standard terms for Executive Directors include a contractual notice period of 12 months. Graham Henderson is employed on an 18 month fixed term contract from 1 January 2006.

No Non-Executive Director has a service contract.

non-executive directors' remuneration

Non-Executive Directors' remuneration comprises a specified fee, which includes extra amounts for specific additional responsibilities, as set out on page 2.

executive bonus entitlements

The Society operates an annual discretionary bonus scheme for Executive Directors. The Society's policy is to ensure that Executive Directors are appropriately incentivised to meet the objectives of the business.

The Chief Executive is awarded a maximum of 66% of basic salary for achievement of Society objectives. The Operations Director is awarded a maximum of 15% of basic salary for the achievement of individual objectives with a further maximum of 15% awarded for the achievement of Society objectives.

long-term benefits

The Executive Directors participate in a long-term bonus scheme, based on the long-term performance of the Group. This has been provided for in the financial statements of Homeowners Financial Administration Limited, but is not payable to the Directors until January 2006. The long term bonus scheme ran from 1 January 2002 to 31 December 2005, at its conclusion Andrew Haigh was awarded £70,000. Kevin Chidwick left the Group in August 2005, accordingly no payment was made under the long term bonus scheme. It is anticipated a further long term benefit scheme for the Executive Directors will run for the period 2006 to the end of 2008, subject to the approval of the Remuneration Committee.

directors' pension entitlement

The company operates a defined benefit pension scheme for its employees. This scheme was closed to new entrants on 29 March 2001.

A stakeholder pension scheme is in place for all new employees. Chris Lazenby is a member of the stakeholder pension scheme and Andrew Haigh is a member of the defined benefit pension scheme. The transfer value of Andrew Haigh's pension at 31 December 2005 was £167,610 (2004: £115,113).

other benefits

Also paid in respect of 2005 for former Directors and their spouses was £3,000 pension (2004: £3,000). There were no payments relating to loss of office in 2005 (2004: £Nil).

independent auditor's report

independent auditor's report to the members of Homeowners Friendly Society Limited

We have audited the Group and Society financial statements of Homeowners Friendly Society Limited for the year ended 31 December 2005 which comprise the Group and Society Income and Expenditure Accounts, the Group and Society Balance Sheets and the related notes. These financial statements have been prepared under the accounting policies set out therein. We are also required to report on the Report of the Directors for the year ended 31 December 2005.

This report is made solely to the Society's members, as a body, in accordance with section 73 of the Friendly Societies Act 1992. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

respective responsibilities of the directors and auditors

The Directors' responsibilities for preparing the financial statements in accordance with applicable law and UK accounting standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 23.

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

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it. In addition we report to you if, in our opinion, the Society has not kept proper accounting records, or if we have not received all the information, explanations and access to documents that we require for our audit.

We also report to you our opinion as to whether the Report of the Directors has been prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it, and as to whether the information given therein is consistent with the financial statements.

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

independent auditor's report

basis of audit opinion

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

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

opinion

In our opinion the financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of affairs of the Group and of the Society as at 31 December 2005 and of the income and expenditure of the Group and of the Society for the year then ended.

In our opinion the financial statements have been properly prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it.

In our opinion the Report of the Directors has been prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it and the information given therein is consistent with the financial statements.

KPMG Audit Plc
Registered Auditor
Chartered Accountants
Leeds
23 February 2006

group income and expenditure
for the year ended 31 December 2005

Technical Account - Long Term Business

	notes	2005 £'000	2004 £'000 Restated See Note 1
Continuing Operations			
Earned premiums			
- Gross premiums written	2	38,633	36,620
- Outward reinsurance premiums		(6,735)	(4,650)
Total earned premiums		**31,898**	31,970
Investment income	3	37,045	20,168
Unrealised gains on investments	3	28,841	22,013
Other technical income	13	1,821	445
Total technical income		**99,605**	74,596
Claims incurred			
- Gross claims incurred	4	72,926	63,565
- Outward claims reinsurance		(1,987)	(1,204)
Total claims incurred		**70,939**	62,361
Charge in other technical provisions			
- Change in long term business provision (net of reinsurance)		(7,610)	(9,123)
- Change in technical provisions for linked liabilities		10,291	2,611
- Net operating expenses	5	16,377	14,917
- Investment expenses and charges		298	193
- Other technical charges	13	4,479	701
- Tax attributable to the long term and linked business	8	277	(397)
- Transfer to fund for future appropriations	9	4,554	3,333
Total charge in other technical provisions		**28,666**	12,235
Total technical charges		**99,605**	74,596
Balance on the long term business - technical account		-	-

Share dividends and interest on deposits held

Increased value of investments held

Policy surrender, maturity and death payments

Change in value of linked policyholder's benefits

Fund managers' charges

Group charge to corporation tax

All recognised gains and losses in relation to long term business and subsidiaries are dealt with in the Group income and expenditure – Long Term Business – Technical Account, except in respect of the prior year adjustment.

