# Annual Report & Financial Statements 2005

F&C Asset Management plc

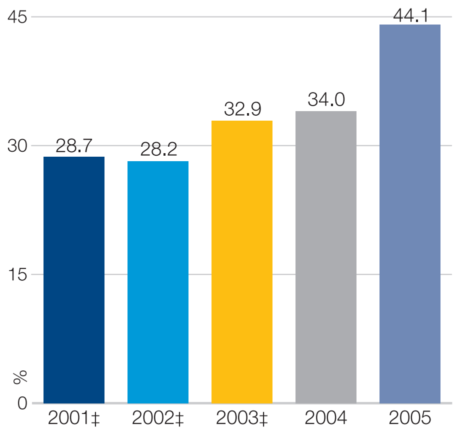
F&C Investments

# Contents

# Financial and Business Highlights

for the year ended 31 December 2005

**Operating margin***




| | 31 December 2005 | 31 December 2004** (Restated) |
|---|---|---|
| Net revenue (before policyholder income) | £267.2m | £151.9m |
| (Loss) before tax | £(106.3)m | £(4.4)m |
| Underlying profit before taxation* | £107.8m | £41.0m |
| Group operating profit* | £117.7m | £51.7m |
| Operating margin* | 44.1% | 34.0% |
| Basic loss per ordinary share | (16.4)p | (1.6)p |
| Underlying earnings per ordinary share* | 15.9p | 12.8p |
| Interim dividend | 4.0p | 4.0p |
| Proposed final dividend | 7.0p | 7.0p |
| Total dividends per ordinary share | 11.0p | 11.0p |
| Assets under management | £131.0bn | £124.8bn |

* before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan

** as restated for the implementation of IFRS

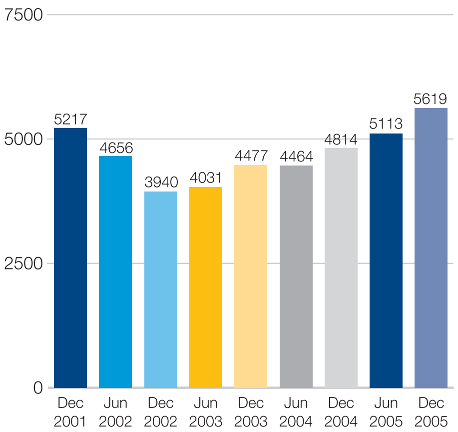
‡ prepared under UK GAAP

**Assets under management by client category**

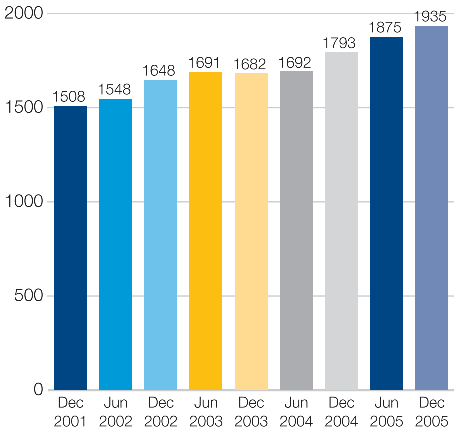
| | 31 Dec 2004 £ billion* | 31 Dec 2004 € billion* | 30 Jun 2005 £ billion* | 30 Jun 2005 € billion* | 31 Dec 2005 £ billion | 31 Dec 2005 € billion |
|---|---|---|---|---|---|---|
| Insurance Funds | 77.4 | 109.2 | 79.6 | 118.0 | 79.2 | 115.2 |
| Institutional Funds | 32.4 | 45.8 | 32.7 | 48.5 | 34.6 | 50.4 |
| Investment Trusts | 5.3 | 7.5 | 6.3 | 9.3 | 6.9 | 10.0 |
| Open Ended Products – Third Party | 2.5 | 3.5 | 2.5 | 3.7 | 2.7 | 3.9 |
| SICAV's | 0.5 | 0.7 | 0.4 | 0.6 | 0.5 | 0.8 |
| Sub-Advisory | 6.2 | 8.8 | 6.1 | 9.0 | 7.1 | 10.4 |
| Total Retail | 14.5 | 20.5 | 15.3 | 22.6 | 17.2 | 25.1 |
| **Total** | 124.3 | 175.5 | 127.6 | 189.1 | 131.0 | 190.7 |
| Private Equity realised 30 June 2005 | 0.5 | 0.7 | 0.5 | 0.7 | – | – |
| | 124.8 | 176.2 | 128.1 | 189.8 | 131.0 | 190.7 |

* restated for reclassification of Private Equity and certain retail funds

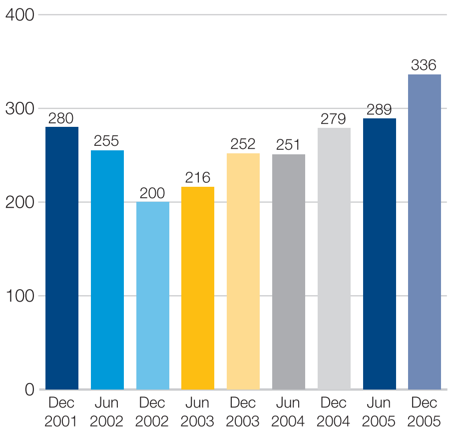
**UK Equity Market Performance**
**FTSE 100 Index**



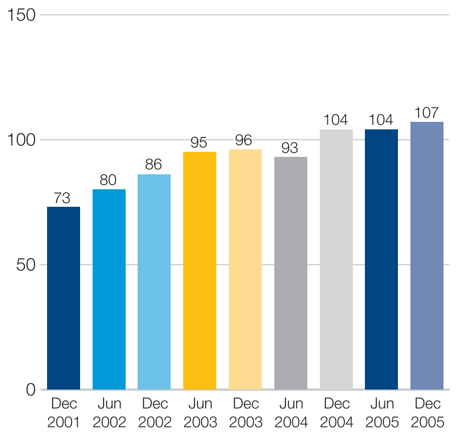

**UK Government Bond Market Performance**
**FTA Brit. Govt. Fixed All Stocks Total Return**



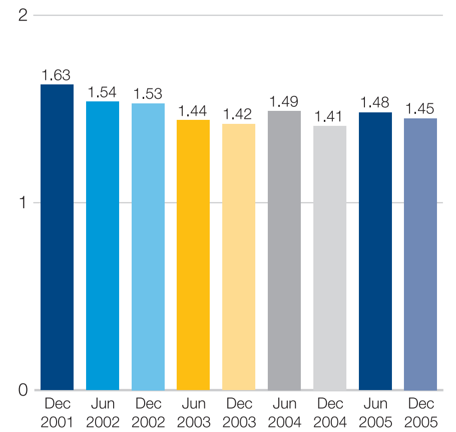

**Continental European Equity Market Performance**
**FTSE World Europe (ex UK) Index (expressed in £stg)**




**Continental European Government Bond Market Performance**
**Lehman Euro Treasury – Total Return (expressed in £stg)**




**Exchange Rate**
**Euro € to £stg**



# Key Highlights of 2005

"Whilst 2004 was dominated by the merger, 2005 was focused on integrating the two companies... we have successfully completed a large and complex integration in just 15 months, possibly a record for the asset management industry..."

- Underlying earnings per share, before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-investment Plan, increased by 24.6% to 15.9p.
- Final dividend of 7.0p giving an unchanged total of 11.0p for the year.
- Operating Margin before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-investment Plan increased from 34.0% to 44.1%.
- Assets under management at 31 December 2005 were £131.0 billion.
- Integration of the merged businesses now substantially complete.
- Synergies of £33 million have been delivered by 1 January 2006.

**"Asset management is a service industry. Our business philosophy is therefore simple; we seek to excel in everything that our clients expect from us."**

# Definitions

| | |
|---|---|
| **"merger"** | The combination of ISIS Asset Management plc and F&C Group (Holdings) Limited which completed on 11 October 2004 |
| **"F&C, FCAM, Group or Company"** | F&C Asset Management plc and its subsidiaries |
| **"F&CGH"** | F&C Group (Holdings) Limited and its subsidiaries |
| **"ISIS"** | ISIS Asset Management plc, which changed its name on 11 October 2004 to F&C Asset Management plc |
| **"FP"** | Friends Provident plc, the Company's ultimate parent undertaking |
| **"Eureko"** | Eureko B.V., a company incorporated in the Netherlands, the owner of F&C Group (Holdings) Limited prior to the merger |
| **"Achmea"** | Achmea Holdings N.V., a Company incorporated in the Netherlands and a subsidiary of Eureko |
| **"BCP"** | Banco Commercial Português S.A., a company incorporated in Portugal and a minority shareholder in Eureko |
| **"Pro forma"** | Financial disclosure of the financial results of F&CGH and ISIS on the basis that they had merged on 1 January 2004 |

# Chairman's Statement

## Company Overview

The year 2004 was dominated by the negotiation and conclusion of the merger between ISIS Asset Management plc and F&C Group (Holdings) Limited. 2005 naturally centred on the integration of the two firms to form one. In this, we were successful. The result is a more diversified, balanced, efficient, and profitable platform. In his comments which follow, our new Chief Executive, Alain Grisay, gives a detailed recap of the year just passed together with management's priorities for the future. Allow me to highlight here two key developments and one, overriding priority for our Company.

The single largest success in 2005 was the completion of the integration effort. This will reduce annualised costs by some £33 million. The single largest setback was the announced loss of Resolution Life assets. This will reduce annualised revenues by some £27 million. The positive impact of cost synergies has been partially registered in 2005. The negative impact of asset shifts by Resolution Life will bite predominantly in 2006.

Management's principal focus during the second half of the year was the strengthening of the quality and execution of our product offering. This remains a priority. Much action has been taken. There are encouraging signs. We will look for validation of these efforts in the form of positive flows and top line growth. Improved returns for our clients must underpin improved returns for our shareholders.

## Results and Dividend

The Group is reporting a loss per share of 16.4 pence. This reflects a number of non-cash and non-recurring items including amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan. The Board believes a more appropriate measure to be underlying earnings per share which rose to 15.9 pence, an increase of 24.6 per cent on the comparative number for 2004.

In line with our stated dividend policy the Board is recommending an unchanged final dividend of 7.0 pence per ordinary share payable on 19 May 2006 to shareholders on the register on 7 April 2006.

## Board Developments

During 2005, the Board re-visited and re-affirmed the Group's pan-European proposition as articulated to investors at the time of the 2004 merger. The Board's principal focus however, was very much on the key first step in that strategy – the successful execution of the merger itself. I would like to thank the Directors for the dedication shown and results achieved.

In September, we announced the prospective retirement of Howard Carter and appointment of Alain Grisay to succeed him as Chief Executive. The transition has gone smoothly. Alain took up his formal responsibilities on the 1 January 2006, and Howard will, as planned, step down from the Board at the upcoming Annual General Meeting. We would like to thank Howard for his many years of service. Without his efforts, the Company would certainly not be in its strengthened position today. We sincerely wish him the very best in the years ahead.

Meanwhile, this January, it was announced that our Chief Financial Officer, Ian Paterson Brown, would be standing down by mutual agreement. Ian has been with the Company in its various incarnations for no less than 24 years. He has played a key role in the Company's expansion. He was of course central to the merger in 2004 and a key contributor to the identification and realisation of the cost synergies that flowed from the subsequent integration. Ian will retire from the Board at the Annual General Meeting. We thank him for his tireless efforts and wish him all the very best.

## Industry Developments

In last year's communiqué, I highlighted a trend toward industry consolidation. That trend accelerated in 2005, and promises to continue in the years ahead. The search for critical mass, economies of scale, acceptance of open architecture (which facilitates separation of production and distribution), and finally the re-examination by owners of what is core and what is not, are factors contributing to sector activity. Two recent transactions are worth noting. Both Citigroup and Merrill Lynch have exchanged their very considerable asset management businesses for shares in a more focused, stand alone asset management competitor. The view seems to be that a dedicated asset management company is a more successful model. This is of course, our model.

## Summary and Conclusion

If 2004 was the year of the transaction, 2005 was the year of integration, the result of which is a better balanced Company. Notwithstanding the immediate earnings challenges, we believe the Company to be well positioned to take advantage of the expanding opportunities for asset management in the pan-European marketplace.

On behalf of the Board, allow me to thank our employees and clients whose dedication and support have made these strides possible.

Robert Jenkins
*Chairman*
20 March 2006

# Chief Executive's Report

This is the first Annual Report covering a full year of trading by the enlarged Company formed by the merger of F&C Group (Holdings) Limited and ISIS Asset Management plc in October 2004. It is also my first report as Chief Executive, having succeeded Howard Carter on 1 January. As a result of the merger and subsequent integration, F&C is now one of the largest asset managers in Europe with £131 billion (at 31 December 2005) of assets under management, an achievement of which my predecessor can rightly be proud.

Whilst 2004 was dominated by the transaction, 2005 was focused on integrating the two companies. I am pleased to report that:

- We have successfully completed a large and complex integration in just 15 months, possibly a record for the asset management industry.
- We have achieved £33 million of annualised cost synergies, the full benefits of which will be seen in the 2006 numbers.
- The above synergies have been achieved through the removal of duplication in functions, the consolidation of premises, product rationalisation and the adoption of a single brand.
- The only outstanding integration activity relates to certain IT projects which will run for another 18 months.

During 2005 we were advised by Resolution Life of its decision to internalise the management of its assets following its own merger with the Britannic Group. Whilst the loss of some £20 billion in assets in Q1 2006 was of course unfortunate, it was by no means related to F&C's performance or service levels.

While the integration is now firmly behind us and we have moved to a business as usual environment there remain a number of business risks which I highlight later in my report. To ensure strategic focus, provide greater accountability and enhance our control environment we have implemented a number of changes to our management governance structure.

We have streamlined our decision making process by setting up an Executive Committee and a Management Committee in lieu of some six existing management levels. We have also replaced the function of Chief Investment Officer by that of a Head of Investments to recognise the business management approach required by a larger operation.

Asset Management being a service industry, we have articulated our business philosophy as seeking to excel in everything our clients expect. To this end we have launched an initiative, "Performance First", across the business which:

- Defines top quartile performance standards for every area of activity: investment management, marketing and client servicing, operations and all the support functions;
- Sets clear and measurable departmental and individual goals; and
- Incentivises individuals to achieve their goals. This will be achieved through proposed amendments to the Company's Long Term Remuneration Plans, details of which are contained on pages 27 to 29.

These initiatives, combined with a strengthening of some of our human capital, reinforce a common business culture across the group and give us a focused platform for growth.

## Business Overview & Strategy

The key characteristics of F&C's business are:

- **We are a pure asset manager:** Our only activity is asset management.
- **We are focused on the UK and Continental Europe:** Headquartered in London, F&C has offices in seven countries (UK, Netherlands, Portugal, Ireland, Germany, France and the US) and is focused on growth in Europe.

# Chief Executive's Report

- **We are an active manager and an active investor:** Our investment process utilises proprietary research to add value for our clients. Our investment style is both active and pragmatic; we are not bound by labels such as ''value'' or ''growth''.

  As shareholder representatives we also actively engage with the companies in which we invest with the goal of enhancing and protecting long term shareholder value.

- **We are a diversified business** by client type, asset mix and geography (see tables opposite) which provides us with a robust business model across market cycles.

- **Our distribution model is based on intermediaries and strategic partnerships.**

  - In the UK institutional market we sell principally through investment consultants, who now advise the overwhelming majority of pension funds on the selection of investment managers.

  - In the UK retail market we distribute primarily through financial advisers. Our approach is to develop long-term relationships based on providing business solutions.

  - Across Europe we have developed wholesale and sub-advisory relationships with local partners where we benefit from long-term contracts and leverage local presence. These include Friends Provident (UK), Eureko (The Netherlands), Millennium BCP (Portugal), Friends First (Ireland) MAAF Assurances and Imperio (France).

  **We are a ''multi-boutique'' Company which leverages on scale:** We benefit from our scale in terms of research, infrastructure, distribution and access to the market. In terms of our investment model though we are a ''multi-boutique''. Our investment professionals work in small teams on specific products to foster an entrepreneurial culture of ownership and accountability for performance. These teams include property, fund of private equity funds, single strategy hedge funds and fund of hedge funds. Alongside the mainstream asset classes we are a multi-specialist with significant strength in niche areas such as Governance and Socially Responsible Investment (GSRI), Emerging Market Debt, Liability Driven Investment (LDI), Global Tactical Asset Allocation (GTAA) and Multimanager Fund of Funds.

### Our Strategy

Our strategy is grounded in our belief in a virtuous circle: delivering excellent performance will be validated by organic growth which will, in turn, translate into earnings growth and stock price performance. Going forward, our three strategic priorities are therefore:

### 1. A focus on investment performance

Our performance is already strong in a number of areas. Where there is room for improvement we have taken, and will continue to take, action:

- We have reorganised the investment management division, replacing the traditional Chief Investment Officer function as custodian of the House Market View with the new role of Head of Investments; a role which focuses on the broader approach to business management required to deliver consistent performance. This gives us a wider based front office senior leadership team where the heads of each asset class now have a more focused responsibility and accountability for investment decisions. We believe this is an appropriate model for an investment division with over 180 professionals.

- Where appropriate, we have and will continue to upgrade selectively the quality of our investment teams. Last October we recruited a team of highly regarded UK equity fund managers. We have already attracted institutional and retail assets on the back of this move.

### 2. Organic growth

Our priority is to grow organically. We will take an opportunistic attitude towards further acquisitions. We will consider transactions that would enable us to either leverage our platform or to secure new distribution channels.

### 3. We are targeting new business in higher margin areas

Following the successful integration of F&C with ISIS, we have one of the most efficient platforms in the asset management industry with an operating margin of 44.1% in 2005. While we recognise that maintaining this operating margin will be a challenge, our aim is to leverage this platform and improve our business mix by targeting new business in higher margin areas:

- We continue to strengthen F&C's retail brand through advertising and by deepening our relationships with financial advisers, our primary distribution channel for retail products in the UK.
- Our network of offices and presence in local markets mean we are well placed to increase funds under management from the more profitable continental European markets.
- We are investing in developing our higher margin products including Liability Driven Investment ('LDI'), alternatives and specialist institutional mandates yielding performance fees such as emerging market debt, high yield, high alpha equities, hedge funds, and Private Equity Fund of Funds. We have been successful in attracting some outstanding managers to lead these efforts.
- Our "multi-boutique" approach allows us to offer a broad range of products to our clients, and positions us to maximise our share of their assets under management in response to shifts in their portfolios.

### Assets Under Management

The table below provides a breakdown of assets under management at 31 December 2005 by client category, asset class and geographic source.

### Assets Under Management by Client Category

| | 31 December 2005 £bn | (%) | 31 December* 2004 £bn |
|---|---|---|---|
| Insurance Funds | 79.2 | 60.5 | 77.4 |
| Institutional Funds | 34.6 | 26.4 | 32.4 |
| Investment Trusts | 6.9 | 5.2 | 5.3 |
| Open Ended Products (Third Party) | 2.7 | 2.1 | 2.5 |
| SICAV's | 0.5 | 0.4 | 0.5 |
| Sub-Advisory | 7.1 | 5.4 | 6.2 |
| Total Retail | 17.2 | 13.1 | 14.5 |
| Venture Capital Trusts/Limited Partnerships | – | – | 0.5 |
| Total | 131.0 | 100.0 | 124.8 |

* as reclassified to be consistent with 2005.

Insurance clients represent 60 per cent. of our assets under management but this is spread across a number of clients with whom we have long term contracts. These include Friends Provident, Eureko, Achmea, RSA, Friends First and Millennium BCP. The level of insurance client assets has reduced during the first quarter of 2006 to about 53 per cent. of total assets under management following Resolution's final transfer of assets to its in-house asset management operation.

### Assets Under Management by Asset Class

| | 31 December 2005 £bn | (%) | 31 December 2004 £bn |
|---|---|---|---|
| Fixed Interest | 72.8 | 55.6 | 72.6 |
| UK Equities | 19.4 | 14.8 | 16.8 |
| Overseas Equities | 25.8 | 19.7 | 23.1 |
| Property | 6.5 | 5.0 | 6.0 |
| Other Alternative Investments | 1.2 | 0.9 | 0.9 |
| Liquidity | 5.3 | 4.0 | 4.9 |
| Private Equity | – | – | 0.5 |
| Total | 131.0 | 100.0 | 124.8 |

Fixed interest assets represent some 56 per cent. of our total assets under management. Within this asset class F&C has developed a strong track record managing a large book of corporate credit for both institutional and retail clients. We have also developed expertise in specialist higher margin products, particularly in emerging market debt and high yield bonds.

# Chief Executive's Report

Whilst alternative investments represent a relatively small portion of our overall assets under management, the fee rates are higher than average. This is an area we have been growing rapidly.

### Assets Under Management by Geographic Source

| | 31 December 2005 £bn | (%) | 31 December 2004 £bn |
|---|---|---|---|
| United Kingdom | 77.7 | 59.3 | 74.8 |
| The Netherlands | 32.1 | 24.5 | 30.4 |
| Portugal | 13.5 | 10.3 | 12.7 |
| Ireland | 2.9 | 2.2 | 2.8 |
| Germany | 1.9 | 1.5 | 1.7 |
| France | 1.2 | 0.9 | 0.7 |
| Other | 1.7 | 1.3 | 1.7 |
| Total | 131.0 | 100.0 | 124.8 |

## Review of 2005 & Prospects

### Investment Performance

Performance was mixed over the year with major areas of strength but also some weakness. Some 54 per cent. of our retail funds delivered above average performance in their respective IMA sectors* during 2005, compared to 60 per cent over the last three years and just 38 per cent over five years.

Credit was an area of particular strength with the F&C Long Dated Corporate Bond Fund finishing the year ranked first out of fifty-two funds and the F&C Corporate Bond Fund ranked second out of seventy-two funds in their respective sectors over three years, according to the CAPS pooled pension fund survey[1].

We also outperformed over the year in high yield, emerging debt, Continental European equities, US smaller companies, UK smaller companies, Japan and Asia ex-Japan. Balanced portfolios benefited from positive asset allocation decisions.