group balance sheet as at 31 December 2005

Assets

Harrogate head office and Kew Gardens property

With Profits fund and surplus investments

Value of unit linked investments

Fixtures, fittings and computer hardware

Accumulated sales costs that are associated with acquiring new policies and are spread over several years

	notes	2005 £'000	2004 £'000 Restated See Note 1
Investments			
- Investment in land and buildings	10	6,300	6,175
- Financial investments	10	134,359	134,975
Total investments		**140,659**	141,150
Assets held to cover linked liabilities	11	**456,561**	446,270
Reinsurers' share of technical provisions			
- Long term business provision		4,604	2,795
Debtors			
- Other debtors		530	453
Other assets			
- Tangible assets	12	805	689
- Cash at bank		3,255	1,332
- Pension asset	17	546	413
Total other assets		**4,606**	2,434
Prepayments and accrued Income			
- Accrued interest and rent		5,772	5,934
- Deferred acquisition costs		859	2,371
- Other prepayments and accrued income		977	1,883
Total prepayments and accrued income		**7,608**	10,188
Total assets		**614,568**	603,290

group balance sheet as at 31 December 2005

Liabilities

Money held for regulatory reserves and other surplus funds, including possible future with profits bonuses

Provision for with profits policies and other known contingencies

Maturities, surrenders and death claims awaiting processing and payment

Value of unit linked policyholders' benefits

Expenses due in the period yet to be processed

	notes	2005 £'000	2004 £'000 Restated See Note 1
Fund for future appropriations	9	**49,416**	44,862
Technical provisions			
- Long term business provision	14	98,126	103,927
- Claims outstanding	14	6,768	4,170
Total technical provisions		**104,894**	108,097
Technical provisions for linked liabilities	14	**456,561**	446,270
Creditors			
- Creditors arising out of insurance operations	15	261	818
- Other creditors including taxation and social security	16	2,818	1,456
Total creditors		**3,079**	2,274
Accruals and deferred income		618	1,787
Total liabilities		**614,568**	**603,290**

Prior year adjustment to fund for future appropriations	
Balance at 1 January 2004 as previously reported	41,951
Prior year adjustment (see note 1)	(422)
Transfer from restated income and expenditure account	3,333
Balance at 31 December 2004 as restated	**44,862**

Details of the prior year adjustment are disclosed fully in note 1 to the accounts.

Approved at a meeting of the Board of Directors on 23 February 2006 and signed on its behalf by:

R F Pierce *- Chairman*

A Haigh *– Chief Executive*

A J Horsley *– Secretary*

society income and expenditure
for the year ended 31 December 2005

Technical Account - Long Term Business

	notes	2005 £'000	2004 £'000
Continuing Operations			
Earned premiums			
- Gross premiums written	2	38,633	36,620
- Outward reinsurance premiums		(6,735)	(4,650)
Total earned premiums		**31,898**	31,970
Investment income	3	37,045	20,168
Unrealised gains on investments	3	28,841	22,013
Other technical income	13	688	695
Total technical income		**98,472**	74,846
Claims incurred			
- Gross claims incurred	4	72,926	63,565
- Outward claims reinsurance		(1,987)	(1,204)
Total claims incurred		**70,939**	62,361
Charge in other technical provisions			
- Change in long term business provision (net of reinsurance)		(7,610)	(9,123)
- Change in technical provisions for linked liabilities		10,291	2,611
- Net operating expenses	5	16,377	14,917
- Investment expenses and charges		298	193
- Tax attributable to the long term and linked business	8	278	(399)
- Transfer to fund for future appropriations	9	7,899	4,286
Total charge in other technical provisions		**27,533**	12,485
Total technical charges		**98,472**	74,846
Balance on the long term business - technical account		-	-

Share dividends and interest on deposits held

Increased value of investments held

Policy surrender, maturity and death payments

Change in value of linked policyholders' benefits

Fund managers' charges

Society charge to corporation tax

All recognised gains and losses in relation to long term business are dealt with in the Society income and expenditure – Long Term Business – Technical Account.

society balance sheet as at 31 December 2005

Assets

Harrogate head office and Kew Gardens property

With Profits fund and surplus investments

Value of unit linked investments

Accumulated sales costs that are associated with acquiring new policies and are spread over several years

	notes	2005 £'000	2004 £'000
Investments			
- Investment in land and buildings	10	6,300	6,175
- Financial investments	10	134,359	134,975
Total investments		**140,659**	141,150
Assets held to cover linked liabilities	11	**456,561**	446,270
Reinsurers' share of technical provisions			
- Long term business provision		4,604	2,795
Debtors			
- Other debtors		7,204	4,072
Other assets			
- Cash at bank		3,006	669
Total other assets		**3,006**	669
Prepayments and accrued income			
- Accrued interest and rent		5,772	5,934
- Deferred acquisition costs		859	2,371
- Other prepayments and accrued income		684	1,494
Total prepayments and accrued Income		**7,315**	9,799
Total assets		**619,349**	604,755

society balance sheet as at 31 December 2005

Liabilities

Money held for regulatory reserves and other surplus funds, including possible future with profits bonuses