Our ethical funds were relatively disadvantaged against the wider market in 2005 by their natural under-weight exposure to oils and financials, but they continued to deliver good absolute returns and were performance leaders against competitor ethical products.

We underperformed in emerging equities, UK equities and Euro government bonds.

### Operations

As outlined in our last Annual Report, our intention had been to outsource to Mellon certain operational functions related to the former ISIS business. This would have involved the transfer of some of our staff. After a year of due diligence and contractual negotiations we took the decision in November to terminate our discussions with Mellon, as we were not satisfied that to proceed would have been in the best interests of all our stakeholders.

Our existing platform for client administration of the former ISIS book of business is efficient and there has been no disruption to clients as a result of our decision to disengage from this project. We have considerable experience in using a multi-provider approach as we currently use some five providers for outsourcing services . We are now enhancing our flexibility by building a data warehouse to consolidate data from various providers.

A separate client and fund administration outsourcing project with ABN AMRO Mellon Global Services in The Netherlands did proceed successfully in December. This resulted in 22 of F&C Netherlands staff transferring to ABN AMRO Mellon's Amsterdam office. F&C Netherlands is now able to focus entirely on client servicing and asset management.

### Fund flows for the year to 31 December 2005

| Client Category | Inflows £m | Outflows £m | Net £m |
|---|---|---|---|
| Insurance Funds | N/A | N/A | (6,577) |
| Institutional Funds | 4,523 | (5,482) | (959) |
| Open Ended Products (Third Party) | 367 | (211) | 156 |
| Investment Trusts | 1,144 | (690) | 454 |
| SICAV's | 517 | (530) | (13) |
| Sub Advisory | 2,511 | (1,711) | 800 |
| | N/A | N/A | (6,139) |

As the table above illustrates, during 2005 we experienced net outflows of £6.1 billion of assets under management. Some £5.2 billion of these related to one insurance client, Resolution plc. Additional net outflows were experienced from institutional clients. In contrast there were net inflows from higher margin retail client categories such as sub-advisory relationships, open-ended funds and investment trusts. Further commentary is provided below.

*Excludes funds with target returns.
1 Russell Mellon CAPS Pooled Pension Fund Update to 31 December 2005. The F&C MPF Corporate Bond Fund sits in the UK Bonds – Standard Sector. The F&C MPF Long Dated Corporate Bond Fund sits in the UK Bonds – Long Term sector. Calculation basis: offer to offer, income reinvested at offer, net of fees.

## Insurance

The successful integration of the two previous businesses was over-shadowed by the termination of our contract to manage assets for Resolution plc, the major negative event for us during 2005. This was particularly disappointing as it was not related to investment performance or any other reasons within our control.

- During 2005 outflows from Resolution plc represented £5.2 billion, a significant proportion of the total £6.6 billion net outflows from insurance clients.
- The remaining £19.9 billion of Resolution plc assets will be withdrawn during Q1 2006.
- F&C will receive £27 million in compensation for the termination of this contract.
- Going forward, F&C has little exposure to closed life books and natural run-offs will be small.

We see further opportunities in the insurance sector given F&C's expertise in this area. In particular;

- We have developed a dedicated Asset and Liability Management (ALM) capability to provide solutions to meet the specific needs of insurance clients.
- With some of our insurance clients, F&C has a contractual right to manage additional assets acquired through corporate activity. For example, following the merger of Achmea and Levob in 2005, assets were transferred to F&C. Similarly, the merger between Achmea and Interpolis in 2005 will create new opportunities for F&C.
- Insurance clients are increasingly interested in allocating some assets to alternatives such as hedge funds and private equity, where we have developed expertise and where margins are higher than traditional asset classes.

## Institutional

During 2005, despite inflows of some £4.5 billion we experienced net outflows of about £1 billion. Asset losses were related broadly to three factors:

- An industry trend away from balanced to specialist management. This was a factor primarily impacting our business in The Netherlands;
- A switch by some clients away from equities and bonds to other asset classes; and
- Some instances of disappointing investment performance, particularly in emerging equities.

In the UK the main contributor to new business has come through the Friends Provident Defined Contribution and investment products (£1.2 billion of new assets). In general, sales activity has been focused on the investment consultants, with over 150 research meetings taking place during the year. Whilst the majority have been with the largest consulting firms (Watsons, Mercers, Hewitts, Hymans Robertson and Psolve,) we have extended our coverage to encompass over 50 other firms nationwide. We have concentrated on presenting for new business those areas of investment expertise where we believe we have competitive advantage including composite UK bonds, high alpha UK equities, UK property and other more specialist areas such as fund of private equity funds, fund of hedge funds and ALM. In addition, the F&C Managed Pension Fund continues to provide smaller schemes with the opportunity to invest in a diversified manner across a choice of 25 specialist investment vehicles.

In The Netherlands we have seen opportunities created by policy and regulatory developments in two areas where we have strong specialist expertise:

- There is growing interest in Governance & Socially Responsible Investment where we operate our market leading *reo*® (responsible engagement overlay) service. Achmea has recently applied *reo*® to €1.5 billion of its assets under management.
- The second area is ALM and LDI.

The adoption of market consistent valuations for both the assets and liabilities of pension funds has highlighted the valuations' sensitivity to interest rate movements where pension funds are invested in more asset classes than just bonds. This mismatch causes the so called "duration gap" where the value of assets can change at a different pace to the value of liabilities. In order to benefit from the long term value creation of different asset classes pension funds need to actively manage their risks.

# Chief Executive's **Report**

In The Netherlands, from January 2007, Dutch pension funds will be subject to the new Financieel Toetsingskader (nFTK) regulation which will require them to structure their investments to lock in their ability to cover their liabilities.

F&C, as a leading manager of insurance portfolios, has a strong technical expertise in liability modelling and LDI. To provide a solution to our pension fund clients and leveraging on our experience, we have recently launched a series of LDI pooled funds which have already attracted over €500 million of Dutch client assets. These structures allow clients to commit only part of their assets to cover the risk of interest rates movements on their liabilities whilst retaining the flexibility to seek higher returns on their remaining assets.

In Portugal we continue to manage institutional assets for Millennium BCP-Fortis and have been working with them on their new asset allocation strategy. One disappointment was an outflow of around £1.4 billion as a result of Caixa's decision to manage in-house the assets of Império Bonança. F&C will be compensated for this loss under its long-term arrangement with BCP.

In Ireland attention has been directed on property where our performance has been very strong. We have also been focusing on widening the marketing of our Governance and Socially Responsible Investment (GSRI) capabilities ahead of the launch of a Charities Managed Fund in 2006.

In Germany during 2005, institutional investors have continued to redefine the value chain between investment managers, custodians and Master KAGs and the growing market share of the Master KAGs underlines this trend. In this context, F&C has built on its reputation as a specialist provider of investment solutions in the areas of bonds, convertibles and, more recently, single strategy hedge funds.

In France we continued to develop our relationship with MAAF Assurance. Sales and marketing activity has centred around a planned second tranche of FOSCA (a closed-ended property investment vehicle focused on the French office market). The first tranche was launched with their property subsidiary, MAAF REIM, in 2004. Our relationship with Imperio Assurances continues to be robust and assets have grown significantly.

### UK Retail

Industry sales in 2005 started slowly, but picked up from May on the back of strong growth in equity markets. All major equity markets posted positive returns during 2005 with the FTSE All Share Index generating a 22 per cent. total return.

Statistics from the Investment Management Association (IMA) indicate that, whilst net retail sales in 2005 were some 73 per cent. higher than 2004, this improvement was not reflected in sales of Individual Savings Accounts (ISAs). Net ISA sales actually ended 2005 some 10 per cent. lower than 2004 and were at their lowest level since 1999. As Howard Carter indicated in his Report last year, we are concerned that ISA sales have been impacted by the decision of the Government to abolish tax credits on ISA dividends. This is a factor which the Government should consider when it conducts its review of the future of ISAs later this year.

Industry wide, equity funds represented 39 per cent. of net retail sales compared to 32 per cent. from bond funds. Investors showed a strong preference for equity income funds and other yield based investments. Demand for property based investments remained high.

Our own net retail sales were up 21 per cent. in 2005. We are pleased with this progress so soon after a major merger. In particular:

- We completed a fund rationalisation programme during the first half of the year and consolidated the fund accounting, trustee and third-party administration.
- The two legacy ranges of investment trust wrapper products such as Peps, ISAs and regular savings schemes were migrated into one product suite by December 2005.
- The Company consistently advertised throughout the year to build the F&C brand in the IFA market place.

Key product highlights during 2005 were:

- The Stewardship Income Fund, an ethical equity income fund, was our best-selling OEIC which received widespread recognition and media attention for its excellent long term performance compared to other equity income funds;
- In July we sought to capitalise further on the success of the Stewardship Income management team by appointing them to run the F&C UK Growth & Income Fund, a previously poorly performing product. The fund has now moved into the top quartile of the IMA Equity Income Sector and has more than doubled in size on the back of new inflows and strong performance;
- Our multi-manager range of funds accounted for 25 per cent. of our UK retail fund sales. This is a fast growing area, receiving support from intermediaries seeking to outsource client portfolio management to professional fund of funds teams. In particular, we saw the greatest level of support for the F&C Multi-Manager Distribution Fund which has grown to over £150 million in just two years;
- Corporate bond funds represented 17 per cent. of our retail sales, a slowdown on 2004 as advisers turned their attention towards equity funds. Performance has remained strong throughout the year and the lead manager on these funds now carries a coveted AAA-rating from Citywire, the highest possible rating; and
- The Venture Capital Trust (VCT) market saw significant growth in 2005 on the back of favourable tax changes introduced in the 2004 Budget. Currently subscriptions to VCT new issues attract 40 per cent. income tax relief. F&C is the largest distributor of VCT products, marketing trusts managed by ISIS EP LLP (under the Baronsmead brand). F&C saw an increase in gross VCT sales of 40 per cent. in 2005.

It was an eventful year for the investment trust industry with arbitrageurs active in the market and plenty of corporate activity. As a market leader in the investment trust sector we were not immune from these trends. Developments involving investment trust clients included:

- The launch of the F&C Commercial Property Trust Limited in March. With gross assets of £965 million invested in high quality UK commercial property, principally sourced from Friends Provident, this is the largest listed commercial property trust to date. Over £250 million of new funds were raised as part of this initiative;
- The hiring of a private equity fund of funds team from Martin Currie Investment Management. The deal was accompanied by the mandate for the Martin Currie Capital Return Trust plc which has now been renamed F&C Private Equity Trust plc. The team have expanded our investment capabilities and improved our ability to grow our exposure to alternative assets in a scaleable way;
- The merger of the F&C Income Growth Investment Trust plc with F&C Capital and Income Investment Trust plc;
- The outsourcing of certain US and Japanese assets by Foreign & Colonial Investment Trust plc;
- A reconstruction and tender offer by F&C Global Smaller Companies plc;
- The introduction of discount control mechanisms by Foreign & Colonial Investment Trust plc, European Assets Trust N.V. and F&C Global Smaller Companies plc; and
- The loss of the mandate to manage F&C Pacific Investment Trust plc and the recent announcement by Latin American Investment Trust plc that it intends to withdraw its funds.

# Chief Executive's Report

F&C has long been recognised as a market leader in the provision of investment trust savings wrappers and an important development during the year was the launch of the F&C Child Trust Fund. This provides access to a range of F&C managed investment trusts through the Government's recently introduced savings scheme for new born children.

The group's leading position as an investment trust product provider has once again been validated in the market place with numerous awards including "Investment Trust Company of the Year" (Financial Adviser); "Best Investment Trust Provider" (Shares Magazine); "Best Investment Trust ISA Provider" (Personal Finance); "Best Investment Trust Group" (Professional Adviser).

A further positive achievement for our retail business was winning the Financial Adviser Five Star Service Award. This was particularly pleasing as F&C was the only asset manager to win this award which is based on voting by financial advisers.

### European Wholesale

Our strategy for accessing the retail market outside of the UK is primarily, although not exclusively, as a wholesaler working with local distributors. This channel was one of the most successful for F&C during 2005. The three key retail markets for F&C in Continental Europe are Portugal (where we provide sub-advisory services to Millennium BCP Funds de Investimento (MFI), the mutual funds of Millennium BCP), The Netherlands (where we sub-advise mutual funds for Achmea, the largest Dutch insurance group) and Germany (where we market SICAV funds). Retail assets under management arising from these relationships were €10.7 billion at year end, a rise of 27 per cent. across the year and ahead of our forecasts.

A summary of key developments in these markets includes the following:

- In Portugal we saw net sales of €829 million. Our partner Millennium-BCP has retained its position as the number one provider of mutual funds in Portugal with a 21 per cent. market share. We are continuing to work with MFI to review and enhance their product range;
- In The Netherlands net sales were €475 million which included the transfer of €218 million assets resulting from Achmea's merger with Levob; and
- In Germany net sales were €115 million with the focus being F&C HVB-Stiftungfonds, a low risk product co-branded with HypoVereinsbank and managed by F&C Alternatives which is designed to provide predictable returns, as well as three SICAV funds: F&C European High Yield, F&C Emerging Market Bond and F&C US Smaller Companies. Working with our institutional business we have negotiated an exclusive share class on the F&C Emerging Market Bond Fund for Commerzbank. We have increased our visibility in the German market place through seminars, roadshows and conferences.

### F&C Alternative Investments

Interest in alternative assets continues to grow across our client bank.

The F&C Alternative Investments team currently manages three single strategy hedge funds; F&C Amethyst (an equity volatility trading fund), F&C Sapphire (a quantitative asset allocation fund) and F&C Citrine (a European equity long/short fund).

In addition to these three funds, the team also manage a number of retail funds which leverage our derivatives expertise, including F&C Higher Income Plan, F&C BLUE and F&C HVB-Stiftungsfonds, all of them with an absolute return bias.

Despite the challenging environment for the hedge fund industry in 2005, it was a successful year for F&C Alternative Investments:

- Assets under management increased 33 per cent. to £1.2 billion;
- F&C Amethyst won the prestigious EuroHedge Award as the best Mixed Arbitrage & Multi-Strategy fund;
- F&C Amethyst closed for new business having successfully raised €470 million; and
- F&C Citrine launched its first major fund raising in September 2005.

### F&C Partners LLP

F&C Partners is a fund of hedge funds boutique, founded in late 2004, which is majority owned and controlled by F&C. The team manages two products; a Balanced Alpha Fund and a Select Alpha Fund. Both portfolios delivered positive absolute returns and assets under management at year end were £295 million.

### ISIS Equity Partners LLP

As previously reported during the summer, assets managed by F&C's private equity subsidiary, ISIS Equity Partners, were transferred to a new Limited Liability Partnership (ISIS EP LLP) in which F&C has a small minority interest. As such, these assets are no longer included in F&C's quarterly reporting of AUM. However, we continue to enjoy a profit share as an investor in ISIS EP LLP.

Two C-share issues on Venture Capital Trusts managed by ISIS EP LLP and marketed by F&C were fully subscribed during the year, securing ISIS EP LLP with the largest market shares of new VCT fund raising.

### Business Risks

In addition to the ''normal risks'' facing the business relating to market, clients, personnel and regulation, the Company faces a number of short-term operational challenges. These operational challenges, principally created by the loss of the Resolution Life contracts and the decision to withdraw from the UK outsourcing negotiations with Mellon, are being managed and prioritised through the Company's risk management activities. We have also taken action to address investment performance but the loss of key mandates as a result of historic investment underperformance remains a business risk and a key area of management focus as we seek to embed ''Performance First'' across the business.

### Financial Review

2005 was not only the year of integration and cost synergies, it also saw listed companies adopt International Financial Reporting Standards (''IFRS'') for the first time. Recognising that the financial statements represent the first full twelve months of the enlarged group and the benefit of certain cost synergies, the numbers are not directly comparable with those for 2004.

## Results – Consolidated Income Statement

Under IFRS the results of our Managed Pension Fund business are consolidated on a line by line basis rather than being included as a single line item ''other operating income'', as previously reported under UK GAAP. The effect of this is to inflate revenues and operating costs attributable to policyholders' underlying assets.

The other major factors impacting the Income Statement are the Re-Investment Plan expense of £22.2 million which related to the share scheme established at the time of the merger to lock-in and incentivise senior staff. This was commented on in last year's Annual Report and Accounts and further information is included within the Remuneration Report.

Historically we have been required to amortise goodwill. However, with the introduction of IFRS it is necessary to separately recognise the value of intangible assets and to amortise those assets over their estimated useful lives. These intangible assets represent the value of underlying management contracts acquired.

### Intangible Assets – Management Contracts

| | Carrying Value at 1 January 2005 £m | Additions in Year £m | Impairment in Year £m | Amortisation in Year £m | Foreign Exchange Movements in Year £m | Carrying Value at 31 December 2005 £m | Amortisation Period Years |
|---|---|---|---|---|---|---|---|
| **F&C Acquisition** | | | | | | | |
| Investment Trusts | 118 | – | (56) | (6) | – | 56 | 20 |
| Insurance | 124 | – | – | (12) | (4) | 108 | 10 |
| Institutional | 182 | – | (55) | (18) | (3) | 106 | 10 |
| Retail/Other | 87 | – | – | (9) | (1) | 77 | 10 |
| | 511 | – | (111) | (45) | (8) | 347 | |
| **RSA Acquisition** | | | | | | | |
| Insurance | 38 | – | – | (5) | – | 33 | 10 |
| Retail/Other | 41 | – | – | (6) | – | 35 | 10 |
| | 79 | – | – | (11) | – | 68 | |
| Other | – | 1 | – | – | – | 1 | 20 |
| Total | 590 | 1 | (111) | (56) | (8) | 416 | |

The remaining carrying value of intangible assets needs to be reviewed if indicators of their potential impairment exist. If there has been an impairment then the intangible assets is written down to its recoverable value.

This is a topic I will return to under the review of the balance sheet but both amortisation and impairment of intangible assets are added back in calculating underlying earnings, one of the mechanisms the Board uses for measuring the progress of the business.

# Chief Executive's **Report**

### Results – Highlights

Previously, under UK GAAP, we have shown Earnings Per Share ("EPS") on a "clean" basis being EPS before restructuring costs, amortisation and the cost of the Re-Investment Plan. Under IFRS the Board continue to believe that it is appropriate to give some measure of the underlying earning of the business and hence while the basic loss per share was 16.4 pence for the year the underlying earnings per share was 15.9 pence (2004: 12.8 pence). Further comment is provided on underlying earnings below.

### Net Revenues

Net revenues for the year, excluding investment income attributable to policyholders were £267 million (2004: £152 million).

Investment management fees in the year were £277.4 million. While new business of £9.1 billion was added during the year and markets rose adding approximately £12.8 billion to our assets under management, we also incurred significant business outflows which, while impacting 2005, will have a more significant effect on 2006 revenues.

As previously discussed, the loss of Resolution assets through corporate activity was the major factor impacting our outflows. Resolution outflows in 2005 were approximately £5.2 billion and a further £19.9 billion has been withdrawn in Q1 2006. We have agreed a termination payment with Resolution in respect of this business of £27 million which will be received in April 2006. Some of the other institutional business losses, such as certain emerging equities mandates, were at a higher revenue margin than our average at 31 December 2004 (21 basis points). When taken together with the disposal of our private equity business, we expect our recurring revenue margin for 2006 to be 20 basis points. While this short term set-back is disappointing, our focus remains on generating net new business in higher margin areas.

While we lost some mandates due to investment performance it is pleasing to note that we also earned £13 million of performance fees during the period.

### Operating Expenses

Operating expenses excluding the Re-Investment Plan costs, amortisation and impairment of intangible assets, restructuring costs and net operating costs on investment and insurance contracts were £151 million (2004: £101 million) which represent the ongoing costs of running the business. Some 60 per cent. of these are staff related costs. Management of headcount is therefore a fundamental discipline.

### Headcount

| | 31 Dec 2005 Actual | 31 Dec 2004 Actual | 31 Dec 2003 Actual F&C | 31 Dec 2003 Actual ISIS | 31 Dec 2003 Total |
|---|---|---|---|---|---|
| United Kingdom | 616 | 700 | 311 | 521 | 832 |
| Overseas | 121 | 140 | 146 | – | 146 |
| Total | 737 | 840 | 457 | 521 | 978 |

(Figures for 2004 and 2005 do not include temporary staff or vacancies.)

Since the year-end we have further reduced our headcount, recognising that all areas of the integration, apart from some of the technology aspects, are now concluded. As previously highlighted, technology integration is always the last part to be completed but to gain the full operational synergies it is essential that this is concluded.

While we continue to pay attention to our operating margin, it is only one of the measures we use to assess our business efficiency and progress. As indicated earlier, organic growth measured by assets under management, net new business and revenue margin will be the real measures of our success going forward.

## Integration Expenditure and Synergies

The table below shows the integration expenditure incurred since the merger. It is pleasing to report that in all areas of our business, apart from certain IT systems, integration is essentially concluded. Based on our budget for 2006 the full benefit of synergies resulting from these restructuring costs are expected to be delivered ahead of our timetable and, as such, we should see a benefit slightly in excess of the forecast £33 million in the results for the year to 31 December 2006.

| | 2005 £000 | 2004 £000 | Total £000 |
|---|---|---|---|
| Redundancy and other related staff costs | 6,330 | 8,975 | 15,305 |
| Premises costs | 2,514 | 4,730 | 7,244 |
| Information Technology and related costs | 6,081 | 640 | 6,721 |
| Re-branding, retail administration and client servicing | 2,335 | 364 | 2,699 |
| Consultancy and other costs supporting the restructuring process | 5,145 | 1,635 | 6,780 |
| Property, plant and equipment write-downs | – | 1,988 | 1,988 |
| Restructuring costs | 22,405 | 18,332 | 40,737 |

## Long Term Remuneration Plans – Share Schemes

While we included the cost of share schemes in last year's accounts, the numbers are not directly comparable for two reasons:

Firstly, the basis used under IFRS for the share schemes including Re-Investment Plan and the matching shares, requires the fair value of the awards to be spread over the period until employees become entitled to the shares. As such, the table opposite shows the cost for 2005. Details of the mechanics of the plans are contained in the Remuneration Report.