Provision for with profits policies and other known contingencies

Maturities, surrenders and death claims awaiting processing and payment

Value of unit linked policyholders' benefits

Expenses due in the period yet to be processed

	notes	2005 £'000	2004 £'000
Fund for future appropriations	9	**55,812**	47,913
Technical provisions			
- Long term business provision	14	98,126	103,927
- Claims outstanding	14	6,768	4,170
Total technical provisions		**104,894**	108,097
Technical provisions for linked liabilities	14	**456,561**	446,270
Creditors			
- Creditors arising out of insurance operations	15	261	818
- Other creditors including taxation and social security	16	1,203	763
Total creditors		**1,464**	1,581
Accruals and deferred income		**618**	894
Total liabilities		**619,349**	**604,755**

Approved at a meeting of the Board of Directors on 23 February 2006 and signed on its behalf by:

R F Pierce *- Chairman*

A Haigh *– Chief Executive*

A J Horsley *– Secretary*

1.accounting policies

basis of presentation

The Accounts are prepared on the basis of the accounting policies set out below. The Accounts have been prepared in compliance with the Friendly Societies (Accounts and Related Provisions) Regulations 1994 and with the Association of British Insurers' Statement of Recommended Practice on Accounting for Insurance Business ("ABI SORP"), dated December 2005. In implementing the requirements of these regulations, the Society has adopted a modified statutory solvency basis for determining technical provisions. The true and fair override provisions of the Companies Act 1985 have been invoked in relation to investment properties (see accounting policies on Investments below).

The Accounts comply with applicable accounting standards.

basis of consolidation

The Group Accounts comprise the assets, liabilities, and income and expenditure account transactions of the Society and its subsidiary undertakings. The ongoing results of subsidiary undertakings are included within Other Technical Income and Other Technical Charges. The net results are included in the Fund for Future Appropriations for the Group. The activities of the Society and Group are accounted for in the income and expenditure – Technical Account.

change of accounting policy

Financial Reporting Standard 17 'Retirement Benefits' ('FRS 17') supersedes Statement of Standard Accounting Practice 24 'Pension Costs' ('SSAP 24'). All the disclosure requirements of FRS 17 were adopted by the Company in the 2003 Accounts. In November 2002, the Accounting Standards Board deferred the effective date of the recognition and measurement elements of the standard to accounting periods beginning on or after 1 January 2005. As such the Company has implemented the recognition and measurement provisions of FRS 17 in 2005 and has restated 2004 comparatives to reflect this.

FRS 17 requires assets in a defined benefit scheme to be measured at their fair value at the balance sheet date. Scheme liabilities are measured using the projected unit method, which takes account of projected earnings increases that are mutually compatible and lead to the best estimate of future cash flows. These cash flows are discounted at the interest rate applicable to high quality corporate bonds of the same currency and term as the liabilities. The surplus (deficit) in a defined benefit scheme is the excess (shortfall) of the value of the assets in the scheme over (below) the value of the scheme liabilities.

A surplus is recognised as an asset to the extent that the employer is able to recover the surplus either through reduced contributions in the future or through refunds from the scheme. A deficit is recognised as a liability to the extent of the employer's legal or constructive obligation to fund it. The current service cost (the increase in the scheme liabilities arising from employee service in the current period), any past service costs (the cost of improvements to benefits for service relating to prior periods), interest cost (the unwinding of the discount on scheme liabilities) net of the expected return on scheme assets and actuarial gains and losses (changes in the surpluses or deficits due to experience of gains and losses) are charged to the technical account in other technical income and other technical charges.

1.accounting policies (continued)

Under SSAP 24 the income and expenditure charge comprised the cost of accruing benefits for active employees offset by a credit for the amortisation of the scheme surplus as measured at the last triennial valuation in 2005. A SSAP 24 debtor was included in the balance sheet, relating to contributions in excess of the charge.