Secondly, the Long Term Remuneration Plan was only introduced towards the end of 2004 and therefore the expense in 2004 only represents a portion of the year. Going forward it is our intention to make annual grants and it is anticipated that a grant of some 5 million shares will be made, after the Annual General Meeting in May 2006. The table below shows the number of outstanding share awards at 31 December 2005 and the cost in the year.

## Share Schemes

| | Outstanding share awards at 31 Dec 2005 (Number 000s) | Cost in respect of 2005 (£000) |
|---|---|---|
| **Re-Investment Plan:** | | |
| Investment Shares | 4,626 | 14,369 |
| Matching Shares | 9,534 | 7,793 |
| | | 22,162 |
| **Recurring Arrangements:** | | |
| Long Term Remuneration Plan | 5,954 | 3,466 |
| Other Share Schemes | 8,776 | 1,973 |
| | | 5,439 |

## Underlying Earnings

The Board believes that it is necessary to look at a number of factors to determine the progress of the business. Underlying earnings is one of those metrics and to assist clarity the table below shows how this is determined.

## Reconciliation of Earnings per Share

| | 31 Dec 2005 Basic pence |
|---|---|
| Loss per Ordinary Share | (16.4) |
| Amortisation of intangibles, net of tax | 8.3 |
| Cost of the Re-Investment Plan, net of tax | 3.8 |
| Restructuring costs, net of tax | |
| – Reorganisation post acquisition of F&CGH Group | 3.4 |
| – Operations outsourcing | 0.3 |
| Impairment of intangibles, net of tax | 16.5 |
| Earnings per ordinary share before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan* | 15.9 |

*Defined as 'underlying earnings per share'.

# Chief Executive's **Report**

### Dividend

We have in previous Annual Reports set out our dividend policy and it is appropriate to do so here.

Our dividend policy is:

- To maintain and, if appropriate, grow the dividend.
- To target over the medium term 1.5 times dividend cover based on "underlying earnings".
- To review dividend cover in light of future business and regulatory requirements and distributable reserves.

Given the business outflows during 2005 and the loss of the Resolution business in early 2006 it would be imprudent to increase the dividend at present, albeit it remains an objective. The Board has therefore declared an unchanged final dividend of 7.0 pence per ordinary share for the year which will be payable on 19 May 2006 to shareholders on the register on 7 April 2006. This dividend, when taken with the interim dividend of 4.0 pence per Ordinary Share, results in an unchanged total dividend of 11.0 pence per share for the year to 31 December 2005. Under IFRS the final dividend of 7.0 pence per Ordinary Share is not recognised in the financial statements until it is approved by shareholders and, as such, no liability for it is included within the 2005 financial statements.

### Foreign Currency

During the year we earned about 25 per cent. of our revenues in Euros. After recognising Euro costs, the net impact is that less than 16 per cent. of our "net revenues" are exposed to exchange rate fluctuations. The Board has decided that it will not seek to hedge our exposure to short-term fluctuations in currency and in particular the Euro/Sterling exchange rate. We will, however, seek to repatriate surplus overseas currency into Sterling. Surplus currency balances are defined as being that level of cash which exceeds our regulatory capital requirements in the respective countries plus the necessary working capital to finance short term expenditure requirements and other business initiatives.

As part of our debt refinancing exercise, outlined below, we will be exploring all of the options available, including the possibility to refinancing our Sterling borrowings with a Euro-based loan. If we proceed down this route it will provide a hedge for both our Euro denominated net revenues and that part of our intangible assets which fall to be treated as Euro denominated under IFRS. We are still at an early stage in the discussion process with our advisers and, as such, the above outlines only one option. We will keep shareholders updated, reporting further at the half-year.

### Regulatory Capital

F&C continues to operate under a waiver from the requirements of consolidated supervision. While we remain confident that the status quo will continue, we cannot foresee what future changes in regulation will bring, particularly as they are typically driven from Europe and are not directly under the FSA's control. We await the finalisation of the revised regulations on capital adequacy scheduled for later this year. We will continue to monitor developments and consider the options open to us, as addressed under the heading Debt Refinancing.

### Goodwill and Intangible Assets

| | Goodwill £m | Management Contracts £m | Other £m | Total £m |
|---|---|---|---|---|
| At 31 December 2004 | 577.9 | 589.8 | 0.5 | 1,168.2 |
| Amortisation for year | – | (55.8) | (0.4) | (56.2) |
| Impairment | – | (111.5) | – | (111.5) |
| Other | – | (6.4) | 1.5 | (4.9) |
| At 31 December 2005 | 577.9 | 416.1 | 1.6 | 995.6 |

Under IFRS, when an acquisition is made there is a requirement to recognise separately the fair value attributed to intangible assets, which in this case are management contracts. The excess of consideration over the fair value of net assets acquired represents the business value and infrastructure and is recognised as goodwill.

Management contracts acquired are separated by nature of client, e.g. insurance, investment trust, and are amortised over their expected useful lives. We are required to review the carrying value of these contracts where any indicator of potential impairment arises, e.g. higher than anticipated fund losses. Such mandate losses may have the effect of creating an impairment charge regardless of the level of new business that has been achieved. A good example of this is investment trusts where we have generated net new business during the year, but the loss of investment trust mandates purchased as part of the 2004 business combination at a rate higher than originally estimated means we need to recognise an impairment charge of some £56 million. The nature of investment management businesses is that mandates will always be won and lost, sometimes, as in the case of Resolution, for reasons outwith the business's control. While this depicts a short-term loss of business, it does not signal a long-term loss of business value – a factor that is driven by stock markets, net new business, revenue margin and other factors.

The level of fund losses during 2005 and anticipated losses in respect of both institutional and investment trust clients and resultant impact on future revenue was significant enough to be considered a potential indicator of impairment in respect of the related intangible assets. A full impairment review of these assets was therefore undertaken.

This review determined the recoverable amount of the intangible assets in respect of investment trust and institutional fund management contracts was lower than their carrying value and has therefore resulted in impairment charges of £56.1 million and £55.4 million respectively. These calculations have been based on different risk discount rates using the Group's weighted average cost of capital of 8.9 per cent. allowing for the nature of the contracts and the estimated life as shown above. The recoverable amount assumes an estimated loss rate of 5 per cent. and 14 per cent. per annum respectively.

We are required to conduct an annual impairment review of the carrying value of goodwill although there is no annual amortisation charge. Our review demonstrated that there was no impairment and hence no requirement to write down goodwill as at 31 December 2005.

### Cash Resources

While we have debt on our balance sheet and have incurred restructuring costs of £24.6 million, during the year, fund management businesses are cash generative, requiring minimal working capital other than that required to maintain compliance with regulatory capital requirements. With cash of £118 million on our balance sheet at 31 December 2005, current assets less current liabilities (excluding the £180 million of debt which we intend to refinance later this year) of £105.2 million and projected future profitability, we remain satisfied with our current position and will seek to continue to manage both cash resources and the balance sheet for the benefit of shareholders.

### Pension Fund Deficits

While we have seen a strong rise in equity markets over the last 12 months which has resulted in an increase in the pension funds assets this has more than been negated by the strengthening in the mortality assumption and the reduction in the discount rate, both of which have significantly increased the quantum of our defined benefit pension liabilities as at 31 December 2005. At the year-end the aggregate pension funds deficit had increased to £33.6 million, net of deferred tax.

The Board has established a committee of non-executive Directors to review our final salary pension funds and consider matters such as the level of the deficit and future funding strategies, the feasibility of combining the ISIS and F&C schemes and, the proposed PPF levy. These are also matters that the trustees of the pension schemes are considering.

### Debt Refinancing

As highlighted in last year's Annual Report the £180 million of debt drawn down from our parent company, Friends Provident, to acquire RSA's investment management business in 2002 falls to be repaid in November 2006.

# Chief Executive's Report

We are at an advanced stage of formally appointing advisers to assist us with refinancing our debt requirements. In addition to the £180 million, we have £34 million of subordinated debt and a £50 million facility of which £5 million is drawn. As part of our refinancing exercise we are considering rolling all of this together and consolidating our debt requirements through either a public or private placement. We are also addressing the rating agency considerations, regulatory capital considerations, accounting and tax issues and, as covered under foreign currency, the business needs going forward. While the loan does not require to be refinanced until the end of 2006 we believe it is important to move matters forward at this time to create flexibility and time for proper consideration of all these matters.

If we were to seek to issue some form of tier 1 or tier 2 capital this would have a positive impact on our regulatory capital position without necessarily materially changing the structure of our balance sheet. With the potential for future changes in the capital adequacy requirements this is an avenue that is currently being considered as it could materially strengthen our regulatory capital position.

**Conclusion**

The integration was successful and swiftly completed with no consequences to our client franchise directly related to the deal.

The loss of Resolution Life was unfortunate but has validated the rationale to create a business with significant scale and diversification of revenues by asset class, business type and in particular client mandate.

Throughout this period F&C employees have shown tremendous commitment and I would like to pay tribute to their hard work and professionalism.

Looking ahead, I am confident that over the medium term we will achieve to our stated objective of excelling in everything we do.

Alain L. Grisay
*Chief Executive*
20 March 2006

# Corporate Responsibility ("CR") Report

### CR Commitment

The Board is committed to maintaining the highest standards of governance and corporate citizenship. We recognise that in addition to our responsibilities to clients and shareholders we also have responsibilities to employees, suppliers, the environment, the companies in which we invest and the wider community in which we operate.

### 2005 Commentary/CR Highlights:

Good progress was made during 2005 by way of taking the Company's CR principles to the recently acquired overseas offices. The appointment of a CR Manager has benefited the organisation by providing a focus for CR initiatives and co-ordination of CR activity across the group. Here we summarise our approach to CR and highlight key activities undertaken during the year. The full CR report can be viewed on our website. The CR report and Annual Report and Financial Statements together provide a comprehensive review of our economic, social and environmental performance.

### F&C's CR Principles

The Board of F&C has adopted a statement of principles in relation to all governance, and corporate responsibility matters.

### Areas of Influence

F&C operates within a highly regulated industry with offices in the UK, Ireland, The Netherlands, Portugal, France, Germany and the US. F&C recognises the requirement to ensure it has in place strong internal procedures and good housekeeping practices to promote best practice governance and CR activities within the F&C Group. F&C also acknowledges that our "direct impacts" on our local environment and communities are inevitably much less than our "indirect impacts". The enlarged group is committed to governance and social responsibility in its investment philosophy.

### Ethically screened funds

F&C offers a range of ethically screened funds including the top performing Stewardship Fund, which was named as the top performing UK Equity Pooled Pension Fund.

### Engagement on governance, social, environmental and ethical issues

As a major asset management company investing over £131 billion on behalf of our clients, our most significant contribution continues to be through our ability to influence the behaviour of companies in which we invest on our clients' behalf. This ability – and the associated responsibilities – are greatest in respect of the £27.1 billion (2004 – £20.1 billion) of equity shares we manage on behalf of our clients under our responsible engagement overlay ("*reo*®") service. The *reo*® service is also extended to certain clients where we do not manage the underlying investments. In these cases, the service extends to either engagement or engagement and voting on clients' behalf. At 31 December 2005 these services extended to a further £9 billion of assets. We continue to be a leading force for influencing the way the companies in which we invest are run and their approach to longer-term issues such as human rights and climate change.

Since the merger, our Governance and Socially Responsible Investment ("GSRI") team has not only been meeting with representatives of our overseas offices but has also undertaken presentations to a number of overseas clients who have an interest and need for the services provided by the GSRI team. We believe that this is an exciting area of opportunity for the business and one where we have a leading edge product which is now becoming recognised on a pan European basis.

At 31 December 2005 the GSRI team comprised 14 staff. During 2005, the GSRI team engaged globally with 834 companies and achieved 272 milestones representing significant change by companies, as a result of F&C's intervention.

# Corporate Responsibility ("CR") Report

### Governance Structure, Risk and Management Systems

The Board is ultimately responsible for corporate governance and CR within the Company. Development of F&C's policies on CR and their implementation throughout the F&C group are co-ordinated by a CR Committee chaired by Ian Paterson Brown, an Executive Director of the Company. Fernando Ribeiro, Head of Investments, chairs the Corporate Governance Committee, which review the standards of corporate governance we expect from the companies in which we invest.

F&C operates an effective risk management system, including reputational and other Social Environmental and Ethical risks, through quarterly "Turnbull" management reporting. CR and governance policies are reviewed at least annually and, where appropriate, revised to meet improving standards and to help embed them further within the organisation. All individuals responsible for managing aspects of CR have, within their role profiles, references to reflect CR responsibilities. This facilitates the management of CR targets and, where relevant, is taken into account in determining performance related bonuses.

F&C also continues to work closely with its majority shareholder, Friends Provident plc, on CR policies and practices throughout the wider Friends Provident group.

F&C has in place a CR management system which complements the database currently in place for the management and reporting of F&C's indirect impacts relating to engagement and governance of the companies in which it invests. At each meeting of the CR Committee, progress against the annual targets and objectives set by the Board is reviewed with reference to key performance indicators derived from the CR management system. Further detail of the CR targets and objectives are contained in the CR report published on the Company's website.

### Stakeholder Engagement

F&C identifies its key stakeholders as shareholders, clients, employees, suppliers, non-government organisations, the wider community, other asset management companies and companies in which we invest. We engage widely with stakeholder groups through regular dialogue which is tailored to meet the requirements of each stakeholder group.

### CR Performance Indicators

F&C has established key performance indicators (KPI's) for Economic, Environmental and Social performance in relation to our indirect and direct impacts. A full report on performance against the KPI's can be found in our Annual CR Report published on the Company's website.

### Financial & Economic Contributions

Included within the Directors' Remuneration Report on pages 46 to 60 is further analysis on F&C's employee remuneration packages (salaries, pensions and other benefits). The Company's payment policy and practice to suppliers is set out on page 24. Information on shareholder returns and other financial information is set out in the notes to the financial statements on pages 79 to 159

### Environment

*Indirect Impacts*

F&C engages investee companies particularly on matters of climate change, environmental management and biodiversity. In 2005, the GSRI team published research reports on Investors Statement on Payments Transparency in the Extractive Sectors, HIV/Aids Beyond Africa and The Ethics of Influence identifying the companies and sectors with greatest exposure to those issues and recommendations for how to manage them effectively.

*Direct Impacts*

F&C also recognises that it has some direct impacts on the environment therefore F&C has set and adhered to targets on recycling, carbon dioxide emissions and waste disposal.

### Workplace

*Labour practices and Human Rights.*

*Indirect Impacts*

F&C engages with investee companies in relation to labour standards, HIV/Aids and human rights.

*Direct Impacts*

F&C has an Equal Opportunities policy covering gender, race, sexual orientation etc. Training will be delivered to all managers during 2006 and will be repeated for all managers on a regular basis.

F&C has policies on Health & Safety practices and provides training to appropriate employees.

Details of the remuneration policies applied to all employees are contained within the Directors' Remuneration Report on pages 46 to 60.

### Marketplace

F&C adopts a responsible approach to all external marketing and advertising. All literature issued by F&C is reviewed and approved by the Audit, Risk & Compliance department prior to release. All employees within F&C receive training and once in every two year period are required to pass a test to ensure their understanding of the importance of general regulatory compliance and Money Laundering prevention.

F&C's Charities Committee, a sub-committee of the CR Committee, is responsible for considering and approving any donations to charity under four key criteria: Education and Young People; Health and Healthcare; Sustainability and Environment; and Community. In addition, the Company provides the facility for all employees to make contributions under the Give As You Earn ("GAYE") arrangements and, within certain restrictions, will match employee led fundraising or contributions. During 2005 approximately 8 per cent. of all employees participated in GAYE.

### Assurance

This section of the Annual Report and Financial Statements, when read in conjunction with the CR report published on the Company's website, is in accordance with the 2002 GRI Guidelines.

F&C has been a constituent of FTSE4GOOD since the inception of the index in 2001.

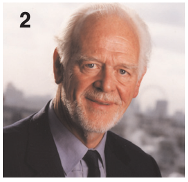
Our ethically screened funds and *reo*® process are subject to external review by an Independent Committee of Reference.

All statements made in the CR Report together with further details on all CR policies can be found within the CR section on the Company's website, www.fandc.com.

Alain Grisay
10 April 2006

Ian Paterson Brown
10 April 2006

# Non-executive Directors








### 1. Robert Jenkins‡, BA, MA
Age 55 *Chairman*

Mr Jenkins joined the Board on completion of the merger in October 2004. Prior to his appointment Mr Jenkins was Chief Executive of the acquired F&CGH. Prior to joining F&CGH in 1997, Mr Jenkins spent over five years with Credit Suisse Asset Management ("CSAM") and 16 years with Citibank. At Citibank Mr Jenkins held senior assignments in Dubai, Bahrain, Zurich, New York and Tokyo. From 1992 until 1995 he was Chief Investment Officer and Head of Asset Management for CSAM in Japan. In 1995 he transferred to London where he was Chief Operating Officer for CSAM in the UK and Central and Eastern Europe. Mr Jenkins joined F&CGH in 1997 and served as Chief Executive from January 1998 to October 2004.

### 2. Christopher Jemmett†
Age 69 *Deputy Chairman and Senior Independent Director*

Mr Jemmett joined the Board in February 1998. Mr Jemmett was appointed as an independent, Non-Executive Director of Friends Provident plc in June 2001 having been an independent, Non-Executive Director of Friends' Provident Life Office from 1997 until 2001. He was formerly a Director and member of the Executive Committee of Unilever plc and Unilever NV, a member of the Council of The Crown Agents Foundation and a member of The Council of Royal Warrant Holders Associations. Mr Jemmett was appointed Deputy Chairman of F&C in May 1998.

* Member of the Remuneration Committee

† Member of the Audit & Compliance Committee

‡ Member of the Nomination Committee

### 3. Keith Bedell-Pearce*†, LLB, MSc
Age 60 *Independent Director*

Mr Bedell-Pearce, a solicitor, joined the Board in December 2002. Until December 2001, Mr Bedell-Pearce was an Executive Director of Prudential plc with over 30 years experience in the financial services industry. He is currently Non-Executive Chairman of Norwich & Peterborough Building Society and Executive Chairman of The Student Loans Company Limited (a part-time public appointment).

### 4. Dick de Beus‡
Age 59 *Independent Director*

Mr de Beus joined the Board on completion of the merger in October 2004. Mr de Beus has worked for over 30 years in the pension fund industry. He joined PGGM, the Dutch pension fund for the healthcare and welfare industry, in 1979 and retired as Chairman in 2004. Mr de Beus is vice chairman of the Supervisory Board of Kas Bank N.V. (European custodian services, Amsterdam). Mr de Beus served as a Non-Executive Director of F&CGH since his appointment in February 2004.

### 5. David Gray†‡, CA
Age 54 *Independent Director*

Mr Gray joined the Board in May 1999. Until November 1999, he was Business Development Director of Scottish and Southern Energy plc, having previously been Finance Director of Scottish Hydro-Electric plc. He is a Director of DTZ Holdings plc and Romag Holdings plc, Chairman of DTZ Pieda Consulting Ltd and a board member of Scottish Water.

### 6. John Heywood*†, LLB
Age 68 *Independent Director*

Mr Heywood joined the Board on completion of the merger in October 2004. Mr Heywood worked for 20 years at Jardine Matheson & Co Ltd where he served as Managing Director. He was Chairman of Clayhithe PLC from 1993 – 1998. Mr Heywood is a Non-Executive Director of Lavendon plc. Mr Heywood served as a Non-Executive Director of F&CGH since his appointment in January 1998.

### 7. Brian Larcombe*,
Age 52 *Independent Director*

Mr Larcombe joined the Board in January 2005. Prior to his appointment, Mr Larcombe was Chief Executive of 3i Group plc and is currently Deputy Chairman of Party Gaming plc and a Non-Executive director of Smith & Nephew plc.

### 8. Karen McPherson*‡, MA
Age 54 *Independent Director*

Ms McPherson joined the Board on completion of the merger in October 2004. Ms McPherson has had a long term international career in human resources management with Royal Dutch Shell Group, Edward Lumley Limited, Towers Perrin, Chemical Bank and JP Morgan. In 2000 Ms McPherson founded Potential Unlimited, a strategic change management and executive coaching consultancy. Ms McPherson served as a Non-Executive Director of F&CGH since her appointment in September 1998, having previously spent over a year as an executive member of staff.

### 9. Jeff Medlock, B.Sc(Econ), F.I.A.

Age 65

Mr Medlock joined the Board on completion of the merger in October 2004. Mr Medlock, an actuary, was Chief Executive Officer of Eureko from its formation in 1992 until 1999 when he became Chief Financial Officer at Achmea. Mr Medlock returned to the board of Eureko in 2002 shortly after its merger with Achmea and Seguros e Pensoes as Chief Financial Officer. Mr Medlock retired from Eureko in March 2004 but remains a member of the board of several of the group's insurance subsidiaries, and is an adviser to the board of Eureko. Mr Medlock previously spent 20 years with Equity & Law and 8 years on the board of Royal Life Holdings.

### 10. Philip Moore, TD, MA, F.I.A.

Age 46

Mr Moore joined the Board in January 2005. He joined Friends Provident plc on 1 July 2003 and was appointed Group Finance Director of Friends Provident plc on 1 September 2003. Mr Moore was previously at AMP (UK) where he was Corporate Director of Finance and Head of Mergers and Acquisitions, having been Finance Director and actuary of NPI on its acquisition by AMP. Prior to joining NPI in 1998 he spent 9 years at PricewaterhouseCoopers, initially in London and then based in Hong Kong as the partner responsible for the firm's East Asia Insurance Consultancy Practice.

### 11. Keith Satchell‡, BSc, F.I.A.

Age 54

Mr Satchell, an actuary, joined the Board in February 1998. Mr Satchell was appointed Group Chief Executive and an executive director of Friends Provident plc in June 2001, having been an Executive Director of Friends' Provident Life Office since 1992 and its Chief Executive since 1997. He is also a member of the senior board of Banco Commercial Portugues SA (incorporated in Portugal) and a board member of Swiss Mobiliar Cooperative Company (incorporated in Switzerland) and European Alliance Partners AG (which is incorporated in Switzerland).