The effect of this change of policy on the technical account has been an increase in other technical charges of £132,000 (2004: £194,000). An FRS 17 pension asset of £546,000 (2004: £413,000) has been recognised on the balance sheet and the 2004 opening SSAP 24 debtor of £805,000 has been eliminated. The total prior year adjustment £422,000 reduced the funds for future appropriation as shown in note 9.

premiums

Premiums are credited when they become due. Reinsurance premiums are charged when they become payable.

claims

Death claims are recorded on the basis of notifications received. Annuity payments are recorded when due. Maturities and surrenders are recorded on the earlier of the date when paid or when the policy ceases to be included within the long-term business provision and / or the technical provision for linked liabilities. Reinsurance recoveries are credited to match the relevant gross amounts.

investment income and expenses

Investment income and expenses include dividends, interest, rents, gains and losses on the realisation of investments and related expenses. Dividends are included as investment income on the date that shares become quoted ex-dividend. Interest, rents and expenses are included on an accruals basis.

Realised gains and losses on investments are calculated as the difference between net sales proceeds and original cost. Unrealised gains and losses are calculated as the difference between the valuation of investments at the balance sheet date and their original purchase price, or if they have been previously valued, their valuation at the last balance sheet date.

The movement in unrealised gains and losses recognised in the year also includes the reversal of unrealised gains and losses recognised in earlier years in respect of investment disposals in the current period.

investments

Investments consist of land and buildings, listed investments, loans secured on house purchases, units in authorised unit trusts, shares in open ended investment companies (OEICs), subsidiary companies and deposits. Land and buildings are included on the basis of independent valuations. Listed investments are included at mid-market value. Units in unit trusts are included at published bid prices. OEICs are included at the published price. Subsidiary companies are valued at the cost of share capital less any provisions. Deposits are included at current value. Mortgage loans are included at amount outstanding less any provision for unrecoverable amounts.

1.accounting policies (continued)

The freehold property investments are valued at open market value. In accordance with SSAP 19, no depreciation is provided in respect of freehold investment properties. This is a departure from the requirements of the Regulations, which require all properties to be depreciated. Depreciation is only one amongst many factors reflected in the valuation of properties and accordingly the amount of depreciation, which might otherwise have been charged, cannot be separately identified or quantified. The Directors consider that this policy results in the Accounts giving a true and fair view.

deferred acquisition costs

The costs of acquiring new insurance contracts are deferred to the extent that they are recoverable out of future revenue margins. Such costs are disclosed as an asset in the balance sheet. The rate of amortisation of the deferred acquisition cost assets is consistent with a prudent assessment of the pattern of receipt of future revenue margins over the period the relevant contracts are expected to remain in force.

technical provisions

The long-term business provision is determined by the Society's Actuarial Function Holder following his annual investigation of the long-term business, which is based on methods and assumptions that have been approved by the Board of Directors. It is calculated initially to comply with the reporting requirements under the Integrated Prudential Sourcebook. This statutory solvency basis of valuation is then adjusted by eliminating certain reserves required under Friendly Society Regulations. This adjusted basis is referred to as the modified statutory solvency basis. The long-term business provision includes the non-linked liabilities in respect of linked business.

The technical provision for linked liabilities is based on the actuarial valuation of the related assets.

uncertainties and estimation techniques

One of the purposes of insurance is to enable policyholders to protect themselves against uncertain future events. Insurance companies accept the transfer of uncertainty from policyholders and seek to add value through the aggregation and management of these risks. The uncertainty inherent in insurance is inevitably reflected in the financial statements of insurance companies and principally arises in respect of the technical provisions of the company.

As a consequence of this uncertainty, the insurance company needs to apply sophisticated estimation techniques to determine the appropriate provisions.

Long-term business provisions are computed using statistical or mathematical techniques, which are expected to give approximately the same results as if an individual liability were calculated for each long-term contract. The computations are made by suitably qualified personnel (employed by the Group) on the basis of recognised actuarial methods. This methodology takes into account the risks and uncertainties of the particular classes of long term business written and the results are certified by the professionals undertaking the valuations.

1.accounting policies (continued)

fund for future appropriations

The fund for future appropriations represents all funds, the allocation of which has not yet been determined by the end of the financial year. Any surplus or deficit arising on the Technical Account is transferred to or from the fund on an annual basis.

deferred taxation

Deferred tax assets and liabilities are recognised in accordance with the provisions of Financial Reporting Standard 19 'Deferred Taxation' ('FRS 19'), issued in December 2000. The Society has chosen not to apply the option available under FRS 19 of discounting such assets and liabilities to reflect the time value of money. Except as set out in FRS 19, deferred tax is recognised in respect of all timing differences that have originated but not reversed by the balance sheet date. Deferred tax assets are recognised only to the extent that it is regarded as more likely than not that they will be recovered.

Allowance is made in the long-term business provision for deferred taxation at appropriate discounted rates in respect of the unrealised gains on investments, unrelieved management expenses and other timing differences.

fixed assets

Depreciation is provided on the cost of assets in annual instalments over their estimated lives. The rates of depreciation applied per annum are as follows:

Fixtures, fittings and office equipment	20% straight line
Computer equipment	25% straight line

The cost of new computer software is depreciated in full in the year in which it is incurred and eliminated from the accounts after five years.

cash flow statement

The Society, being a mutual life assurance company, is exempt from the requirement under Financial Reporting Standard 1 'Cash Flow Statements' ('FRS 1') to produce a cash flow statement.

foreign currencies

Assets and liabilities held in foreign currencies are translated to sterling at rates of exchange ruling at the end of the year. Income and expenditure denominated in foreign currencies are translated at the appropriate rates prevailing during the year.

financial derivatives

The Society's fund managers use derivative financial instruments for efficient portfolio management. The profits or losses arising on these contracts are recognised in the Long Term Business - Technical Account, as they arise. The Society monitors exposure to such instruments on a weekly basis. The fund managers must justify and obtain prior approval from the Society for any exposure in excess of 5% of the underlying fund.

1.accounting policies (continued)

pensions

The Group operates a defined benefit pension scheme for staff whose employment commenced before 6 April 2001, and a defined contribution pension scheme for those whose employment commenced on or after 6 April 2001. Defined benefit scheme liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate that equals the current rate of return on a high quality corporate bond of the equivalent term and currency to the scheme liabilities. Scheme assets are measured at their fair value. Any surplus or deficit of scheme assets over liabilities is recognised in the balance sheet as an asset (surplus) or liability (deficit). An asset is only recognised to the extent it can be recovered through reduced contributions in the future or through refunds from the scheme. The current service cost (the increase in the scheme liabilities arising from employee service in the current period), any past service costs (the cost of improvements to benefits for service relating to prior periods), interest cost (the unwinding of the discount on scheme liabilities) net of the expected return on scheme assets and actuarial gains and losses (changes in the surpluses or deficits due to experience of gains and losses) are charged to the Technical Account.

The Group also administered a pension scheme on behalf of the former UK Civil Service Benefit Society (UKCSBS). The UKCSBS operated a defined benefit scheme, which was closed in July 2002 with staff becoming deferred members of the scheme. The UKCSBS then operated a defined contribution scheme. On 1 September 2004 the UKCSBS scheme was merged with the Homeowners pension scheme.

2. premium analysis

a. Gross premiums written

Society and Group Life Assurance Business	2005 £'000	2004 £'000
Linked contracts:		
- periodic premium	16,363	18,011
- single premium	192	468
Non linked contracts:		
- periodic premium	12,529	10,792
- with profits periodic premium	6,554	7,349
- with profits single premium	2,995	-
Total premiums written	**38,633**	36,620

b. Gross new annualised premiums

Society and Group Life Assurance Business	2005 £'000	2004 £'000
Linked contracts	143	293
Non linked contracts	3,913	3,257
Total new annualised periodic premiums	**4,056**	3,550

3. investment income

Society and Group	2005 £'000	2004 £'000
Income from listed investments	3,429	10,326
Income from other investments	14,283	10,521
Realised gains / (losses) on investments	19,333	(679)
Total investment income	**37,045**	20,168
Unrealised gains on investments	28,841	22,013
Net investment return	**65,886**	42,181

4. claims incurred

Society and Group	2005 £'000	2004 £'000
Gross claims paid	70,329	63,529
Change in provision or claims outstanding at year end	2,597	36
Gross claims incurred	**72,926**	63,565

5. net operating expenses

	Society 2005 £'000	Society 2004 £'000	Group 2005 £'000	Group 2004 £'000
Acquisition costs	13,084	9,609	13,084	9,609
Change in deferred acquisition costs	1,512	2,177	1,512	2,177
Administrative expenses	6,036	7,780	6,036	7,780
Reinsurance commissions and profit participation	(4,255)	(4,649)	(4,255)	(4,649)
Total net operating expenses	**16,377**	14,917	**16,377**	14,917

Also included in Net Operating Expenses are auditor's fees as illustrated below:

	KPMG Audit Plc		KPMG LLP	
	2005	2004	2005	2004
SOCIETY	£'000	£'000	£'000	£'000
Audit services				
- Statutory audit	72	63	-	-
- Audit related regulatory reporting	22	16	-	-
Further assurance services	-	-	12	212
Tax services				
- Advisory services	-	-	-	29
- Compliance services	-	-	24	-
Total	**94**	79	**36**	241

	KPMG Audit Plc		KPMG LLP	
	2005	2004	2005	2004
GROUP	£'000	£'000	£'000	£'000
Audit services				
- Statutory audit	93	81	-	-
- Audit related regulatory reporting	22	18	-	-
Further assurance services	-	-	12	217
Tax services				
- Advisory services	-	-	-	37
- Compliance services	-	-	24	-
Other services				
- Regulatory compliance services	-	1	3	-
- Other	-	-	6	-
Total	**115**	100	**45**	254

Further assurance services provided by KPMG Audit Plc and KPMG LLP in 2004 was largely in relation to due diligence work undertaken by the Group.