## Executive **Directors**




### 12. Howard Carter, BA, MA

Age 54, *Executive*

Mr Carter joined the Friends Provident Group in 1988 from Prudential-Bache Capital Funding Limited, where he was a director. He served as the Company's Chief Investment Officer from February 1998 until his appointment as Chief Executive in September 2000. Mr Carter was appointed an Executive Director of Friends Provident plc on 5 June 2001.

### 13. Alain Grisay, LLM, MA

Age 51, Chief Executive

Mr Grisay, joined the Board on completion of the merger in October 2004 having previously been Deputy Chief Executive of F&CGH and head of the institutional business. Prior to joining F&C in April 2001, Mr Grisay was at JP Morgan for 20 years, serving as Managing Director responsible for the investment bank's market client business in Europe. Mr Grisay was appointed an Executive Director of Friends Provident plc on 1 January 2006.

### 14. Ian Paterson Brown, CA, MSI, ACIS

Age 52, *Chief Financial Officer*

A chartered accountant, Mr Paterson Brown joined the Board following the acquisition of Royal & SunAlliance Investments in July 2002. Prior to his appointment to the Board, Mr Paterson Brown was Group Company Secretary of Friends Ivory & Sime plc. He joined the company in 1982.

# Report of the Directors

The Directors submit the Report and Financial Statements of the Company and of the group for the year ended 31 December 2005. These are the first full consolidated financial statements which have been prepared in accordance with International Financial Reporting Standards (IFRS). This report together with the Directors' Reports on Corporate Governance and Remuneration and the financial statements that follow will be laid before the Annual General Meeting on Tuesday, 16 May 2006.

### Results, business review and dividend

The group's results for the year ended 31 December 2005 are shown in the consolidated income statement on page 65. A business review of the year ended 31 December 2005 and future developments are covered in the Chairman's Statement and Chief Executive's Report on pages 2 and 3 respectively.

The group loss for the year, after tax, amounted to £77,273,000.

The Directors recommend a final ordinary dividend of 7.0 pence per share, amounting to £33,381,000, resulting in a total of 11.0 pence and £52,246,000 for the year respectively. Preference dividends of £53,000 were also incurred during the year.

The final ordinary dividend, if approved, will be paid on 19 May 2006 to ordinary shareholders whose names are on the register on 7 April 2006. No liability for the proposed dividends has been recognised as at 31 December 2005, in accordance with IFRS.

### Principal activity and status

The group's business is asset management. Details of the progress of the business during the year and of future prospects are contained in the Chairman's Statement and the Chief Executive's Report.

The Company is registered as a Public Limited Company in terms of the Companies Act 1985 and is currently a constituent of the FTSE 250 Index.

The Company is incorporated in Scotland and the Company is domiciled in the United Kingdom.

### Property, Plant and Equipment

Details of changes in property, plant and equipment are disclosed in note 12 to the financial statements. At 31 December 2005, there were no significant differences between the net book and market value of property, plant and equipment.

### Financial Instruments

Details of financial instruments are disclosed in note 19 to the financial statements. The financial risk management and objectives of the group are contained in note 35.

### Share capital and directors' interests

During the year the Company issued 1,234,106 ordinary shares in respect of options granted under the 1995 Share Option Scheme and 2002 Share Option Scheme.

Details of shares under option at 31 December 2005 are shown on pages 58 to 60 of the Directors' Remuneration Report. Details of all shares issued during the year ended 31 December 2005, are given in note 30.

The Directors who held office at the year end and their interests in the share capital of the Company are shown below:

| | | 31 December 2005 Ordinary Shares | 31 December 2004 or date of appointment if later Ordinary Shares |
|---|---|---|---|
| Robert Jenkins | Beneficial | **100,000** | 100,000 |
| | Non Beneficial* | **890,200** | 969,700 |
| Christopher Jemmett | Beneficial | **24,476** | 23,065 |
| Howard Carter | Beneficial | **39,063** | 43,364 |
| Dick de Beus | Beneficial | **Nil** | Nil |
| Keith Bedell-Pearce | Beneficial | **51,285** | 51,285 |
| David Gray | Beneficial | **5,000** | 5,000 |
| Alain Grisay | Beneficial† | **726,297** | 1,195,637 |
| John Heywood | Beneficial | **4,326** | 4,326 |
| Brian Larcombe | Beneficial | **Nil** | Nil |
| Karen McPherson | Beneficial | **Nil** | Nil |
| | Non Beneficial* | **890,200** | 969,700 |
| Jeff Medlock | Beneficial | **10,000** | 10,000 |
| Philip Moore | Beneficial | **2,163** | 2,163 |
| Ian Paterson Brown | Beneficial | **195,771** | 195,021 |
| | Non Beneficial** | **Nil** | 158,382 |
| Keith Satchell | Beneficial | **14,326** | 14,326 |

* Robert Jenkins and Karen McPherson are Directors of the F&C Group ESOP Trustee Limited, a company incorporated in 1995 as a discretionary employee benefit trust to encourage and facilitate the acquisition and holding of shares in the Company by employees.

** Ian Paterson Brown is a trustee of the Friends Ivory & Sime Staff Share Ownership Scheme.

† These shares represent the extent of Alain Grisay's participation in the Re-Investment Plan and Purchased Equity Plan approved by shareholders on 4 October 2004. Further details of these plans are set out in the Remuneration Report on pages 46 to 60.

Since 31 December 2005, Messrs Carter and Paterson Brown have each acquired a total of 181 ordinary shares through monthly subscriptions into the Company's Share Incentive Plan. On 24 March 2006 Alain Grisay acquired 197,674 ordinary shares at a price of 215.00 pence per share under the mandatory deferral rules of the Company's Purchased Equity Plan. On 28 March 2006 Howard Carter sold 37,461 ordinary shares at a price of 215.00 pence per share and Robert Jenkins bought 100,000 ordinary shares at a price of 215.50 pence per share. No other changes to Directors' interests have occurred.

In addition, Kenneth Inglis and Brian Sweetland served as Directors of the Company until their resignations on 26 April 2005 and 24 January 2005 respectively.

The Directors who held office at the year end and their interests in the share capital of the ultimate parent undertaking, Friends Provident plc, are shown below:

| | | 31 December 2005 Ordinary Shares | 31 December 2004 Ordinary Shares |
|---|---|---|---|
| Howard Carter | Beneficial | **24,560** | 24,560 |
| Christopher Jemmett | Beneficial | **2,655** | 2,655 |
| Philip Moore | Beneficial | **1,332** | 1,332 |
| Keith Satchell | Beneficial | **63,528** | 62,668 |

# Report of the Directors

### Directors' and officers' insurance

The Company maintains insurance cover in respect of directors' and officers' liability.

### Charitable and political contributions

During the year the group made contributions to charity of £75,000 (2004 – £85,000). No political donations were made during the year (2004 – £nil). Further details on the criteria for charitable giving are contained on page 19, in the Corporate Responsibility Report.

### Payment policy and practice

It is the Company's payment policy to ensure settlement of suppliers' accounts in accordance with the stated terms. In certain circumstances, settlement terms are agreed prior to any business taking place. It is our policy to abide by those terms.

At 31 December 2005, trade creditors represented the equivalent of 15 days (2004 – 20 days) of the annual purchases invoiced by the suppliers to the group.

### Substantial interests in share capital

The Company has been informed of the following substantial interests as at 31 March 2006. No other person has notified an interest in the ordinary shares of the Company required to be disclosed to the Company in accordance with sections 198 to 208 of the Companies Act 1985.

| | Ordinary Shares | Percentage |
|---|---|---|
| Friends Provident plc | 251,255,680 | 51.9 |
| Eureko B.V. | 99,283,053 | 20.6 |

### Capital Requirements Directive (''CRD'')

In October 2003 the Financial Services Authority (FSA) issued a policy statement ''Amendments to the Interim Prudential Sourcebook for Investment Businesses chapter 5 rules on consolidated supervision''. In this policy statement the FSA set out the requirements that need to be met and the procedure that needs to be followed to obtain a ''CAD waiver''. Since the introduction of the policy statement the group has issued annual notifications to the FSA under rule 5.7.1(4) advising that it was seeking to forego consolidated supervision and would comply with the FSA requirements which include disclosing in the audited financial statements that it operates under a waiver in respect of the regulatory consolidated capital requirements.

### Markets in Financial Instruments Directive (''MiFID'')

MiFID is a wide ranging Directive, constituting a major element in the EU's Financial Services Action Plan. The Directive substantially revises the current Investment Services Directive and is intended to promote a single market for wholesale and retail transactions in financial instruments. We anticipate that this Directive will impact F&C in a number of areas. An initial impact assessment has been completed and as such we are well placed to implement the required changes that will follow the FSA Consultation papers this year. The Directive will affect various matters but in particular addresses: best execution; product design; trade and transaction reporting; governance and risk; outsourcing; cross border business; client classifications; and marketing and distribution.

Final rules are expected in the UK by 31 January 2007, and compliance by all firms required by 1 November 2007.

### Employees

At 1 February 2006 there were 713 full-time employees and 45 part-time employees within the group
(1 February 2005 – 815 full-time employees and 48 part-time employees).

### Disabled employees

The group gives full consideration to applications for employment from disabled persons where the requirements of the job can be adequately fulfilled by a handicapped or disabled person.

Where existing employees become disabled, it is the group's policy wherever practicable to provide continuing employment under normal terms and conditions and to provide training, career development and promotion to disabled employees wherever possible.

### Employee involvement

During the year, the policy of providing employees with information about the group has been continued through internal presentations by the Management Committee and the internal publication of relevant information. Wherever appropriate, employees are consulted to ensure that their views are taken into account before decisions are taken which are likely to affect their interests.

### Equal opportunities

The Company aims to provide equal opportunities for all, without discrimination on the grounds of race, religion, marital status, age, sex, sexual orientation or disability. We recruit and promote those best suited for the job. The Company respects the dignity of individuals and their beliefs. The Company does not tolerate any sexual, racial, physical or mental harassment of staff in the work place.

### Share incentive schemes

During the year employees participated directly in the business through a number of Employee Share Schemes, details of which are included within the Directors' Remuneration Report on pages 46 to 60.

### Annual General Meeting

The Company will hold its Annual General Meeting on Tuesday, 16 May 2006 at The Signet Library, Parliament Square, Edinburgh EH1 1RF. The meeting will start at 12 noon. Details of all resolutions being put to shareholders are set out in the Notice of Annual General Meeting on pages 190 to 192.

### Voting Online

On 4 October 2004, shareholders approved amendments to the Company's Articles of Association to allow electronic voting. In accordance with good governance practice the Company is therefore offering shareholders use of an online voting service, ''sharevote'', offered by the Company's registrar, Lloyds TSB Registrars at www.sharevote.co.uk. Shareholders can use this service to vote or appoint a proxy online. The same voting deadline (12 noon on 14 May 2006) applies as if you were using your Personalised Voting Form to vote or appoint a proxy by post to vote for you. You will need to use the unique personal identification details (Reference Number, Card ID and Account Number) that are printed on your Personalised Voting Form.

### CREST members

Registered shareholders who are CREST members and who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so for the Annual General Meeting to be held on 16 May 2006, or any adjournment of it, by utilising the procedures described in the CREST Manual. CREST Personal Members or other CREST Sponsored Members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf.

In order for a proxy appointment made by means of CREST to be valid, the appropriate CREST message (a ''CREST Proxy Instruction'') must be properly authenticated in accordance with CRESTCo's specifications and must contain the information required for such instructions, as described in the CREST Manual. The message regardless of whether it constitutes the appointment of a proxy or an amendment to the instruction given to a previously appointed proxy must, in order to be valid, be transmitted so as to be received by the issuer's agent, Lloyds TSB Registrars (ID 7RA01), by 12 noon on 14 May 2006. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the issuer's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001.

**Relationship agreement**

The relationship agreement formalises the ongoing relationship between the Company and its parent, Friends Provident plc, and Friends Provident plc's subsidiaries. The relationship agreement contains provisions which permit the Friends Provident group to participate in future issues of equity shares by the Company not made to existing shareholders in proportion to their existing holdings in order to maintain its percentage shareholding in the Company. Your Directors are recommending that the relationship agreement be re-approved and the authority be renewed at this year's Annual General Meeting pursuant to resolution 9. Members of the Friends Provident group will abstain from voting on such ordinary resolution.

**Board changes**

As reported in December 2005, the Group is expecting in 2006 to meet the £33m of synergies indicated at the time of the merger. Therefore, the Board is now focussing on how best to take advantage of the opportunities provided by the enlarged group in future years, and is putting in place an executive team to steer the Company through its next phase of growth.

As has previously been reported, Howard Carter will retire from the Board and leave the Company on conclusion of this year's Annual General Meeting. This follows Alain Grisay's appointment as CEO with effect from 1 January this year.

Mr Carter will leave the Company on contractual terms.

In addition, having assisted with the successful integration of F&C and ISIS and the achievement of the synergy targets set at the time of the merger, it has been announced that Ian Paterson Brown, the Company's Chief Financial Officer will also retire from the Board and leave the Company on conclusion of this year's Annual General Meeting.

Ian Paterson Brown has been employed by the Company for 24 years, serving 9 of them as an Executive Director. Through that period he has been a key member of the management team and has played an important role in overseeing the creation of a top five UK asset manager. Most recently Mr Paterson Brown played a major role in the integration of F&C following the merger in 2004.

Mr Paterson Brown will leave the Company on 16 May 2006 with a severance package valued at approximately £712,900. This represents £65,000 in respect of his statutory employment protection entitlement and £647,900 in respect of his contractual entitlements. This latter element is comprised as follows: (a) £22,900 (accrued holiday entitlement), (b) £587,000 as a pension augmentation (by way of compensation sacrifice by Mr Paterson Brown) and (c) £38,000 cash. The Company has also made available to Mr Paterson Brown outplacement support and has made a contribution to Mr Paterson Brown's legal fees.

In addition, recognising the significant contribution Mr Paterson Brown has made to the Company over his 24 years of service, the Board is proposing to augment the pension terms for Mr Paterson Brown by waiving the early retirement factor within his pension arrangements. The cost of this augmentation has been quantified at £514,000 on an on-going basis.

The Board acknowledge that this pension augmentation means that Mr Paterson Brown's separation terms exceed his contractual and statutory entitlements and has therefore included in the Notice of Annual Meeting set out on page 190 a separate resolution to shareholders on this matter.

### Overview of changes to the Remuneration Framework

During 2005 and early in 2006, the Remuneration Committee undertook a comprehensive review of the remuneration practices at F&C Asset Management plc and in particular the effectiveness of the Company's long term incentive schemes. This review was conducted in light of the current challenges facing the Company as set out in the Chairman's Statement and Chief Executive's Report.

The ability to attract and retain high calibre employees who are incentivised to take the Company into its next phase of development following the merger, for the benefit of all shareholders, is essential.

As a result of this review the Remuneration Committee and the Board concluded that the long term element of the Company's remuneration framework should be modified. In particular the Remuneration Committee had addressed the question of staff retention among the less senior, but nevertheless important members of staff. The mechanism proposed is to make awards of stock, the level of award dependent on performance, restricted for three years which in effect represents a deferred bonus paid in stock. In determining the most appropriate mechanism to make such awards the Committee realised that they would either need to introduce a new scheme or modify the rules of the Company's existing Long Term Remuneration Plan (LTRP) to produce the same result. To minimise cost and to ease administration the Remuneration Committee are proposing to modify the rules of the Company's existing LTRP under Resolution 12.

In considering the suggested modifications detailed below, the Board, through the Remuneration Committee, has consulted with a number of the Company's shareholders.

### Modifications applying on a transitional basis only

Resolution 11 detailed below is an ordinary resolution relating to the earnings per share performance conditions within each of the Company's Long Term Incentive Schemes. This proposal is a one off transitional adjustment applying only to the existing awards and any awards to be made in 2006. It will provide the Company with enhanced retention arrangements until 2009. This is the period believed by the Board to cover the duration of the next phase in the Company's development.

### Modifications applying on an ongoing basis

Resolution 12 detailed below is an ordinary resolution seeking the authority to amend the terms of the Company's Long Term Remuneration Plan (LTRP). The proposed change, if approved, will provide the Board with the flexibility to grant equity awards to employees below Executive Director level that are not subject to ongoing performance conditions. All grants made to participants of the LTRP are made on merit, awarded on an assessment of the participants past performance (based on their specified objectives) and expected contribution to the business. Award levels are determined by the Remuneration Committee with reference to Company performance, market competitiveness (assessed on a total compensation basis using independent market total compensation data) and individual performance.

### Adjustments to Earnings per Share (EPS) performance condition within the Company's Long Term Incentive Schemes

#### (i) Withdrawal of Resolution Life funds

As reported in December 2005, the full-year impact on the Company's earnings of the withdrawal of Resolution funds will be in the region of 3.0 pence per ordinary share. With 60 per cent. of the Resolution funds being withdrawn through January 2006, a significant proportion of this impact will be felt in 2006.

As compensation for the withdrawal of funds, the Company will receive a payment of approximately £27 million from Resolution plc. For technical accounting reasons this payment will be offset by a corresponding reduction in the carrying value of the intangible management contracts. Accordingly, while the loss of earnings from the Resolution plc assets will impact 2006 EPS, the counterbalancing compensation payment will not.

In recognising the exceptional circumstances surrounding the loss of the Resolution Life assets and the fact that the loss was in no way attributable to weaknesses in the services provided to Resolution plc as a client, the Board is seeking within resolution 11 set out in the Notice of Annual General Meeting on page 190 authority to make a one off adjustment to the 2006 earnings for the purposes of measuring the performance conditions attached to the Company's long term incentive schemes. While the Board have been advised that the proposed adjustment is permissible under the rules of each of the Company's long term incentive schemes, the inclusion of resolution 11 within the Notice of Annual General Meeting reflects the Board's desire to adopt the highest standards of corporate governance and shareholder relation practices.

The Board is proposing to finalise the quantum of the above adjustment after the 2006 year end results have been completed and the true impact of the loss of the Resolution plc contracts on the 2006 earnings is known with certainty. The actual adjustment made will therefore depend upon the precise timing of the withdrawal of the Resolution funds. The Board has resolved within resolution 11 that the maximum adjustment that would be applied to the 2006 EPS would be the full year impact of 3.0 pence per share.

The Board is satisfied that with this adjustment the performance conditions attached to the long term incentive schemes remain appropriately stretching and in line with the original intention of the plans set out at the time of the merger.

For future awards under the Company's long-term plans, the Board is proposing to exclude earnings from Resolution Life funds from the base year EPS figure, to ensure a challenging yet achievable basis for comparison for future years.

**(ii) International Financial Reporting Standards (IFRS)**

The introduction of IFRS introduces a requirement, in line with best practice, to adjust EPS growth figures for performance periods bridging the transition, in order to ensure a fair and consistent comparison between the base year and the final year.

For the 2004 long-term awards, EPS in 2006 is compared with EPS in 2003. To ensure consistency of comparison, the Board is proposing to measure growth over each year of the performance period using figures calculated on a consistent set of accounting standards. Therefore, growth from 2003 to 2004 will be measured using underlying EPS figures calculated under UK GAAP, and growth for each future year will be measured using figures calculated under IFRS compared with 2004 underlying EPS restatement under IFRS.

Each of these amendments will be made formally at the end of 2006 once the pattern of outflows of Resolution funds is known and once the 2006 EPS is finalised. We are, however, bringing these issues to shareholders' attention, in accordance with best practice in shareholder consultation.

**Amendments to the rules of the Company's Long Term Remuneration Plan (LTRP)**

At present, the vesting of all awards granted under the LTRP is governed by the extent to which specified performance conditions (currently a combination of Total Shareholder Return (TSR) and EPS targets) are achieved over a pre-determined performance period (currently a period of three consecutive financial years). In addition, vesting is also dependent on the relevant participant remaining in employment until the third anniversary of the date of grant.

All grants made to participants of the LTRP are made on merit, awarded on an assessment of the participants' past performance (based on their specified objectives) and expected future contribution to the business.

The Remuneration Committee is of the view that it is entirely appropriate for awards granted under the LTRP to Executive Directors to continue to be governed by the above performance conditions, as well as a continuing service requirement. Executive Directors have the ability to influence, and are ultimately responsible to shareholders for delivering, share price and earnings growth. As a result, Executive Directors have a clear ''line of sight'' to the targets currently applied to their LTRP awards, which make them an effective and appropriate means of incentivising high levels of performance.

In the case of other members of the senior management team who participate in the LTRP, the link between their specific roles, responsibilities and objectives and the overall performance conditions that need to be satisfied for their LTRP awards to vest is less direct. The Committee is also of the view that the imposition of targets over which these participants have less control or ability to influence reduces the effectiveness of the LTRP awards as a means of retaining their services over the medium to long term.

In light of the above, the Board is seeking authority within resolution 12 set out in the Notice of the Annual General Meeting on page 190 to amend the rules of the LTRP as a mechanism to provide the Remuneration Committee and management with the flexibility to grant awards, the vesting of which is conditional solely on the continued employment of the relevant participant over a three year period from grant. The availability of this new form of award, which in effect would represent a Deferred Share Plan element of the LTRP, would enhance management's ability to use the plan as a means of retaining key staff below Executive Director level. It would also allow the Committee to align better the conditions attached to future awards with the contribution made to the business by the relevant participants.

A summary of how the amended LTRP will be operated is set out below:

- In the case of the less senior participants in the LTRP, it is proposed that future awards granted to them under the plan will not be subject to any ongoing performance conditions. As a result, vesting of their awards will be dependent on continued employment until the third anniversary of the date of grant. To the extent that awards are made without ongoing performance conditions, the number of shares will be reduced so as to give no more than the same anticipated accounting cost as an award with ongoing performance conditions. (The average and median face value of awards under this category, to be awarded to around 150 participants, are expected, on an annual basis, to be around £30,000 and £20,000 respectively). No individual award under this category is expected to exceed a face value of £200,000.
- Members of the Company's Executive Committee and Management Committee excluding Executive Directors (being those members of staff responsible for the management of the business and in delivering the Board approved strategy) and other members of staff deemed key to the long term success of the business, will receive a combination of performance based and non-performance based awards. (The average and median face value of the combination awards under this category, awarded to around 20 participants, are expected, on an annual basis, to be around £150,000 and £120,000 respectively). No individual award under this category is expected to exceed a face value of £400,000.
- No change will be made to the awards made to the Company's Executive Directors (i.e. their awards will continue to be fully conditional on the extent to which the existing performance conditions are satisfied).

No other substantive changes are proposed to the rules of the LTRP and all awards made under the LTRP will continue to be made on merit. The Company will continue to operate within the dilution limits approved by shareholders on creation of the LTRP in October 2004 and the changes are, due to intended reductions in the level of grants, also expected to be cost neutral in terms of the annual charge in the Group's Income Statement.

Copies of the revised rules of the Company's LTRP are available for inspection at the Company's registered office.

### Authority to allot ordinary shares and disapplication of pre-emption rights

Ordinary resolution 13 will be put to the Annual General Meeting of the Company to renew the present authority of the Directors to exercise their powers to allot authorised but unissued ordinary shares. Such authority will cover a maximum of 159,249,760 unissued ordinary shares, being up to an aggregate maximum nominal amount of £159,249.76. This maximum nominal amount represents 33.33 per cent. of the Company's total ordinary share capital in issue at the date of this report (calculated exclusive of treasury shares) and meets institutional guidelines. The Company holds 6,564,104 ordinary shares in treasury, through ESOP Trusts, at the date of this report. This amount represents 1.37 per cent. of the Company's total ordinary share capital in issue at the date of this report (calculated exclusive of treasury shares). The authority conferred by this resolution will expire on the conclusion of the Annual General Meeting of the Company to be held in 2007.

Special resolution 14 will be put to the Annual General Meeting of the Company to renew the present power to allot unissued ordinary share capital and to sell ordinary shares held in treasury for cash without first being required to offer such shares to existing shareholders. Such power will cover a maximum of £159,249.76 of unissued ordinary share capital and, if renewed, will apply to:

(a) any ordinary shares allotted and treasury shares sold in accordance with the relationship agreement referred to above (conditional upon the passing of the ordinary resolution 9 referred to above);

(b) any ordinary shares allotted or treasury shares sold in order to satisfy options or awards under any share scheme for employees or share incentive plan approved by the Company in general meeting;

(c) any ordinary shares allotted or treasury shares sold pursuant to a rights issue or other pre-emptive offering (where legal or regulatory or other difficulties prevent the issue of shares wholly on a pre-emptive basis); and

(d) otherwise to ordinary shares representing 5 per cent. of the Company's issued ordinary share capital as at the date of this report.

The Directors consider that the authority proposed to be granted by resolution 13 and the power proposed to be granted by resolution 14 are necessary in order to take advantage of opportunities as they arise and to retain flexibility. The Directors do not have any intention of exercising such authority or power at the present time other than for the purposes referred to in (b) above.

The Companies (Acquisition of Own Shares Treasury Shares) Regulations 2003 (as amended) (''Treasury Shares Regulations'') came into force on 1 December 2003 and, by virtue of such regulations, companies which buy-back their own shares are now permitted to hold up to 10 per cent. in nominal value of the issued share capital in treasury rather than cancelling them as previously required. The Company may now hold such shares ''in treasury'' and then sell them at a later date for cash provided that, pursuant to the Treasury Shares Regulations, such sale is on a pre-emptive basis to existing shareholders unless shareholders agree by special resolution to disapply such pre-emption rights. Accordingly, in addition to giving the Directors power to allot unissued ordinary share capital on a non pre-emptive basis, special resolution 14 will also give the Directors power to sell ordinary shares held in treasury on a non pre-emptive basis, subject always in both cases to the limitations noted above. (Treasury shares are explained in more detail under the heading ''Purchase of own shares'' below).

**Purchase of own shares**

Special resolution 15 will be put to the Annual General Meeting to renew the present power to make market purchases of the Company's own ordinary shares. Pursuant to special resolution 15 the maximum aggregate number of ordinary shares which may be purchased pursuant to the authority shall be 10 per cent. of the issued ordinary share capital (excluding treasury shares) of the Company as at the date of the passing of the resolution (being 47,779,707 ordinary shares as at the date of this report). The minimum price which may be paid for an ordinary share shall be 0.1 pence (exclusive of expenses). The maximum price for an ordinary share (again exclusive of expenses) shall be an amount equal to 105 per cent. of the average of the middle market quotations for the Company's ordinary shares for the five business days immediately preceding the date of purchase. As at the date of this report, the Company had 21,253,232 options to subscribe for ordinary shares outstanding (representing 4.5 per cent. of the issued ordinary share capital of the Company (excluding treasury shares) at the same date). If the buy-back authority is renewed at the 2006 AGM and is then utilised in full, the options outstanding at the date of this report would represent 4.9 per cent. of the issued ordinary share capital of the Company (excluding treasury shares). The power conferred by this resolution will expire on the earlier of the first anniversary of the passing of this resolution and the conclusion of the Annual General Meeting of the Company to be held in 2007.

With the coming into force of the Treasury Shares Regulations on 1 December 2003, the Company may do any of the following things in respect of its own ordinary shares which it buys back and does not immediately cancel but, instead, holds ''in treasury'':

(a) sell such shares (or any of them) for cash (or its equivalent under the Treasury Shares Regulations);

(b) transfer the shares (or any of them) for the purposes of or pursuant to an employees' share scheme; or

(c) cancel the shares (or any of them).

The Directors may use the Treasury Shares Regulations in any one or more of the ways noted above and intend to take advantage of this flexibility as they deem appropriate. While any shares are held in treasury, voting rights are suspended and currently no dividends (or any other distribution) are paid (or made) on such shares.

While the Directors recognise that, due to the free float requirements, the scope for buy-backs may currently be limited, they consider it appropriate to have in place the facility to acquire shares in circumstances where they believe that future shareholder returns can be enhanced by taking such action. This authority, if renewed, will only be exercised if to do so would result in an increase in earnings per ordinary share and if it is considered to be in the best interests of shareholders generally.

During the year to 31 December 2005 the Company purchased 104,780 of its own Ordinary Shares of 0.1p representing less than 0.1 per cent. of the Ordinary Shares in issue at 31 December 2005 (2004 – 500,000 ordinary 0.1 pence shares representing 0.1 per cent. of the ordinary shares in issue at 31 December 2004) pursuant to this authority. The aggregate consideration paid for own share purchases in 2005 was £223,000 (2004 – £1,156,000).

### Auditors

Ernst & Young LLP have expressed their willingness to continue in office as auditors and a resolution proposing their re-appointment and for the Directors to determine their fees will be submitted at the Annual General Meeting.

Details of the auditors' remuneration is provided in note 4 to the financial statements and further detail on how the Board ensures the independence of the auditors is detailed on pages 44 and 45 within the Directors' Report on Corporate Governance.

By order of the Board,

W Marrack Tonkin, FCCA
*Secretary*

80 George Street
Edinburgh EH2 3BU
10 April 2006

# Directors' Report on Corporate Governance

The Company is committed to and strives for best practice in corporate governance. The Board is accountable to the Company's shareholders for good corporate governance. This statement describes how the principles of corporate governance set out in section one of the Combined Code issued in 2003 (''the Code'') have been applied.

### Statement of Compliance

The Directors consider that, save as next mentioned, the Company has throughout the year ended 31 December 2005 and up to the date hereof, applied the principles and met the requirements of the Code.

As disclosed in last year's Annual Report & Accounts, the appointment of Robert Jenkins as Non-Executive Chairman on 11 October 2004 following his role as Chief Executive of the acquired F&CGH meant that, on appointment, Mr Jenkins did not meet the definition of independence under the Code. The Directors continue to believe that Mr Jenkins' experience as the Chief Executive of F&CGH prior to the merger provides stability and continuity to ex-F&CGH clients and staff and that this stability and continuity together with the independence and extensive industry experience displayed by Mr Jenkins remains in the best interests of the Company.

The Board believes that the appointment of Alain Grisay as Chief Executive on 1 January 2006 does not in any way adversely impact the ongoing relationship between the Chairman and the Chief Executive. However, it acknowledges that some shareholders may hold a different view, given that Mr Jenkins and Mr Grisay previously served as Chief Executive and Deputy Chief Executive respectively within F&CGH (one of the two ''legacy'' companies prior to the merger). In the event that this relationship should ever become an issue for the Board, Christopher Jemmett, the Deputy Chairman and Senior Independent Director will as part of his board responsibilities consult with the other non-executive Directors and intervene as appropriate.

In light of this departure from the Code, and in the interests of promoting best practice shareholder relations, the Board is inviting shareholders to vote on the re-election of Robert Jenkins under resolution 3 set out in the Notice of Annual General Meeting on page 190.

While the Board has been provided with high level management information during the year, due to the extent of the merger activity and the resultant integration of systems and business processes, management information at a level of detail that the Board might reasonably expect was not readily available. Management have put in place processes and procedures that will in the future enhance the reporting of management information to the Board and the business.

The Chairmen of the Audit & Compliance, Remuneration and Nomination committees will be available to answer questions at this year's Annual General Meeting to be held on Tuesday, 16 May 2006.

### Going concern

The Code requires Directors to report, under the terms set out in the relevant guidelines to the Code, on the appropriateness of adopting the going concern basis in preparing financial statements.

The Directors consider that the group has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Directors consider that the business is a going concern and continue to adopt the going concern basis in preparing the financial statements.

### The Board

The Board of Directors currently comprises the Chairman, three Executive Directors and ten Non-Executive Directors, seven of whom the Board has identified as Independent Directors. Christopher Jemmett is the Deputy Chairman and Senior Independent Director. The biographies of the Directors appear on pages 20 and 21. These demonstrate a range of experience, skills and personal standing sufficient to bring independent judgement on issues of strategy, performance, resources and standards of conduct which are vital to the success of the group. All Directors have access to the advice and services of the Company Secretary, who is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with. The Board meets formally on a regular basis and is responsible for approving the group's objectives and policies. The Board focuses mainly on strategy, investment and financial performance, the group's control environment and executive management and board succession. To enable the Board to discharge its duties, all Directors receive appropriate and timely information ensuring that they are properly briefed on issues for consideration in advance of meetings. In addition, all Directors have access to senior management and can request, either during meetings or at other appropriate times, further explanation or written papers on matters as they see fit.

The Board has a detailed list of matters specifically reserved to it – the "Board Reserved List". This is contained in "The Directors' Guide", a training and reference document issued to all Directors on appointment and updated as appropriate. The Board Reserved List is reviewed annually and clearly sets out that authority is delegated from the Board to Board Committees and to management. This ensures that matters of significance are overseen and reviewed by the Board prior to implementation. Examples of matters reserved for the Board as set out in the Board Reserved List are the approval of: the group strategy; the annual budget; the composition and terms of reference of any of the Board Committees; the high level organisational structure and the review of the effectiveness of the group's system of internal control.

### Board composition

F&C Asset Management plc is a quoted subsidiary of Friends Provident plc ("FP"), which owns 51.9 per cent. of the Company. There are, in addition to a formal agreement to manage funds on behalf of FP, various other arrangements in place between the Company and FP, all of which are governed by independent agreements, the terms of which are approved by the minority shareholders as appropriate. New business created by FP has a direct benefit to the Company and the Company's investment performance has a direct impact on FP and its ability to develop its business. Because of this relationship, close co-operation and understanding of each other's businesses and strategies is very important. To facilitate this, Keith Satchell (FP Group Chief Executive) and Philip Moore (FP Group Finance Director), two of FP's Executive Directors, are Non-Executive Directors of the Company and Howard Carter, an Executive Director and Alain Grisay, the Company's Chief Executive, are Executive Directors of FP. Messrs Carter and Grisay receive no remuneration or benefits from FP. In addition, Christopher Jemmett is an independent Non-Executive Director of both FP and the Company. The Board considers Mr Jemmett to be independent in character and judgement and that this independence is demonstrated in the integrity, objectivity and professionalism displayed by Mr Jemmett's contributions to Board and Audit & Compliance Committee discussions and debates. The Board acknowledges and respects that some parties may hold a different view of Mr Jemmett's independence as a consequence of his being an independent Non-Executive Director of FP.

The other Non-Executive Directors of the Company are Robert Jenkins (Chairman), Keith Bedell-Pearce, Dick de Beus, David Gray, John Heywood, Brian Larcombe, Karen McPherson and Jeff Medlock. With the exception of Jeff Medlock, who in 2004 retired as Chief Financial Officer of Eureko, a 20.6 per cent. shareholder in the Company, all of the Non-Executive Directors listed above, other than the Chairman, meet the criteria of independence as set out in the accepted guidance.

The composition of the Board is reviewed annually.

# Directors' Report on Corporate Governance

### The Board Committees

The Board has established a number of standing committees to facilitate the smooth transaction of business within the group. The terms of reference of each Board Committee outlining the authority and duties of each Committee are reviewed and approved annually by the Board and are published on the Company's website and are available on written request from the Company Secretary. The terms of reference of each of the Board Committees provide the authority to take independent professional advice, if necessary, at the Company's expense.

### (a) The Nomination Committee

### Statement of the Nomination Committee

### Purpose and Terms of Reference

The Committee leads the process, and makes recommendations to the Board, for all new Board appointments and the appointment of Non-Executive Directors to any Board Committee. It is responsible for evaluating the balance of skills, knowledge and experience on the Board and ensuring that a formal, rigorous and transparent procedure exists in the appointment process to ensure that all appointments are appropriate to the needs of the group and complement the balance of the Board.

The terms of reference of the Committee, which explain the purpose, delegated authority and duties of the Committee are published on the Company's website and can be obtained on written request from the Company Secretary.

### Membership and Attendance

The Committee is chaired by Robert Jenkins. The Committee comprises the Chairman and four Non-Executive Directors, three of whom are Independent Non-Executive Directors.

Throughout 2005 the Committee met formally on three occasions. However, none of the many meetings when the Committee, and other members of the Board interviewed or discussed prospective candidates for board membership, was regarded as a formal meeting of the Committee.

Members of the Nomination Committee: Robert Jenkins (Chairman), Dick de Beus, David Gray, Karen McPherson and Keith Satchell.

### Activities and Work of the Committee

In September 2005, Howard Carter, the Company's then Chief Executive Officer announced his intention to stand down from the Board on conclusion of the Annual General Meeting of the Company to be held on Tuesday, 16 May 2006. The Committee, following a succession planning programme commenced early in 2005 was able to, in the same announcement, confirm that Alain Grisay, the Company's then Deputy Chief Executive, would succeed Mr Carter as Chief Executive Officer with effect from 1 January 2006.

In December 2005, as part of a review of succession planning, the Committee revisited the balance and composition of the Board including the number of Directors serving thereon. After due deliberation the Committee and the Board re-affirmed the Company's commitment to striving to achieve best practice corporate governance by continuing with a Code compliant Board structure.

In January 2006, Mr Paterson Brown, the Company's Chief Financial Officer, announced his intention to stand down from the Board on conclusion of the Annual General Meeting of the Company to be held on Tuesday, 16 May 2006. The Committee, assisted by external independent search consultants, has now commenced a recruitment programme to identify a suitable candidate to succeed Mr Paterson Brown.

On an annual basis the Committee reviews the terms and conditions of appointment of Non-Executive Directors set out in the standard letter of appointment to ensure that they continue to meet the requirements of the Code. This standard letter of appointment can be inspected during normal working hours at the Company's registered office by contacting the Company Secretary. The Committee considers on an annual basis the time required of Non-Executive Directors for the fulfilment of their duties and assesses the contribution of the Directors, their independence and their suitability for re-election prior to an appropriate resolution being put to shareholders. All Directors are subject to election by shareholders at the first opportunity after their appointment and to re-election at least every three years.

For the Board
Robert Jenkins
*Chairman, Nomination Committee*
10 April 2006

# Directors' Report on **Corporate Governance**

**(b) The Audit & Compliance Committee**

**Statement of the Audit & Compliance Committee**

**Purpose and Terms of Reference**

The Committee vouchsafes the processes and controls surrounding the production of the group's financial statements and provides the Board with assurance that the processes and controls exist to facilitate reporting on the group's risk management activities, including those related to Social, Ethical and Environmental (''SEE'') matters, internal control and adherence to policies and procedures.

The terms of reference of the Committee, which explain the purpose, delegated authority and duties of the Committee are published on the Company's website and can be obtained on written request from the Company Secretary.

**Membership and Attendance**

The Committee is chaired by Christopher Jemmett. The Committee comprises solely independent Non-Executive Directors.

The Committee usually meets at least four times a year to review the integrity of the Interim Report and Financial Statements and the Annual Report and Financial Statements and other matters as set out in the terms of reference. Senior management and a representative from Friends Provident plc, given the enlarged group's governance requirements, attend as required. These meetings are also attended by senior members of the group's auditors, Ernst & Young LLP.

During the year the Committee met formally on seven occasions and informally on a number of occasions to discuss and consider business matters including the award of non-audit related consultancy work. On two occasions the Committee met members of the external auditors without management present and on two occasions the Committee met with the head of the internal Audit, Risk & Compliance department without any other members of management present.

Members of the Audit & Compliance Committee: Christopher Jemmett (Chairman), Keith Bedell-Pearce, David Gray and John Heywood. The Board is satisfied that at least one member of the Committee has recent and relevant financial experience, a position that should continue throughout 2006.

**Activities and Work of the Committee**

As highlighted earlier, the Committee normally discharges its responsibilities, as allocated by its terms of reference, within a schedule of four meetings. Two meetings are held early in the year, one to deal with matters of governance (for example, compliance with the Code, the Financial Services Act, the effectiveness of internal controls and risk management systems, monitoring and reviewing the internal Audit, Risk & Compliance department and monitoring and reviewing the independence, objectivity and effectiveness of the external audit process) and the other to consider the integrity of the year end financial statements and any formal announcements relating to the Company's financial performance including any significant financial reporting judgements contained in them. A similar process is adopted at the interim reporting stage. The Committee also considers and reviews other risk management or control documentation including the Company's policy on whistleblowing, the results of internal and external audit and compliance reports or management letters and oversees the award of any non-audit related consultancy work. On an annual basis the Committee considers and makes a recommendation to the Board as to the appointment, re-appointment or removal of the external auditors and approves their remuneration and terms of engagement. Other meetings of the Committee are called at the request of the Chairman to consider *ad hoc* control issues that may emerge during the year as well as other matters that the Board has asked the Committee to consider or investigate.

Following the acquisition in October 2004 the Committee recognised that there would be the requirement for additional meetings in 2005 to address a number of specific issues.

These included oversight of the review and subsequent negotiation of the completion accounts, the integration of the finance function including issues relating to the overseas businesses and oversight of the financial and control aspects of the integration. In addition to the merger related activities the Committee met on a number of occasions to address the half year results, the year end results and the many business and technical aspects of the introduction of International Financial Reporting Standards including in particular the subject of impairment of intangible assets as reported in the 2005 results.

For the Board
Christopher Jemmett
*Chairman, Audit & Compliance Committee*
10 April 2006

### (c) The Remuneration Committee

**Purpose and Terms of Reference**

Full details of the purpose and terms of reference, activities and work of the Committee are set out in the Directors' Remuneration Report.

**Membership**

The Committee is chaired by Karen McPherson. The Committee comprises solely independent Non-Executive Directors.

On 26 April 2005 Kenneth Inglis retired from the Board and stood down as a member of the Remuneration Committee. Brian Larcombe joined the Committee on his appointment to the Board on 24 January 2005.

Members of the Remuneration Committee: Karen McPherson (Chairman), Keith Bedell-Pearce, John Heywood, and Brian Larcombe.

**Activities and Work of the Committee**

The Committee is responsible for reviewing the group's remuneration policy (as set out in the Directors' Remuneration Report on pages 46 to 60). Within that policy, the Committee is responsible for determining the remuneration packages of the Executive Directors and making recommendations and monitoring the specific remuneration packages of senior management below Board level. It is also responsible for the Company's incentive schemes for employees, including the bonus scheme and the grant of awards under the long term incentive schemes. Further details of the objectives of the Committee are contained in the Directors' Remuneration Report on page 46.

During 2005, and early in 2006, the Committee met on a number of occasions to consider the effectiveness of the Company's long term incentive arrangements and in particular the impact that the loss of the Resolution assets would have on the retention arrangements in place within the Company. The result of the Committee's and the Board's deliberations on this matter are set out on pages 27 to 29 and in Resolutions 11 and 12 within the Notice of Annual General Meeting on page 190.

The Committee also met on a number of occasions during 2005 and early in 2006 to consider the separation terms of Messrs Carter and Paterson Brown, the details of which are set out on page 26 and in respect of Ian Paterson Brown, in Resolution 10 within the Notice of Annual General Meeting on page 190.

For the Board
Karen McPherson
*Chairman, Remuneration Committee*
10 April 2006

## Attendance at meetings

The following table identifies the number of Board and formal Committee Meetings held in 2005 and the attendance record of the individual Directors as members of committees of the Board. In addition to the meetings detailed below a number of sub-committees of F&C Asset Management plc, including a private meeting of the independent Directors, met to discharge specific items relating to the merger.

| Director | Board Meeting | Non-Executive Director meetings without management present | Remuneration Committee | Audit & Compliance Committee | Nomination Committee |
|---|---|---|---|---|---|
| Number of meetings held in 2005(2004) | 9(7) | 2(2) | 8(4) | 7(3) | 3(2) |
| Robert Jenkins | 9 | 2 | – | – | 3 |
| Christopher Jemmett | 9 | 2 | – | 7 | – |
| Howard Carter | 9 | – | – | – | – |
| Keith Bedell-Pearce | 7 | 2 | 8 | 7 | – |
| Dick de Beus | 7 | 2 | – | – | 3 |
| David Gray | 9 | 2 | – | 7 | 3 |
| Alain Grisay | 9 | – | – | – | – |
| John Heywood | 9 | 2 | 7 | 5 | – |
| Kenneth Inglis(1) | 2 | 1 | 2 | – | – |
| Brian Larcombe(2) | 9 | 2 | 6 | – | – |
| Karen McPherson | 9 | 2 | 8 | – | 3 |
| Jeff Medlock | 8 | 2 | – | – | – |
| Philip Moore(3) | 7 | 2 | – | – | – |
| Ian Paterson Brown | 7 | – | – | – | – |
| Keith Satchell | 9 | 2 | – | – | 3 |
| Brian Sweetland(4) | 1 | – | – | – | – |

(1) Resigned as a member of the Board and relevant Board Committee on 26 April 2005.
(2) Appointed as a member of the Board and relevant Board Committee on 24 January 2005.
(3) Appointed as a member of the Board and relevant Board Committee on 24 January 2005.
(4) Resigned as a member of the Board and relevant Board Committee on 24 January 2005.