6. staff costs

The total staff costs for the Group were comprised as follows:

	2005 £'000	2004 £'000 Restated
Wages and salaries	5,161	4,217
Social security costs	535	477
Other pension costs	(264)	415
Total staff costs	**5,432**	5,109

Total staff costs have been restated due to the adoption of FRS 17, full details are included in note 1. The current service cost and past service credit of the group defined benefit scheme is included in pension costs, full details are in note 17.

The average weekly number of employees in the Group, including Directors. During the year was comprised as follows:

	2005 No.	2004 No.
Administration	145	102
Management	24	26
Marketing	23	15
Total number of staff	**192**	143

All staff are employed and remunerated by Homeowners Financial Administration Limited, which administers the Society's policies. As such no staff are employed directly by the Society.

7. directors' emoluments

Directors' emoluments are shown as part of the Report of the Directors on Remuneration on pages 24 to 25.

8. taxation

	Society 2005 £'000	Society 2004 £'000	Group 2005 £'000	Group 2004 £'000
Corporation tax at 20% and 22% (Society), at 30% (Group Subsidiaries)	-	-	-	2
Adjustment to corporation tax and income tax payable and recoverable relating to prior year	278	15	277	15
Tax credits recoverable on dividends	-	(414)	-	(414)
Total	278	(399)	277	(397)

9. fund for future appropriations

	Society 2005 £'000	Society 2004 £'000	Group 2005 £'000	Group 2004 £'000
Balance at 1 January (2004 previously reported)	47,913	43,627	44,862	41,951
FRS 17 prior year adjustment (see note 1)	-	-	-	(422)
Balance at 1 January as restated	**47,913**	43,627	**44,862**	41,529
Transfer from income and expenditure account	7,899	4,286	4,554	3,333
Balance at 31 December	**55,812**	47,913	**49,416**	44,862

10. investments

a. Property

Society and Group	Current value 2005 £'000	Current value 2004 £'000	Historical cost 2005 £'000	Historical cost 2004 £'000
Land and buildings				
- Property occupied by the Society	5,550	5,550	8,147	8,147
- Property in Kew Gardens	750	625	625	625
Balance at 31 December	**6,300**	6,175	**8,772**	8,772

Land and buildings are freehold. The Society's Head Office was valued on an 'open market with vacant possession' basis as at 22 September 2004, by independent valuers Eddisons Commercial - FRICS, Chartered Surveyors, Leeds in accordance with the RICS Appraisal and Valuation Manual.

The property in Kew Gardens was valued on an 'open market value' basis as at 31 December 2005, by independent valuers Drivers Jonas - FRICS, Chartered Surveyors, London in accordance with the Statement of Asset Valuation Practice and Guidance Notes published by the Royal Institution of Chartered Surveyors.

b. Subsidiaries

The Society owns 100% of the ordinary share capital of the following subsidiaries:

Name of Subsidiary Undertaking	Nature of Business
engage Mutual Funds Limited (formerly Homeowners Investment Fund Managers Limited)	Authorised Corporate Director (ACD) of an OEIC
Homeowners Financial Administration Limited*	Third party administrator
UK Friendly Insurance Services Limited**	Insurance and non-regulated financial product intermediary
Homeowners Membership Services Limited	Dormant company

*Homeowners Financial Administration Limited resolved to change its name to **engage** Mutual Administration Limited on 23 February 2006.

UK Friendly Insurance Services Limited resolved to change its name to **engage Mutual Services Limited on 23 February 2006.

10. investments (continued)

All four companies are registered in England and Wales. The investment in the subsidiaries can be analysed as follows:

Society	Shares in subsidiary undertakings £'000
Cost at 1 January 2005	2,550
Write off	-
Cost at 31 December 2005	**2,550**
Provision at 1 January 2005	(2,550)
Write down	-
Provision at 31 December 2005	**(2,550)**

c. Financial Investments

Society and Group	Current value		Historical cost	
	2005	2004	**2005**	2004
	£'000	£'000	**£'000**	£'000
Other financial investments:				
Shares, other variable yield securities and unit trusts:				
- UK	37,249	51,785	37,259	47,816
- Overseas	-	423	-	404
Debt securities and other fixed income securities	75,854	62,965	75,853	62,899
Mortgage loans	134	134	134	134
Deposits with credit institutions	21,115	19,668	21,115	19,668
Accrued income and receivables	7	-	7	-
Total	**134,359**	134,975	**134,368**	130,921

11. assets held to cover linked liabilities

Society and Group	Current value		Historical cost	
	2005	2004	**2005**	2004
	£'000	£'000	**£'000**	£'000
Assets held to cover linked liabilities	**456,561**	446,270	**456,251**	440,103
These assets are analysed as follows:				
Shares, other variable yield securities and unit trusts	198,176	176,850	197,866	175,891
Debt securities and other fixed income securities	58,367	61,132	58,367	55,924
Deposits with credit institutions	199,944	207,727	199,944	207,727
Accrued income and receivables	74	561	74	561
Total	**456,561**	446,270	**456,251**	440,103

12. tangible assets

Group	office and computer equipment £'000
Cost:	
At 1 January 2005	1,121
Additions	377
Disposals	-
At 31 December 2005	**1,498**
Depreciation:	
At 1 January 2005	432
Provided in the year	261
On disposals	-
At 31 December 2005	**693**
Net book value:	
At 31 December 2005	**805**
At 31 December 2004	689

The charge for depreciation for the Group in the year ended 31 December 2004 was £265,000.

13. other technical income and technical charges

Other technical income in the Society is in relation to rental charged to its subsidiary, Homeowners Financial Administration Limited, for the use of Gardner House. Other technical income in the Group figures refers to income that is wholly earned in the subsidiaries of the Society. Other technical charges in the Group figures refer to expenses that are wholly incurred in the subsidiaries of the Society, together with the acturial loss on the Group pension scheme of £738,000 (2004: £45,000).

14. technical provisions

Society and Group	Long term business provision £'000	Provision for outstanding claims £'000	Technical provision for linked liabilities £'000
At 1 January 2005	103,927	4,170	446,270
Change in other technical provisions	-	-	10,291
Movement in provision for outstanding claims	-	2,598	-
Transfer (to) / from technical account before reinsurers share	(5,801)	-	-
Balance at 31 December 2005	**98,126**	**6,768**	**456,561**

Included within the long-term business provision is a deferred tax liability of £136,000 (£450,000 in 2004) relating to deferred acquisition costs. The long-term business provision has been calculated on the basis of the following principal interest assumptions for 2005:

Class of business	Interest
Linked assurance tax exempt / taxable	3.5% gross / 2.8% net
Life annuities in payments	2.8%
Term assurance / whole of life	2.8%
With profit tax exempt / taxable	3.0% gross / 2.5% net

The mortality assumptions have been based on actual experience with the addition of prudent margins.

15. creditors arising out of insurance operations

All creditors are payable within a period of five years.

16. other creditors including taxation and social security

	Society 2005 £'000	Society 2004 £'000	**Group 2005 £'000**	Group 2004 £'000
Other taxes and social security costs	13	25	165	165
Other creditors	1,190	738	2,653	1,291
Total	**1,203**	763	**2,818**	1,456

17. pension commitments

The Group operates a defined benefit pension scheme for its employees. This Scheme was closed to new entrants on 5 April 2001. A stakeholder pension scheme is in place for all new employees. On 1 September 2004 the UKCSBS scheme was merged with the Homeowners pension scheme to form a single combined pension scheme; at the same time a special contribution of £909,000 was transferred into the former scheme.

The assets of the defined benefit scheme are held separate from those of the Group in an independently administered fund. The contributions are determined by the Scheme Actuary on the basis of triennial valuations.

A full actuarial valuation is performed every three years by the Scheme Actuary, and is updated annually to calculate the present value of scheme liabilities. A full actuarial valuation of the Homeowners Friendly Society Pension Scheme was carried out as at 1 January 2005. The scheme is closed to new entrants. This means that, under the Projected Unit Method, the service cost will increase as the remaining members reach retirement. Scheme assets are stated at their market value at 31 December 2005.

The major assumptions used by the Actuary to calculate Scheme liabilities were:

	2005 % per annum	2004 % per annum	*2003 % per annum
Long term salary progression	4.40	4.40	4.30
Rate of increase in pension payments guaranteed	2.80	2.70	2.70
Discretionary rate of increase in pensions payment	-	1.35	1.35
Rate of price inflation and deferred pension revaluation	2.90	2.90	2.80
Discount rate	4.70	5.30	5.60

**Rates quoted are for the HFS Scheme, and not a combination of the HFS and UKCSBS schemes.*

17. pension commitments (continued)

The total assets and liabilities in the HFS scheme and the expected rates of return were:

	Long-term rate of return expected at 31 December			Value at 31 December		
	2005	2004	**2003	**2005**	2004	*2003
	%	%	%	**£'000**	£'000	£'000
Equities	7.10 pa	7.50 pa	7.75 pa	9,768	8,118	6,912
Bonds	4.10 pa	4.50 pa	4.75 pa	3,767	3,390	2,677
Other	4.50 pa	4.90 pa	4.00 pa	333	454	446
Total market value of scheme assets				**13,868**	**11,962**	**10,035**
Present value of scheme liabilities				(13,322)	(11,549)	(10,561)
Pension asset / (liability)				**546**	413	(526)
Related deferred tax (liability) / asset (at an assumed rate 30%)				(164)	(124)	158
Net pension asset / (liability)				**382**	289	(368)