## Board roles

### Chairman

The Chairman of the Company is Robert Jenkins. As Chairman, Robert Jenkins is responsible for leadership of the Board and ensuring the effective running and management of the Board. The role profile of the Chairman outlines the specific responsibilities of the Chairman including the following:

- Ensuring that the Board agenda for each meeting takes account of the issues and concerns of each Board member and that members of the Board receive accurate, timely and clear information on the Company and related matters to enable them to monitor the Company's performance and take sound decisions.
- Ensuring effective communication with shareholders and ensuring that the Board develops an understanding of the views of major investors.
- Ensuring that, in conjunction with the Company Secretary, a formal induction and development process, including any relevant internal and external training, exists for all Directors and the Board as a whole with a view to enhancing the Board's effectiveness.
- Ensuring constructive relations between Executive and Non-Executive Directors and effective contribution from all Directors.

# Directors' Report on Corporate Governance

The performance of the Chairman during 2005 was reviewed early in 2006 by the Non-Executive Directors in a meeting chaired by Christopher Jemmett, the Deputy Chairman and Senior Independent Director. The Non-Executive Directors concluded at the meeting that Robert Jenkins displayed the characteristics expected of a Chairman including being appropriately independent of the management team.

Mr Jenkins' biography is set out on page 20. Mr Jenkins has no other significant commitments.

### Chief Executive

The Chief Executive of the Company is Alain Grisay. As Chief Executive, Alain Grisay is responsible for overseeing the implementation of the strategy as set by the Board, providing strategic vision and executive leadership of the business to all the group's business activities and ensuring the effective running of the business and management of the Executive Management Committee.

### Non-Executive Directors

Messrs Bedell-Pearce, de Beus, Gray, Heywood, Jemmett, Larcombe, Medlock, Moore, Satchell and Ms McPherson are the Company's Non-Executive Directors. As Non-Executive Directors they are responsible for: promoting entrepreneurial leadership and the highest standards of governance within a framework of prudent and effective controls; constructively challenging and helping develop strategic proposals; ensuring that the Company has in place the necessary resources to meet its strategic objectives; reviewing management performance; determining appropriate levels of Executive Director Remuneration (Remuneration Committee members) and taking a prime role in appointing and where necessary removing Executive Directors; setting the Company's values and standards to ensure its obligations to its stakeholders are understood and met and reviewing communication with shareholders.

### Executive Directors and the Company's Executive Committee and Management Committee

Messrs Carter, Grisay and Paterson Brown are the Executive Directors of the Company. These Executive Directors, together with Messrs Criticos and Ribeiro form the Company's Executive Committee (EXECOM). EXECOM is accountable and responsible for implementing Board strategy, proposing development or new elements of strategy and together with the Company's Management Committee (ManCom) for the day-to-day running of the business. In addition to overseeing the implementation of the strategy, EXECOM and ManCom regularly review business issues and matters not reserved for the Board as a whole. The Committees have reserved lists to assist them in carrying out their functions. Examples of matters reserved for EXECOM and ManCom as delegated authorities from the Board are: the approval of day to day business issues linked to the strategy or the annual budget and include, the launch of new products, approval of contractual commitments, approval of expenditure, and any issue that could have a potential legal or reputational impact on the group.

### Board evaluation and professional development

An external Board evaluation process evaluating the performance of the Board and the Board Committees during 2005 is currently underway. The Board has engaged an external organisation specialising in Board recruitment and development to undertake this review. The findings of the review will be presented to the Board later in the year.

The Chairman, in consultation with the Nomination Committee, has also during the year performed an evaluation of the skills each Board member brings to the Board and created a skills matrix that was presented to the Nomination Committee and the Board for use in identifying professional development requirements and succession planning.

The Company has a full and formal induction process for all new appointments to the Board. The Chairman, in consultation with the Company Secretary and individual Directors, is responsible for assessing the professional development needs of each Director. The induction process and ongoing professional development is facilitated by the Company Secretary who, in consultation with the individual Director, identifies the most appropriate method of ensuring professional development. The Company Secretary also assists in organising attendance at internal or external courses of professional development to develop familiarity with the Company's area of business operation.

During 2005 the Board conducted site visits of the Company's locations in London, Edinburgh, The Netherlands and Portugal. These visits not only afforded an opportunity to meet with senior staff but, in the case of The Netherlands and Portugal, to be better acquainted with our local strategic partners (Achmea and Millennium BCP). The result of these visits is a better understanding by the Board of the Company's activities.

### Directors and Directors' re-election

The Directors who served at any time during the year ended 31 December 2005 are as shown in the Directors' Remuneration Report on page 54. Details of the Executive Directors' service contracts and Non-Executive Directors' letters of appointment can be found on page 53.

In September 2005, Howard Carter, an Executive Director, declared his intention to retire from the Board on conclusion of the Annual General Meeting on 16 May 2006, accordingly, Mr Carter has not been considered for re-election.

In January 2006, Ian Paterson Brown, the Company's Chief Financial Officer, declared his intention to retire from the Board on conclusion of the Annual General Meeting on 16 May 2006, accordingly, Mr Paterson Brown has not been considered for re-election.

Under the terms of the Company's Articles of Association, at least one third of Directors eligible to stand for re-election must do so at each Annual General Meeting. Accordingly Robert Jenkins, the Company's Chairman, Messrs de Beus and Bedell-Pearce, Independent Non-Executive Directors, have been selected by the Nomination Committee and the Board to join Keith Satchell, a Non-Executive Director, who retires by rotation, to offer themselves for re-election at the Annual General Meeting.

The Nomination Committee has reviewed the structure, size and composition of the Board, and confirm that all Directors offering themselves for re-election at the Annual General Meeting demonstrate commitment to their role. The Nomination Committee has also confirmed that all Directors submitting themselves for re-election devote sufficient time to perform their roles as members of the Board and any Board committee and that the Chairman and all Non-Executives display the qualities expected of a Chairman and of an effective Non-Executive Director as set out on pages 39 and 40. The Nomination Committee believes that all Directors submitting themselves for re-election should be re-elected.

Details of the Directors offering themselves for election or re-election can be found on pages 20 and 21.

### Relations with shareholders

The Board as a whole acknowledges its responsibility for ensuring satisfactory dialogue with shareholders and communications are given high priority. The Company welcomes the views of shareholders and, where practicable, enters into dialogue with institutional shareholders based on the need for mutual understanding of objectives. The Company's Chief Executive and other Executive Directors regularly meet the largest institutional shareholders and Company analysts following the announcement of the year end and interim results; the Senior Independent Director and all other Non-Executive Directors have the opportunity to attend these meetings. The Annual General Meeting of the Company provides a forum, both formal and informal, for investors to meet and discuss issues with Directors and senior management of the Company. Details of resolutions to be proposed at the Annual General Meeting on Tuesday, 16 May 2006 can be found in the notice of the meeting on pages 190 to 192.

# Directors' Report on Corporate Governance

At its Annual General Meeting, the Company complies with the provision of the Code relating to the disclosure of proxy votes, the separation of resolutions and the attendance of the Committee Chairmen. The timing of the despatch of the formal notice of the Annual General Meeting complies with the Code. The results of the votes cast at the Annual General Meeting are posted on the Company's website.

The Non-Executive Directors meet twice a year without management present. At these meetings, representatives from the Company's significant shareholders have the opportunity to express their views about the Company and consideration is given to any other relevant views expressed by other shareholders. Unattributed shareholder feedback on the Company, facilitated by the Company's brokers, is also presented to the Board following management's year end results presentations.

In addition the Company's registrar offers a Shareview service.

Information on Shareview provided by Lloyds TSB:

The Shareview service gives you more control over your shares and other investments:

- direct access to data held for you on the share register including recent share movements and dividend details;
- the ability to change your address or dividend payment instructions on-line.

It's easy to sign up for Shareview – you just need the ''shareholder reference'' printed on your proxy form or dividend stationery – and there's no charge to register.

When you register on the site, you can tell us your preferred format (post or e-mail) for shareholder communications. If you select ''e-mail'' as your mailing preference, you will be sent shareholder communications, such as proxy forms and notice of company results by e-mail instead of post, as long as this option is available. If you choose ''post'' as your preference, you will be sent paper documents as usual.

Visit the site for more details: www.shareview.co.uk. Details of software and equipment requirements are given on the website.

### Investee company corporate governance and voting policy

F&C has established a Corporate Governance Committee to address, among other things, issues and policies in respect of investee companies. The Company aims, where practicable, to implement these policies on a global basis, subject to client agreement. The policies are implemented as part of the investment discipline and are carried through into the execution of the voting policy. Corporate governance principles, which are available to investee companies, are applied in a pragmatic and sensible manner that recognises that businesses are dynamic organisations. The Company is therefore seeking to understand the ''governance culture'' rather than merely to confirm compliance with rules and regulations which in some cases may be neither applicable nor appropriate.

Details of proxy votes cast on the retail funds managed by F&C, together with the Company's corporate governance policies applied to investee companies, are published on the Company's website.

### Internal control

The Board has overall responsibility for the group's system of internal control and for reviewing its effectiveness on a regular basis. Management's role is to implement and operate the Board policies on risk and risk management. The system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material errors, losses or fraud.

The Company, as required by the FSA Listing Rules, complied with the Code provisions on internal control for the year ended 31 December 2005.

The procedures that the Directors have established are designed to provide effective control within the group and accord with the Internal Control Guidance for Directors on the Code issued by the Institute of Chartered Accountants in England and Wales ''Internal Control: Guidance for Directors on the Combined Code'' (the ''Turnbull Guidance''). Such procedures have been in place throughout the year and up to 10 April 2006, the date of approval of the Annual Report and Accounts. A high-level overview of the ongoing process for identifying, evaluating and managing significant risks including social, environmental and ethical issues is detailed below. This process is regularly reviewed by the Board to ensure it complies with the Turnbull Guidance.

**Control environment**

The group is committed to the highest standards of business conduct and seeks to maintain these standards across all areas of the business. The group has in place appropriate procedures for the reporting and resolution of activities that do not meet the required standards of business conduct.

The group has an appropriate organisational structure for planning, executing, controlling and monitoring business operations in order to achieve group objectives. The structure is designed to provide clear responsibilities and a control framework for key areas of the group's business.

Operational responsibility rests with the Chief Executive and is devolved through a documented executive structure with clearly delegated and appropriate levels of authority. Members of group management are, therefore, accountable for the operation of the systems of internal controls within the group's business.

**Business risks**

The identification of major business risks is carried out by the Board in conjunction with management, and procedures to control these risks, where possible, are reviewed and agreed.

Quarterly reports are prepared by each of the business units, across all locations including the group's overseas locations in The Netherlands, Portugal, Germany, Ireland, France and the U.S.A. The quarterly reports include issues of material business risk. These reports are discussed in detail by the Management Committee that includes all Executive Directors. All significant items are identified and reported to the Board on a regular basis.

In addition to the ''normal risks'' facing the business relating to the market, clients, personnel and regulation, following the merger, the loss of the Resolution plc contract and the decision to withdraw from the outsourcing negotiations with Mellon, the group faces a number of short-term operational risks. The Board through its risk management reporting processes, has identified these risks and in all cases has assigned appropriate members of management to ensure adequate processes and controls exist to manage these risks. The key risks facing the group at the year end and the mitigating actions assigned to these risks are detailed below.

Risk: ''Risk of poor investment performance, leading to the loss of key investment mandates.''

Mitigation: ''The selection processes during the integration of F&C and ISIS and other actions taken during 2005 and early in 2006 have helped the Company strengthen the investment teams. While investment performance has stabilised or improved in a number of key areas during 2005, there are some product areas to which management are devoting further attention.''

Risk: ''Impact of EU and other regulatory developments.''

Mitigation: ''The Markets in Financial Instruments Directive and Capital Requirements Directive present medium term challenges for asset management businesses. Programmes are in hand to prepare for implementation and opportunities are taken as they arise to influence the drafting and implementation of the Directives.''

# Directors’ Report on Corporate Governance

Risk: ‘‘Risks during integration of administration system operational platforms.’’

Mitigation: ‘‘Subsequent to the Company’s announcement in 2005 to terminate its outsourcing negotiations with Mellon, administrative operations continue on two legacy platforms, one outsourced and one in-house. A project is under way to build a data warehouse to consolidate data, enhance operational efficiencies and improve the level of servicing and reporting to clients and management.’’

Risk: ‘‘Risks during integration of front office control processes.’’

Mitigation: ‘‘New IT systems are being developed and installed to complete the integration of front office dealing, decision support and pre and post execution monitoring systems. Substantial progress has been made with the installation of a new dealing platform and further supporting systems are anticipated to follow during 2006. In the short term adequate controls, albeit more manual in nature, exist to manage the risk’’.

Risk: ‘‘Depth and timeliness of management information’’

Mitigation: ‘‘While the Board has been provided with high level management information during the year, due to the extent of the merger activity and the significant integration to systems and business processes, management information at a level of detail that the Board might reasonably expect was not readily available. Management have put in place processes and procedures that will in the future enhance the reporting of management information to the Board and the business’’.

### Monitoring and corrective action

There is a formal compliance function, which is integrated with the internal audit function and operational risk function, to form an Audit, Risk & Compliance department. The Audit, Risk & Compliance department conducts regular monitoring of various business areas and control procedures in line with a plan agreed annually with the Audit & Compliance Committee. The Audit & Compliance Committee and members of the Management Committee receive a formal monthly report from the Audit, Risk & Compliance department providing an update of the monitoring activity and other relevant regulatory or control matters. Any issues of significance are brought to the attention of the Board by the Audit, Risk & Compliance department and through the regular reporting process. Planned corrective actions are independently monitored for timely completion and reviewed by the Audit & Compliance Committee.

The Audit & Compliance Committee reviews the effectiveness of the operation of this framework at least twice each year.

### Independence of the auditors

The Board has in place rigorous systems for ensuring the independence, objectivity and effectiveness of the group’s auditors and has satisfied itself that during the year no aspect of their work was impaired on these grounds. In maintaining a clear perception of independence and balancing that with the best interests of the Company, the Board has a clear policy that it follows when considering awarding non-audit work to the group’s auditors. The policy applied during 2005 is detailed below.

The Company does not impose an automatic ban on the group’s auditors undertaking non-audit work. The group’s aim is always to have any non-audit work involving accountancy firms carried out in a manner that affords value for money while taking into account relevant ethical guidance. The firm must not be in a position of conflict in respect of the work in question and must have the skill, competence and integrity to carry out the work in the best interests of the group.

Any award of work to the auditors, irrespective of value, requires the prior approval of the Audit & Compliance Committee. The Committee, in addition to considering the costs of any award, considers whether the work is:

- so closely related to the statutory audit – for example, related assurance work, which would include FRAG 21 work, regulatory reports and tax compliance work; or
- such that a detailed understanding of the group is necessary – for example, due diligence and tax advisory work and preparatory work for a shareholder circular;
- that, in the absence of any conflict of interest, it is considered in the best interests of the group to have the work carried out by the auditors.

It is also recognised that audit firms have an internal control process that aims to eliminate conflict and ensure independence and objectivity in dealing with clients. The auditors are specifically excluded from undertaking any assignment or work that would involve them in either auditing or reviewing their own work or in providing services that would require them to function as part of the management of the business.

The award of any other type of non-audit work will be the subject of a short list of appropriate providers if in excess of £30,000 and the subject of a formal tender process wherever appropriate. Irrespective of the value of the contract, such work will always be awarded to the firm which has the necessary skill, competence and integrity and offers the best value for money in the best interests of the group.

The performance, independence, competence and cost of auditors are reviewed annually by the Audit & Compliance Committee. When the Committee considers it appropriate, the provision of audit services will be formally market-tested through a tender process involving those audit firms judged competent to meet the needs of the group. The frequency of this market-testing will depend on the views of the Audit & Compliance Committee, on the needs of the group and prevailing leading practice.

During the year, Deloitte & Touche, KPMG, and PricewaterhouseCoopers, who are independent of the external auditors, provided non-audit related services to the group. Details of fees paid to accounting firms during 2005 are disclosed in note 4 on pages 82 and 83 of the notes to the financial statements.

**Future developments**

The Board believes that the controls in place during 2005 have been appropriate to the needs of the group. Nevertheless, it is committed to the highest standards of governance and business conduct and will ensure that those controls continue to develop in line with the requirements of the Financial Services Authority (''FSA'') and leading practice.

By order of the Board

W Marrack Tonkin, FCCA
*Secretary*

80 George Street
Edinburgh EH2 3BU
10 April 2006

# Directors' Remuneration Report

In designing the total compensation arrangements for the Company and in preparing this report, the Board and the Remuneration Committee have complied with the provisions of the Combined Code issued by the Financial Reporting Council in July 2003 (''the Code''), Schedule 7A to the Companies Act 1985 and the FSA Listing Rules. An ordinary resolution for the approval of this report will be put to shareholders at the forthcoming Annual General Meeting.

Legislation requires the group's auditors to audit certain disclosures within this report. Where disclosures have been audited they are indicated as such.

The following policies represent the policies now adopted by F&C Asset Management plc for the forthcoming year and subsequent financial years, together with, where appropriate, details of transitional arrangements applied in relation to the year ended 31 December 2005.

### Introduction and objectives

The Remuneration Committee is a Standing Committee of the Board, chaired by Karen McPherson, an independent Non-Executive Director. Its other members are Keith Bedell-Pearce, John Heywood and Brian Larcombe, all of whom are independent Non-Executive Directors. Kenneth Inglis served as a member of the Committee until his retirement from the Board on 26 April 2005.

The Committee, which has detailed written terms of reference that are reviewed annually and published on the Company's website and are available on request from the Company Secretary, has been established by the Board to:

(a) recommend to the Board the Company's policy on Directors' remuneration;

(b) ensure that the Company's Executive Directors and senior employees are fairly rewarded and that a significant proportion of Executive Directors' remuneration is linked to the group's corporate, and their individual, performance;

(c) demonstrate to shareholders that the remuneration of Executive Directors and senior employees of the Company is determined by a Committee of Board members who have no personal interest in the level of remuneration of the Company's Executive Directors or senior employees and who will pay due regard to the interests of shareholders and to the financial and commercial health of the Company; and

(d) ensure that full consideration has been given to Section B and Schedule A of the Code's best practice provisions as annexed to the Listing Rules.

### Advice

During the year the Remuneration Committee sought and received independent remuneration research undertaken by Mclagan & Partners, Towers Perrin, DLAMCG Consulting, Deloitte & Touche and Mercer Human Resource Consulting, leading firms of executive remuneration consultants appointed by the Committee to assess comparability of the Company's remuneration policies to the marketplace and in particular the remuneration policies of the Company's competitors. The Committee approves all work undertaken by these specialist consultants and the Board is satisfied that its advisers in respect of remuneration matters are independent.

During 2005 the Remuneration Committee also received advice from PricewaterhouseCoopers (''PwC'') relating to the application of the rules and the operation of the Company's long term incentive plans.

**Statement of the Company's policy on Directors' remuneration**

Statement of the Company's policy on Directors' remuneration

The Company's compensation policy detailed below is based upon the following key principles:

- a single compensation policy applying across the business;
- a focus on market competitive total compensation;
- differentiation by merit and performance;
- an emphasis on variable, performance-driven remuneration;
- alignment with shareholders' interests through equity ownership; and
- clarity, transparency, and fairness of process.

A total compensation approach is central to the operation of the Company's compensation philosophy, with a strong focus on variable compensation. The Board believes that shareholders interests are best served by containing fixed costs and increasing the proportion of total compensation that is directly performance related and thus aligned with shareholders interests. Total remuneration will comprise basic salary, pension provision, annual bonus, any awards under the long term share incentive schemes and all employee share plans.

The total cash component of compensation will be benchmarked to market median for solid performers and to upper quartile for industry leaders. A range of benchmark data is used, based on comparable asset management businesses, with appropriate data being used for each geographic location.

**Policies on the individual elements of remuneration and employment:**

*(a) Salaries*

The salaries of all employees, including Executive Directors, are reviewed annually and are determined by reference to external market research. The Company has an active policy of reducing the emphasis on base salary.

*(b) Bonus*

The size and distribution of the bonus pool is recommended by the Remuneration Committee to the Board for consideration and approval. In considering the size and in determining the distribution of the bonus pool, the Committee considers the performance of the business, the need to recruit, motivate and retain high-calibre individuals, the arrangements operated by the Company's competitors and the need to maintain an appropriate balance between salary and performance-related remuneration that ensures the achievement of objectives is rewarded. The Board has previously declared their aim to determine the size of the bonus pool as a fixed percentage of profits, believing that this provides greater transparency and certainty to both the shareholder and employee, and helps to ensure that bonuses are affordable and linked to the financial performance of the group. The Board intends to apply a fixed percentage range of the underlying earnings to the bonus pool in 2006 and beyond.

Bonus awards to all staff, including the Executive Directors are made under the discretionary bonus scheme. The purpose of this scheme is to reward all staff and the Executive Directors for superior performance relative to agreed targets.

On 4 October 2004 shareholders approved the adoption of a Purchased Equity Plan. The Purchased Equity Plan operates in conjunction with the discretionary bonus scheme and is intended to encourage shareholding by management and employees of the group by providing for:

- The compulsory purchase of shares using annual bonus above a threshold level; and
- Voluntary purchase of shares using annual bonus, with associated matching shares.

# Directors' Remuneration Report

On 24 January 2006 the Board, following consultation with the Company's Remuneration Committee's advisors, approved an amendment to the rules of the Purchased Equity Plan which resulted in an adjustment to the terms of the compulsory purchase element of the plan. The change to the compulsory purchase element of the plan is detailed below. The voluntary purchased element of the plan, being the element of the plan with potential for additional matching shares has not been amended.