The group has a deferred tax asset as presented in note 22, as such the pension asset has been stated before any deferred tax liability.

a. Movement in surplus/(deficit) during the year

	2005	2004	*2003
	£'000	£'000	£'000
Surplus/ (deficit) in scheme at 1 January	413	(526)	(437)
Current service cost	(327)	(269)	(233)
Contributions	229	1,133	305
Past service costs	800	-	(16)
Other finance income	169	120	58
Actuarial loss	(738)	(45)	(203)
Surplus / (deficit) in scheme at 31 December	**546**	413	(526)

Contributions in 2004 includes a special contribution which was made by the Society into the pension scheme totalling £909,000.

b. Analysis of net return on pension scheme under FRS 17

	2005	2004	*2003
	£'000	£'000	£'000
Expected return on pension scheme assets	782	711	579
Interest on pension scheme liabilities	(613)	(591)	(521)
Net return	**169**	120	58

The amounts above are included in other technical income in the Group Long-Term Business – Technical Account on page 29.

* 2003 figures have been restated to provide a combined figure for the UKCSBS and HFS pension schemes for comparative purposes.

** Rate quoted is for the HFS scheme, and not a combination of the HFS and UKCSBS schemes.

17. pension commitments (continued)

c. Analysis of income and expenditure account charge under FRS 17

	2005	2004	*2003
	£'000	£'000	£'000
Current service cost	327	269	233
Past service credit	(800)	-	16
Total charge/(credit)	**(473)**	**269**	**249**

The amounts above are included in other technical charges in the Group Long Term Business – Technical Account on page 29.

d. Analysis of actuarial gains and losses

	2005	2004	*2003
	£'000	£'000	£'000
Actual return less expected return on pension scheme assets	1,178	340	624
Experience gains and losses arising on the scheme liabilities	(446)	234	(26)
Changes in assumptions underlying the present value of the scheme liabilities	(1,470)	(619)	(801)
Total actuarial loss	**(738)**	**(45)**	**(203)**

The amounts above are included in other technical charges in the Group Long Term Business – Technical Account on page 29.

e. History of experience gains and losses

	2005		2004		*2003	
	£'000	**%**	£'000	%	£'000	%
Difference between the expected and actual return on scheme assets	1,178		340		624	
Percentage of scheme assets		8.5		2.8		6.0
Experience losses on scheme liabilities	(446)		234		(26)	
Percentage of present value of scheme liabilities		(3.4)		2.0		(0.2)
Total acturial losses recognised	(738)		(45)		(203)	
Percentage of present value of scheme liabilities		5.5		(0.4)		(1.9)

* 2003 figures have been restated to provide a combined figure for the UKCSBS and HFS pension schemes for comparative purposes.

18. operating leases

Society and Group	**2005**	2004
	£'000	£'000
Operating leases which expire		
- within one year	10	13
- between two and five years	37	29
Total	**47**	**42**

19. commitments

There was no capital expenditure contracted but not provided for in the financial statements (2004 nil).

At 31 December 2005, the Society held FTSE Future contracts with a book value of £110,000 (2004 £2,983,000) and a market value of £112,000 (2004 £3,022,000). The unrealised gain on these contracts of £2,000 has been included in the Long Term Business - Technical Account. These contracts are only used for efficient portfolio management of the Society's funds invested in UK equities.

20. statement of information relating to the actuarial function holder

The Actuarial Function Holder of the Society is Mr T M Batten, an employee of the Society. The following information has been provided, in accordance with Section 77 of the Friendly Societies Act 1992:

- Mr T M Batten was not a member of the Society at any time during 2005;
- No other member of his family was a member of the Society during 2005;
- Mr T M Batten is a member of the Homeowners Friendly Society Pension Scheme;
- The aggregate rate of the remuneration and benefits (excluding pension contributions) of Mr T M Batten for 2005 amounted to £88,923.

21. related party transactions

Homeowners Friendly Society and its subsidiaries (the Group) have a number of transactions between themselves all of which are undertaken in the normal course of business. As these Accounts cover the Society and the Group, no transactions or balances between Group entities, which eliminate on consolidation, require disclosure in accordance with the exemption given in FRS 8 'Related Party Disclosures'.

During 2005, no members of the Board of Directors of Homeowners Friendly Society Limited and its key management had material transactions with any of the Group's related parties.

22. deferred taxation

In accordance with FRS 19 the Group is required to disclose any deferred tax that has not been provided for in the balance sheet. The Group has an unprovided deferred tax asset of £8.0m (£7.8m in 2004) and the Society has £5.4m (£6.4m in 2004).

any questions

call free on 0800 028 8357*

* Freephone applies to UK calls only. Calls may be recorded for security and training purposes.

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