Under the terms of the Purchased Equity Plan, participation can arise in two ways:

- On an annual basis eligible employees who are awarded in a financial year an aggregate bonus in excess of a threshold level of £75,000 will be required to defer one third of the element exceeding £75,000 (prior to 24 January 2006 – one third of the aggregate bonus) into shares (''Compulsory Purchased Equity'') for three years; and
- As and when determined by the Board, eligible employees may be invited to elect to defer into shares any remaining proportion of their gross cash bonus not subject to deferral on a compulsory basis for three years (subject to a minimum deferral of £1,500) (''Voluntary Purchased Equity'').

To encourage participants to defer their bonus on a voluntary basis, a matching award will be made for Voluntary Purchased Equity. The matching award will provide, at most, one share for each two shares received as Voluntary Purchased Equity. Vesting of any matching award is dependent on the satisfaction of performance conditions and continued service. The conditions will relate to real earnings per share growth measured over a three year period as set out below.

| Growth in the group's earnings per share* over three year performance period | Matching Purchased Equity award for each Voluntary Purchased Equity share purchased |
|---|---|
| Below PI + 9% | 1 for 5 |
| PI + 9% | 1 for 5 |
| PI + 24% or higher | 1 for 2 |

* Earnings per share (EPS) is calculated by reference to underlying earnings of the group and will exclude amortisation and impairment of intangible assets, restructuring costs, and the cost of the Re-Investment Plan.

(where PI stands for an appropriate index of price inflation – the Retail Price Index (RPI))

For levels of EPS performance between those shown in the table, the Matching Purchased Equity award will vary on a straight line basis between the minimum and maximum levels shown.

The Compulsory Purchased Equity will not benefit from any form of matching award and is subject to forfeiture in the event that the employee leaves the group for any reason (other than as a ''good leaver'') in the three year retention period.

In the year ended 31 December 2005, the Compulsory Purchased Equity element of the Purchased Equity Plan was applied to 30 employees previously employed by F&CGH prior to the merger (given that similar arrangements previously existed) in relation to any bonus awards payable in respect of their performance in 2004. 750,091 shares were acquired under the Compulsory Purchased Equity element of the Purchased Equity Plan and 35,688 shares were forfeited during the year. All eligible employees will participate in Compulsory Purchased Equity in relation to the 2005 bonus year.

Invitations to participate in the Voluntary Purchased Equity element of the plan are at the discretion of the Board and will only be offered when the Board considers it appropriate to do so.

*(c) Savings-related share schemes*

To foster a culture of share ownership throughout the group, the Board operates a Share Save Scheme and Share Incentive Plan for all eligible employees. Both schemes are "all employee share schemes" and all employees including Executive Directors who meet certain criteria are eligible to participate. Invitations to all employees eligible to participate in these schemes are issued following the announcement of the year end results in March. Details of all "options" held by Directors under the Share Save Scheme are contained on page 58.

At 31 December 2005, 327 employees participated in the Share Save Scheme and 548 employees participated in the Share Incentive Plan.

Shares under option within the Share Save Scheme are detailed below:

| Number of Options | Term (Years) | Exercise Price |
|---|---|---|
| **March 2003 Participation** | | |
| 245,403 | 3 | 114 pence |
| 335,708 | 5 | 114 pence |
| **March 2004 Participation** | | |
| 204,520 | 3 | 181 pence |
| 139,044 | 5 | 181 pence |
| **March 2005 Participation** | | |
| 306,046 | 3 | 186.6 pence |
| 167,704 | 5 | 186.6 pence |

165,391 shares (2004 – 65,763 shares) were held in trust for employees within the Share Incentive Plan. Both "all employee share schemes" seek to buy shares in the market to remove any possible impact of dilution.

*(d) Share incentive schemes*

The Board believes that the share incentive schemes increase the potential for greater importance to be placed upon the performance related element of total remuneration.

In any 10 year period the aggregate number of ordinary shares which will be placed under award under any share incentive scheme, shall not, when aggregated with the number of ordinary shares placed under option or issued in that period under any other employees' share scheme operated by the Company, exceed 10 per cent. of the Company's issued ordinary share capital at that time. For the purposes of measurement against this limit the following will be disregarded: any ordinary shares that have been, or will be purchased, rather than allotted; and any awards or grants that have lapsed or become incapable of vesting.

In order to ensure that the assessment of performance conditions in relation to the share incentive schemes detailed on pages 56 to 60 is independent, PricewaterhouseCoopers LLP will report to the Remuneration Committee as to whether the performance criteria under all schemes have been met.

Proposed changes to the performance conditions relating to the Companies share incentive schemes are set out on pages 27 to 29.

*The F&C Asset Management plc Long Term Remuneration Plan (LTRP)*

The LTRP is the primary long term incentive arrangement of F&C Asset Management plc.

Proposed amendments to the Company's LTRP are set out on pages 28 and 29 and contained within resolution 12 of the Notice of Annual General Meeting on page 190.

The LTRP is a discretionary contingent share award scheme unapproved by the Inland Revenue. The LTRP is designed to support the business objectives of the group. Under the LTRP, contingent awards of shares are made, usually annually, and will vest after three years subject to the achievement of performance conditions and conditions of continued service.

Vesting of the ordinary shares that are currently the subject of an award under the LTRP will be dependent upon the specified performance conditions and conditions of continued service. The performance conditions applied to the LTRP are determined by the Board and are measured over a three year period. For existing awards under the LTRP, 50 per cent. of any award relates to total shareholder return ("TSR") and 50 per cent. of the award relates to real earnings per share growth as set out below.

| **TSR target (applying to 50 per cent. of any award)**<br>**The group's TSR relative to FTSE 250** | **% of Award Vesting** |
|---|---|
| Below Median | Nil |
| Median | 35 |
| Upper Quartile | 100 |

| **EPS target (applying to 50 per cent. of any award)**<br>**Growth in group's EPS over three year performance period** | **% of Award Vesting** |
|---|---|
| Below PI + 9% | Nil |
| PI + 9% | 50 |
| PI + 24% or higher | 100 |

(Where PI stands for an appropriate index of price inflation – the Retail Price Index (RPI))

The TSR target is dependent upon the TSR of the Company compared to the TSR of the other companies who formed the FTSE 250 Index at the start of each performance period (the "comparator companies") over a three year performance period commencing on the first day of the accounting period in which the award was made. In order to determine how much of an award will vest, the Remuneration Committee compares the TSR of the Company with that of the companies that constituted the FTSE 250 Index published by the London Stock Exchange plc immediately before the date of the award. At the end of the performance period, the Company and each of the comparator companies (the "comparator list") are listed and ranked in accordance with their TSR over the performance period. The number of ordinary shares which vest would depend upon the ranking of the Company in the comparator list in accordance with the vesting table above, described as follows. For below median TSR performance no awards would vest; for TSR performance between the median and upper quartile (125th and 63rd position in the index) awards would vest on a straight-line basis between 35 per cent. for median and 100 per cent. for upper quartile. The TSR measure reflects the movement in the value of shares plus any dividends declared during the relevant period. It was therefore, chosen as the performance measure for the LTRP as it is directly related to movements in shareholder value.

For levels of both TSR and EPS performance between those shown in the tables above, any award that vests under the LTRP will vary on a straight line basis between the minimum and maximum levels shown.

During the year no awards were made under the LTRP (2004 – 6,375,904 LTRP awards were made to 215 staff).

During 2005 the growth in the Company's EPS exceeded the growth in the RPI by 22.2 percentage points (2004 – 13.2 percentage points). The Company's TSR ranked 180th out of a FTSE 250 Index comparator group of 199 companies* in the period from 2 July 2004 (the date of the announcement of the proposed merger, the suspension date of ISIS Asset Management plc shares, and the date determined by the Board as the TSR performance period start date for awards made under the LTRP in November 2004) to 31 December 2005.



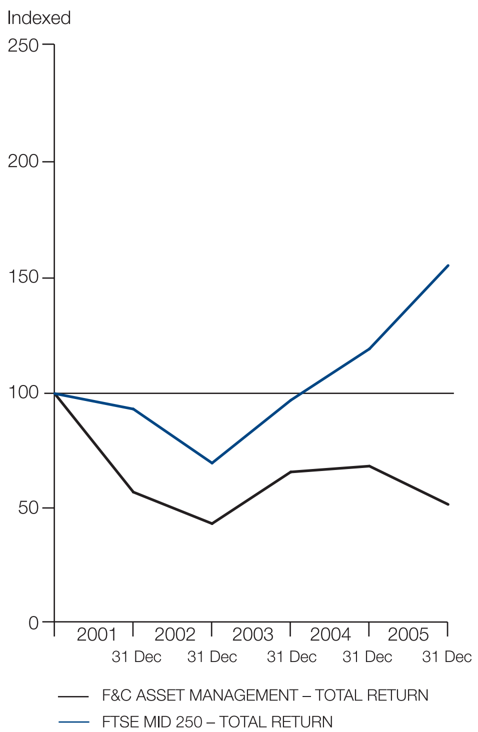
* In line with the definition of the performance condition, the constituent companies of the FTSE 250 Index were taken as at 2 July 2004 and 31 December 2005. Only companies appearing in the index on both dates are included for the purposes of the analysis.

*Policy on grants and awards under the share incentive schemes*

The Company's policy for the granting of awards under the LTRP is that awards and grants are based on an assessment of individual contribution to the business and independent advice obtained on current remuneration practices. Each year the Remuneration Committee will recommend to the Board the individuals to whom LTRPs should be awarded. Award levels will be determined by the Remuneration Committee with reference to Company performance, market competitiveness (assessed on a total compensation basis using independent market total compensation data), and individual performance. Because of the active policy of reducing the emphasis on base salary, the Company will not link or limit any awards under the LTRP explicitly to a multiple of base salary, believing that making such a linkage provides an incentive to increase base salaries, and therefore fixed costs, which is contrary to shareholders' interests.

**Performance Graph for the Share Incentive Schemes**

The graph below compares the performance of the Company for the five financial periods ending 31 December 2005 based on the TSR for each period (assuming all dividends are reinvested) to ordinary shareholders compared with the TSR for each period on a notional investment made up of shares of the group of companies from which the FTSE 250 Index of companies is calculated. The FTSE 250 Index has been chosen as the comparator index as it is the index that includes the Company and is considered an appropriate benchmark as there are very few comparable listed asset management businesses. It is therefore the group against which 50 per cent. of the LTRP is measured.




Source: Datastream

*(e) Policy on other benefits*

The Company provides all staff with life assurance cover. The Company's policy in relation to cars is to provide cars only to employees where the use of a car is essential to the fulfilment of their role and to provide a car cash allowance in all other instances. During 2003, the Board resolved, in a three stage process, to consolidate car allowance payments into base salary.

*(f) Policy on pension*

The Company's policy on pension provision is to provide a means whereby each employee either receives a pension at retirement age or funding to operate a money purchase pension plan. New UK employees are provided with funding to enable them to operate a money purchase pension plan. The funding rate varies according to the age of the employee.

Pension payments are based on basic salary and no other cash payments or benefits are pensionable.

*(g) Policy on contracts of employment*

The Company's policy regarding contracts of employment is that all senior employees, including Executive Directors, should be offered rolling contracts of no longer than twelve months. Where it is commercially appropriate to protect the Company, a longer-term initial contract with any employee, including an Executive Director may be entered into. On completion of the initial contract, the Company's standard terms will be applied. The Remuneration Committee, in considering contracts, has regard to compensation commitments in respect of termination and believes that these are best addressed by restricting the term of the contract. In the event of a termination, the Remuneration Committee would consider all the relevant factors and seek a just solution.

*(h) Policy on Non-Executive Directors' remuneration*

Non-Executive Directors' fees for the year to 31 December 2005 are set out on page 54. None of the Non-Executive Directors have service contracts. Letters of appointment provide for an initial period of three years, subject to review. Non-Executive Directors must submit to re-election at least every three years and are not eligible for bonuses or participation in savings related share schemes or share incentive schemes. Non-Executive Directors are not eligible to join any of the Company's pension schemes. No pension contributions are made on their behalf and no Non-Executive Director receives a salary from the Company. The remuneration of Non-Executive Directors is determined by the Board as a whole within the limits stipulated in the Company's Articles of Association.

Apart from the Chairman and Deputy Chairman, Non-Executive Directors are paid a basic fee, currently £30,000 per annum for their role on the Board and are separately remunerated for services on Board Committees. All fees are reviewed annually. Fees were reviewed following the merger and the current fees became effective 1 January 2005. The Chairman and Deputy Chairman of the Board, who chair the Nomination Committee and Audit & Compliance Committee respectively, receive an annual all inclusive fee only, currently £100,000 and £55,000 respectively. The Remuneration Committee sets the Chairman's annual remuneration. The Board as a whole determine the fees for Non-Executive Directors. Members and Chairmen of Board Committees are currently remunerated as follows:

| Committee | Member's Fee (£) | Chairman's Fee (payable in addition to the member's fee) (£) |
|---|---|---|
| Audit & Compliance | 10,000 | 5,000* |
| Remuneration | 7,500 | 5,000 |
| Nomination | 5,000 | 5,000* |

* Currently included within the all inclusive fees payable to Robert Jenkins and Christopher Jemmett.

### Statement on Executive Directors' service contracts and Non-Executive Directors' letters of appointment

Messrs Carter, Grisay and Paterson Brown have current service contracts with the Company that are for a rolling period of one year, details of which are summarised below.

| Executive Directors | Date of Contract | Notice Period | Unexpired term | Provision for compensation payable by the Company on early termination £000 |
|---|---|---|---|---|
| Howard Carter | 1 Oct 2000 | Twelve months | rolling twelve months | 366[1] |
| Alain Grisay | 11 Oct 2004 | Twelve months | rolling twelve months | 332 |
| Ian Paterson Brown | 1 Feb 1995 | Twelve months | rolling twelve months | 171[2] |

1. Mr Carter will retire from the Board and leave the Company on contractual terms on conclusion of the Annual General Meeting on 16 May 2006.
2. Mr Paterson Brown will retire from the Board and leave the Company on conclusion of the Annual General Meeting on 16 May 2006.

| Chairman and Non-Executive Directors | Date of Contract | Notice Period | Unexpired term at 31 March 2006 | Provision for compensation payable by the Company on early termination £000 |
|---|---|---|---|---|
| Robert Jenkins | 26 Apr 2005 | None | Twenty five months | Nil |
| Keith Bedell-Pearce | 26 Apr 2005 | None | Twenty five months | Nil |
| Dick de-Beus | 26 Apr 2005 | None | Twenty five months | Nil |
| David Gray | 30 Apr 2004 | None | Thirteen months | Nil |
| John Heywood | 26 Apr 2005 | None | Twenty five months | Nil |
| Kenneth Inglis (retired on 26 April 2005) | 30 Apr 2004 | None | N/A | Nil |
| Christopher Jemmett | 30 Apr 2004 | None | Thirteen months | Nil |
| Brian Larcombe | 26 Apr 2005 | None | Twenty five months | Nil |
| Karen McPherson | 26 Apr 2005 | None | Twenty five months | Nil |
| Jeff Medlock | 26 Apr 2005 | None | Twenty five months | Nil |
| Philip Moore | 24 Jan 2005 | None | Twenty five months | Nil |
| Keith Satchell | 25 Apr 2003 | None | One month | Nil |
| Brian Sweetland (retired on 24 January 2005) | 30 Apr 2004 | None | N/A | Nil |

No employee of the group has a service contract that cannot be brought to an end within one year.

### Directors retiring and seeking election/re-election

The names of those Directors proposed for re-election are contained in the Directors' Report on Corporate Governance on page 41.

# Directors' Remuneration Report

## Statement on Directors' remuneration (audited)

The remuneration of the Chairman and the other Directors who held office during the year ended 31 December 2005 is set out below:

| | Salary and fees 2005 £000 | Bonus 2005 £000 | Benefits and allowances 2005 £000 | Compen-sation for loss of office £000 | Total 2005 (excluding pension contribution) £000 | Total 2004 (excluding pension contribution) £000 | Pension Contributions 2005 £000 | Total 2005 £000 | Total 2004 £000 |
|---|---|---|---|---|---|---|---|---|---|
| Executive Directors | | | | | | | | | |
| Howard Carter* | **286** | **825** | **6** | **768†** | **1,885** | 1,240 | **73** | **1,958** | 1,315 |
| Alain Grisay(1)** | **166** | **925** | **5** | **–** | **1,096** | 172 | **18** | **1,114** | 172 |
| Ian Paterson Brown | **170** | **375** | **2** | **1,227#** | **1,774** | 594 | **–** | **1,774** | 594 |
| Chairman and Non-Executive Directors | | | | | | | | | |
| Robert Jenkins (Chairman)(1) | **100** | **–** | **2** | **–** | **102** | 23 | **–** | **102** | 23 |
| Christopher Jemmett | **55** | **–** | **–** | **–** | **55** | 32 | **–** | **55** | 32 |
| Dick de Beus(1) | **35** | **–** | **–** | **–** | **35** | 6 | **–** | **35** | 6 |
| Keith Bedell-Pearce | **48** | **–** | **–** | **–** | **48** | 30 | **–** | **48** | 30 |
| David Gray‡ | **65** | **–** | **–** | **–** | **65** | 31 | **–** | **65** | 31 |
| John Heywood(1) | **48** | **–** | **–** | **–** | **48** | 8 | **–** | **48** | 8 |
| Kenneth Inglis(2) | **12** | **–** | **–** | **–** | **12** | 30 | **–** | **12** | 30 |
| Brian Larcombe(3) | **35** | **–** | **–** | **–** | **35** | – | **–** | **35** | – |
| Philip Moore(3) | **–** | **–** | **–** | **–** | **–** | – | **–** | **–** | – |
| Karen McPherson(1) | **48** | **–** | **–** | **–** | **48** | 7 | **–** | **48** | 7 |
| Jeff Medlock(1) | **30** | **–** | **–** | **–** | **30** | 6 | **–** | **30** | 6 |
| Keith Satchell | **–** | **–** | **–** | **–** | **–** | 26 | **–** | **–** | 26 |
| Brian Sweetland(4) | **–** | **–** | **–** | **–** | **–** | 26 | **–** | **–** | 26 |
| Total | **1,098** | **2,125** | **15** | **1,995** | **5,233** | 2,231 | **91** | **5,324** | 2,306 |

* Howard Carter's pension contributions represent a contribution to a Funded Unapproved Retirement Benefit Scheme in relation to the element of his salary above the earnings cap. Howard Carter is a member of the ISIS Asset Management plc Pension Fund set out on page 55 which provides pension benefits on his salary below the earning cap.

† Includes a cash contribution of £121,000 that will be made to Mr Carter on his retirement in May 2006 in lieu of an intended award under the Company's Long Term Remuneration Plan that could not be made during the year due to the Company being in a restricted period.

** In addition, Alain Grisay received £425,000 deferred for three years in Compulsory Purchased Equity under the terms of the Purchased Equity Plan details of which are shown on pages 47 and 48.

\# Includes a proposed augmentation of £514,000 to Mr Paterson Brown's pension arrangements.

‡ During the year Mr Gray received a one-off fee of £20,000 in connection with work performed on a project requested by the Audit & Compliance Committee into the reasons behind the delay in the Company's announcement of the 2004 year end results.

(1) Appointed a Director on 11 October 2004.

(2) Resigned as a Director on 26 April 2005.

(3) Appointed a Director on 24 January 2005.

(4) Resigned as a Director on 24 January 2005.

No sums were paid to third parties in respect of any Executive Director's services.

The Company received £Nil (2004 – £Nil) in fees payable to Executive Directors in respect of any external directorships held. No Executive Director receives any fees in respect of external appointments.

The Non-Executive Directors' fees of Philip Moore, Keith Satchell and Brian Sweetland (up to his resignation), which would have been payable to Friends Provident plc, were waived in 2005 by Friends Provident in lieu of the services provided by Howard Carter to their Board in his capacity as Director of Friends Provident, for which no fee is payable by them to F&C.

# Directors' Remuneration Report

### Statement on Directors' pensions (audited)

The number of Directors who held office during the year and to whom retirement benefits are accruing is set out below:

| | 2005 Number | 2004 Number |
|---|---|---|
| Members of money purchase pension scheme | **1** | 5 |
| Members of defined benefit scheme | **2** | 2 |

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Company contributions paid to money purchase pension schemes | | |
| – Alain Grisay (from appointment on 11 October 2004) | **275*** | Nil |

* Represents a cash contribution made to Mr Grisay's pension fund in lieu of an intended award under the Company's Long Term Remuneration Plan that could not be made during the year due to the Company being in a restricted period. In January 2006 a contribution of £2,000,000, equivalent to £666,666 per annum for three years, was made into Mr Grisay's pension fund. This payment represents the Company's commitment to Mr Grisay on assuming the role of Chief Executive to provide him with an appropriate pension at age 60. This commitment is contingent on Mr Grisay serving as Chief Executive for a minimum of three years and not resigning or being dismissed for cause during this three year period.

During the year, the Company paid a widow's pension of £85,000 (2004 – £82,000) in respect of the pension benefits which had accrued to a former chairman.

The pension entitlements of the Directors who are members of ISIS Asset Management plc Pension Fund as detailed in note 26, are set out below.

The following Directors were members of defined benefit schemes provided by the Company during the year. Pension entitlements and corresponding transfer values increased as follows during the year.

| | (1) Gross increase in accrued pension | (2) Increase in accrued pension net of inflation | (3) Total accrued pension at 31/12/2005 | (4) Transfer value of net increase in accrual over period | (5) Total change in value during period | (6) Value of accrued pension at 31/12/2005 | (7) Value of accrued pension at 31/12/2004 |
|---|---|---|---|---|---|---|---|
| Howard Carter | £2,300 | £1,900 | **£16,400** | £25,300 | £54,600 | **£248,400** | £190,600 |
| Ian Paterson Brown | £3,100 | £1,100 | **£76,500** | £18,400 | £1,069,400 | **£2,014,000** | £937,400 |

Notes

(a) Pension accruals shown are the amounts which would be paid annually on retirement at normal pension age based on service to the end of the year.

(b) Transfer values have been calculated in accordance with version 9.2 of guidance note GN11 issued by the actuarial profession.

(c) The value of net increase (4) represents the incremental value to the Director of his service during the year, calculated on the assumption service terminated at the year-end. It is based on the accrued pension increase (2) and is net of Director contributions for the period and therefore represents the notional Company "cost".

(d) The change in transfer value (5) includes the effect of fluctuations in the transfer value due to factors beyond the control of the Company and Directors, such as stockmarket movements. These factors can influence the transfer value quoted significantly. The resulting disclosed change in value may therefore be subject to a large degree of volatility and could even be negative. It is calculated net of Director contributions.

(e) Voluntary contributions paid by Directors and resulting benefits are not shown.

(f) Pensionable Salary for I Paterson Brown is not subject to the Earnings Cap. Pensionable Salary for H Carter is subject to the Earnings Cap.

(g) The value of accrued pension at 31/12/2005 (6) for I Paterson Brown has been calculated assuming an unreduced pension is payable from 1 June 2006. The value in (6) does not represent the actual transfer value available to I Paterson Brown from the ISIS Asset Management plc Pension Fund were he to transfer his benefits to another arrangement.

# Directors' Remuneration Report

Mr Jenkins has an entitlement from F&C to an unfunded pension benefit of £100,000 per annum from age 60, index linked with attaching spouse's benefits.

| | (1) Gross increase in accrued pension | (2) Increase in accrued pension net of inflation | (3) Total accrued pension at 31/12/2005 | (4) Transfer value of net increase in accrual over period | (5) Total change in value during period | (6) Value of accrued pension at 31/12/2005 | (7) Value of accrued pension at 31/12/2004 |
|---|---|---|---|---|---|---|---|
| Robert Jenkins | £2,700 | £0 | **£102,700** | £0 | £264,000 | **£1,794,000** | £1,530,000 |

Notes

(a) Pension accruals shown are the amounts which would be paid annually on retirement at age 60. The pension will be indexed before and after retirement in line with the Retail Prices Index on 1 January each year.

(b) Mr Jenkins became entitled to the benefit on 11 October 2004 following the completion of the deal to form F&C Asset Management plc.

(c) Transfer values have been calculated in accordance with version 9.2 of guidance note GN11 issued by the actuarial profession.

(d) The transfer values represent the actuarial value of a liability to the Company, and are not a sum paid to Mr Jenkins.

### Statement on Directors' share incentive schemes (audited)

The Executive Directors who held office during the year and their awards under any of the group's share incentive schemes at 31 December 2005 are shown below.

Non-Executive Directors do not participate in any of the group's long term incentive plans.

## Long Term Remuneration Plan awards

Details of the Long Term Remuneration Plan are set out on pages 49 and 50. Proposed changes to the Long Term Remuneration Plan are set out on pages 28 and 29.

During the year no awards were made to Executive Directors under the Long Term Remuneration Plan, no awards were exercised by Executive Directors and no awards held by Executive Directors lapsed.

| Date of Grant | Howard Carter | Alain Grisay | Ian Paterson Brown | Share price on award date |
|---|---|---|---|---|
| 2005 | | | | |
| No awards made | – | – | – | N/A |
| 2004 | | | | |
| 15 November | 416,667 | 208,333 | 143,750 | 240.25p |

| | 31 December 2005 | 31 December 2004 |
|---|---|---|
| Howard Carter | **416,667** | 416,667 |
| Alain Grisay | **208,333** | 208,333 |
| Ian Paterson Brown | **143,750** | 143,750 |

## Re-Investment Plan

The Re-Investment Plan was a plan established to allow employees previously employed by F&CGH prior to the merger to voluntarily re-invest one half of their entitlement under the Shadow Equity Plan into ordinary shares in F&C Asset Management plc or rights to receive ordinary shares in F&C Asset Management plc. The purpose of the Re-Investment Plan, which was a one off plan linked to the merger, was to encourage key former F&CGH individuals to re-invest one half of the proceeds of their vested Shadow Equity Plan entitlement into ''Investment shares'' which will be forfeitable for a period of up to 2 years should the participant voluntarily resign or be dismissed for gross misconduct within 24 months of completion of the merger on 11 October 2004.

**Forfeiture table in relation to ''Investment Shares''.**

| Time between 11 October 2004 and Voluntary resignation or Dismissal | Percentage of shares held in the Re-Investment Plan forfeited |
|---|---|
| Less than 12 months | 100 |
| Between 12 months and 24 months | 50 |
| More than 24 months | 0 |

On the 11 October 2004, 11,021,991 Investment shares were awarded to 119 employees in the plan. During the period ended 31 December 2005, 836,054 Investment Shares held in the Re-Investment Plan were forfeited and 5,560,311 investment shares were released from the plan.

To encourage reinvestment, and in recognition of the fact that the Investment Shares carry forfeiture provisions, after three years participants will receive up to one ''Matching share'' for each Investment Share (subject to continued employment and achievement of performance conditions).

The performance condition, described below, is based on growth in earnings per share (''EPS'') in the group. This measure was chosen by the Board for its transparency to participants and to incentivise executives to deliver the benefits of the merger.

| EPS Growth 2003 – 2006 | Number of Matching Shares for each Investment Share |
|---|---|
| PI + 9% or less over three years | 1 for 3 |
| PI + 24% or more over three years | 1 for 1 |

(where PI stands for an appropriate index of price inflation – the Retail Price Index (RPI))

For levels of EPS performance between those shown in the table above, the number of matching shares awarded will vary on a straight line basis between the minimum and maximum levels shown.

During 2005 the growth in the company's EPS exceeded the growth in the RPI by 22.2 percentage points (2004: 13.2 percentage points).

During the year the following Executive Directors participated in the Re-Investment Plan.

| Investment shares | 31 December 2004 | First Release from Re-Investment Plan on 11 October 2005 | 31 December 2005 |
|---|---|---|---|
| Alain Grisay | 1,195,637 | **597,819** | **597,818** |

# Directors' Remuneration Report

## Share Options

Details of the Share Option schemes are set out on pages 59 and 60.

Following the introduction of the Long Term Remuneration Plan no further grants will be made under the 1995 or 2002 Executive Share Option Schemes.

No options were granted to Directors or former Directors during 2005. No options were exercised by Directors during 2005. During 2005 Messrs Arthur, Back and Talbut, former Directors of the Company, exercised 64,112, 115,107 and 109,711 options respectively realising gains on exercise of £13,000, £51,000 and £117,000 respectively. 25,000 options previously granted to Directors lapsed during 2005 and 441,098 options previously granted to former Directors lapsed during 2005.

| | 31 December 2005 | 31 December 2004 | 31 December 2005 Share Save* | 31 December 2004 Share Save* |
|---|---|---|---|---|
| Howard Carter | **525,423** | 525,423 | **6,915** | 6,915 |
| Ian Paterson Brown | **297,170** | 322,170 | **6,915** | 6,915 |

* Options held at an exercise price of 114 pence by saving up to £120 per month in the F&C Asset Management plc Share Save Scheme for five years (6,915).

### Options granted under the 1995 & 2002 Executive Share Option Schemes:

| Date of Grant | Howard Carter | Ian Paterson Brown* | Option Price |
|---|---|---|---|
| 1995 Executive Share Option Scheme | | | |
| 13 October 1995 | – | 25,000 | 230.7p |
| 9 June 1998 | 194,036 | 55,331 | 203.8p |
| 16 July 1999 | 48,437 | 83,095 | 232.5p |
| 28 April 2000 | 76,580 | 47,830 | 214.0p |
| 1 March 2001 | 44,500 | 3,000 | 455.8p |
| Opening position at 1 January 2005 | 363,553 | 214,256 | – |
| Options exercised during the year | – | – | – |
| Options lapsed during the year | – | (25,000) | – |
| Options remaining at 31 December 2005 | 363,553 | 189,256 | – |
| 2002 Executive Scheme | | | |
| 19 March 2003 | 161,870† | 107,914 | 139.0p |
| Opening position at 1 January 2005 | 161,870 | 107,914 | – |
| Options exercised during the year | – | – | – |
| Options lapsed during the year | – | – | – |
| Options remaining at 31 December 2005 | 161,870† | 107,914 | – |

* All of Ian Paterson Brown's options granted under the 1995 Executive Option Scheme were awarded prior to his appointment as a Director on 1 July 2002. Accordingly at 31 December 2005 and 20 March 2006 Ian Paterson Brown had received 107,914 options for ''qualifying services'' as a Director.

† On 28 March 2006 Mr Carter exercised and sold all 161,870 options realising a gain on exercise of £123,000.

The earliest date on which all options can be exercised, assuming the performance criteria have been satisfied, is three years after the date of grant. Following the announcement of the 2005 Annual Results, the performance conditions attached to all options granted to Directors under both the 1995 and 2002 Executive Share Option Scheme have been met in full. All options expire on the tenth anniversary of the date of grant.

## 1995 Executive Share Option Scheme

Options granted under the 1995 Executive Share Option Scheme have a ten year life and cannot be exercised until both (a) a period of three years has elapsed from the date of grant; and (b) the performance goal of growth in earnings per share at a rate of 2 per cent. above the rate of inflation in respect of each year cumulatively has been met. Once both these criteria have been achieved, up to one-third can be exercised, up to two-thirds after a period of six years from the date of grant and the total or any outstanding amount after a period of eight years.

Following the introduction of the 2002 Executive Share Option Scheme no further grants were made under the 1995 Executive Share Option Scheme. During the year no options were granted under the 1995 Executive Share Option Scheme. During the year 81,369 options were exercised at prices of between 203.83 pence and 214.00 pence. 837,817 options were forfeited or expired in the year which had been granted under the 1995 Scheme.

At 31 December 2005 the following options granted under the 1995 Executive Share Option Scheme to acquire Ordinary Shares were outstanding:

| No. of Ordinary Shares | Exercisable before | Exercise Price(p) |
|---:|---:|---:|
| 730,028 | 9 June 2008 | 203.83 |
| 781,834 | 16 July 2009 | 232.50 |
| 642,029 | 28 April 2010 | 214.00 |
| 18,740 | 20 October 2010 | 320.17 |
| 520,500 | 1 March 2011 | 455.83 |

The Company has now met the three year cumulative performance criteria and all outstanding options under the 1995 Executive Share Option Scheme are now exercisable.

During 2005 the growth in the company's EPS exceeded the growth in the RPI by 22.2 percentage points (2004: 13.2 percentage points).

## 2002 Executive Share Option Scheme

The exercise of options granted under the 2002 Executive Scheme is dependent on the achievement by the Company of specified thresholds of earnings per share before impairment and amortisation of goodwill, restructuring costs and the cost of the Re-Investment Plan ("EPS"), and growth in excess of the growth in the Retail Price Index ("RPI") over a three year performance period commencing on the first day of the accounting period in which the grant was made.

An option will not become exercisable unless the growth in the EPS of the Company over the period exceeds the growth in the RPI over the same period by 9 per cent. Where that 9 per cent. target is achieved, one half of the number of ordinary shares forming the option will become exercisable.

For an option to become exercisable in full, the growth in the EPS of the Company over the period must exceed the growth in the RPI over the same period by a minimum of 24 per cent. The number of ordinary shares under option which will become exercisable will increase on a sliding scale if the growth in the EPS exceeds the growth in the RPI by between 9 per cent. and 24 per cent. over the performance period. The EPS measure is chosen because it is designed to enable the 2002 Executive Scheme to reward sustained improvement in the group's underlying financial performance.

Following the introduction of the Long Term Remuneration Plan in 2004, no grants have been made or will be made under the 2002 Executive Share Option Scheme. During the year 1,152,737 options were exercised at a price of 139.00 pence and 258,639 options lapsed in the year which had been granted under the 2002 Scheme.

# Directors’ Remuneration Report

At 31 December 2005 the following options granted under the 2002 Executive Share Option Scheme to acquire Ordinary Shares were outstanding:

| No. of Ordinary Shares | Earliest Exercise Date (assuming performance criteria satisfied) | Exercisable before | Exercise Price(p) |
|---:|---:|---:|---:|
| 2,729,971 | 19 March 2006 | 19 March 2013 | 139.00 |
| 1,270,331 | 9 March 2007 | 9 March 2014 | 240.83 |

The Options granted on 19 March 2003 have met the performance conditions set out above in full and are now exercisable.

During 2005 the growth in the company’s EPS exceeded the growth in the RPI by 22.2 percentage points (2004: 13.2 percentage points).

The share price at 31 December 2005 was 177.25 pence. During the year the highest price was 256.25 pence per share and the lowest price was 174.00 pence.

### Other senior executives

There are a number of senior executives who make a significant contribution to the group. These senior executives directly support the Company’s Executive Directors. The Remuneration Committee has regard to the remuneration of members of this group whose total remuneration including salary, bonus and benefits but excluding pension contributions and share scheme participation is summarised below. These numbers have been prepared on a comparable basis with the figures shown in the column headed ‘‘Total 2005 (excluding pension contributions)’’ within the Statement on Directors’ Remuneration on page 54.

The table below covers the total remuneration of all senior executives who served at any time during the year.

| Total Remuneration £000 | Number of senior executives (excluding executive directors) 2005 | Number of senior executives (excluding executive directors) 2004* |
|---|---:|---:|
| 100-125 | **54** | 34 |
| 126-150 | **32** | 18 |
| 151-175 | **13** | 12 |
| 176-200 | **17** | 11 |
| 201-225 | **17** | 8 |
| 226-250 | **6** | 6 |
| 251-300 | **19** | 8 |
| 301-400 | **3** | 6 |
| 401-500 | **4** | 2 |

* Statistics include the remuneration of F&CGH employees for the period 11 October 2004 to 31 December 2004.

By order of the Board,

W Marrack Tonkin, FCCA
*Secretary*

80 George Street
Edinburgh EH2 3BU
10 April 2006

# F&C Asset Management plc
# Consolidated Financial Statements
## for the year ended 31 December 2005

**These Financial Statements have been prepared in accordance with International Financial Reporting Standards.**

**The Financial Statements of F&C Asset Management plc (the Company), given on pages 162 to 189, have been prepared in accordance with UK GAAP.**

# Statement of Directors' Responsibilities in respect of the Consolidated Financial Statements

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards (IFRSs) adopted by the European Union.

The Directors are required to prepare Financial Statements for each financial year that present fairly the financial position of the Group and the financial performance and cash flows of the Group for that period. In preparing those financial statements, the Directors are required:

- To select suitable accounting policies and then apply them consistently;
- To present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- To provide additional disclosure when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance; and
- To state that the Group has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the Financial Statements comply with the Companies Act 1985 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors confirm that they have complied with these requirements and, having a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future, continue to adopt the going concern basis in preparing the financial statements.

# Independent Auditors' Report to the Shareholders of F&C Asset Management plc

We have audited the group financial statements of F&C Asset Management plc for the year ended 31 December 2005 which comprise the Group Income Statement, the Group Balance Sheet, the Statement of Recognised Income and Expense, the Group Cash Flow Statement, and the related notes 1 to 42. These group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of F&C Asset Management plc for the year ended 31 December 2005 and on the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an 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 company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report and the group financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the group 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 group financial statements give a true and fair view and whether the group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors' Report is not consistent with the group financial statements, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding director's remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited group financial statements. The other information comprises only the Financial and Business Highlights, Key Highlights of 2005, Chairman's Statement, Chief Executive's Report, Corporate Responsibility Report, Non-executive Directors, Executive Directors, Report of the Directors, Directors' Report on Corporate Governance, the unaudited part of the Directors' Remuneration Report, Notice of the Annual General Meeting and Corporate Information. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the group financial statements. Our responsibilities do not extend to any other information.

### Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the group financial statements.

It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the group financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

# Independent Auditors' Report to the Shareholders of F&C Asset Management plc

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 group 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 group financial statements.

**Opinion**

In our opinion the group financial statements:

- give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's affairs as at 31 December 2005 and of its loss for the year then ended; and
- have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

Ernst & Young LLP

ERNST & YOUNG LLP
Registered Auditor
Edinburgh

10 April 2006

# Consolidated Income Statement

| | Notes | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|---|
| **Revenues** | | | |
| Investment management fees | 2 | **277,356** | 154,507 |
| Investment income attributable to policyholders | 2 | **28,918** | 28,047 |
| Other income | 2 | **691** | 3,249 |
| **Total revenues** | | **306,965** | 185,803 |
| Fee and commission expenses | 2 | **(10,895)** | (5,837) |
| **Net revenues** | 2 | **296,070** | 179,966 |
| **Operating expenses** | | | |
| Losses on financial instruments carried at fair value through profit or loss | 3 | **(26,408)** | (24,373) |
| Dealing costs on investment contract assets | | **(1,226)** | (2,526) |
| **Net operating costs: investment and insurance contracts** | | **(27,634)** | (26,899) |
| Operating expenses | 4(b) | **(150,695)** | (101,367) |
| Re-Investment Plan costs | | **(22,162)** | (5,428) |
| Impairment of intangible assets – management contracts | 13 | **(111,500)** | – |
| Amortisation of intangible assets – management contracts | 13 | **(55,801)** | (20,762) |
| **Total operating expenses before restructuring costs** | | **(367,792)** | (154,456) |
| **Operating (loss)/profit before restructuring costs** | | **(71,722)** | 25,510 |
| Restructuring costs: | | | |
| – Reorganisation costs post acquisition of F&CGH Group | 6(a) | **(22,405)** | (18,332) |
| – Operations outsourcing | 6(b) | **(2,235)** | (932) |
| **Operating (loss)/profit after restructuring costs** | | **(96,362)** | 6,246 |
| Finance revenue | 7 | **15,570** | 4,641 |
| Finance costs | 8 | **(19,495)** | (14,983) |
| Impairment in associates and other financial investments | 14 | **(5,026)** | – |
| Loss on disposal of subsidiaries | 16(c) | **(672)** | – |
| Share of loss of associates | 15 | **(339)** | (318) |
| **Loss before tax** | | **(106,324)** | (4,414) |
| Tax – Policyholders | | **(118)** | (445) |
| Tax – Shareholders | | **29,169** | 1,318 |
| Tax income | 9 | **29,051** | 873 |
| **Loss for the year** | | **(77,273)** | (3,541) |
| **Attributable to:** | | | |
| Equity holders of the parent | | **(77,273)** | (3,541) |
| Minority interests | | **–** | – |
| **Loss for the year** | | **(77,273)** | (3,541) |
| **Memo – dividends proposed** | 10(a) | **33,381** | 32,914 |
| **– dividends paid** | 10(a) | **51,817** | 16,480 |
| **Basic loss per share** | 11 | **(16.36)p** | (1.60)p |
| **Diluted loss per share** | 11 | **(15.77)p** | (1.56)p |

# Consolidated Balance Sheet

| | Notes | As at 31 December 2005 £000 | As at 31 December 2004 (as restated) £000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 12 | **11,242** | 10,912 |
| Intangible assets: | | | |
| – Goodwill | 13 | **577,946** | 577,946 |
| – Management contracts | 13 | **416,141** | 589,823 |
| – Other intangible assets | 13 | **1,641** | 506 |
| | 13 | **995,728** | 1,168,275 |
| Other financial investments | 14 | **3,397** | 4,195 |
| Loan to associate | 21 | **2,500** | – |
| Investment in associates | 15 | **335** | 4,767 |
| Deferred acquisition costs | 17 | **8,342** | 7,808 |
| Deferred tax assets | 18 | **34,083** | 30,223 |
| **Total non-current assets** | | **1,055,627** | 1,226,180 |
| **Current assets** | | | |
| Financial investments | 19 | **982,943** | 813,595 |
| Reinsurance assets | 20 | **2,617** | 2,352 |
| Stock of units and shares | 19 | **676** | 556 |
| Trade and other receivables | 21 | **92,858** | 63,071 |
| Deferred acquisition costs | 17 | **3,018** | 2,566 |
| Cash and cash equivalents: | | | |
| – Policyholders | 22 | **28,152** | 47,145 |
| – Shareholders | 22 | **118,045** | 133,939 |
| | 22 | **146,197** | 181,084 |
| **Total current assets** | | **1,228,309** | 1,063,224 |
| **Total assets** | | **2,283,936** | 2,289,404 |
| **Liabilities** | | | |
| **Non-current liabilities** | | | |
| Interest bearing loans and borrowings | 23 | **34,800** | 214,800 |
| Trade and other payables | 24 | **–** | 3 |
| Provisions | 25 | **12,960** | 10,322 |
| Pension deficit | 26(a) | **48,032** | 17,707 |
| Deferred income | 27 | **14,351** | 10,752 |
| Deferred tax liabilities | 18 | **125,295** | 177,963 |
| **Total non-current liabilities** | | **235,438** | 431,547 |
| **Current liabilities** | | | |
| Investment contract liabilities | 28 | **1,006,928** | 862,308 |
| Insurance contract liabilities | 29 | **2,617** | 2,352 |
| Interest bearing loans and borrowings | 23 | **185,000** | 5,000 |
| Trade and other payables | 24 | **58,724** | 61,274 |
| Provisions | 25 | **6,463** | 2,534 |
| Employee benefits | | **29,954** | 35,331 |
| Deferred income | 27 | **3,679** | 4,999 |
| Current tax payable | | **9,713** | 6,401 |
| **Total current liabilities** | | **1,303,078** | 980,199 |
| **Total liabilities** | | **1,538,516** | 1,411,746 |
| **Equity attributable to equity holders of the parent** | | | |
| Share capital | 30, 31 | **484** | 482 |
| Share premium account | 31 | **30,730** | 28,956 |
| Merger reserve | 31 | **606,146** | 749,754 |
| Other reserves | 31 | **52,179** | 108,401 |
| Retained earnings | 31 | **56,379** | (9,935) |
| **Total equity attributable to equity holders of the parent** | | **745,918** | 877,658 |
| Minority interests | 31 | **(498)** | – |
| **Total equity** | 31 | **745,420** | 877,658 |
| **Total liabilities and equity** | | **2,283,936** | 2,289,404 |

The financial statements were approved by the Board of Directors and authorised for issue on 10 April 2006. They were signed on its behalf by:

Robert Jenkins *Chairman*

10 April 2006

Alain Grisay *Chief Executive*

10 April 2006

# Consolidated Statement of Recognised Income and Expense

| | Notes | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|---|
| **Loss for the year** | | **(77,273)** | (3,541) |
| Foreign exchange movements on translation of foreign operations | | **(4,246)** | 4,846 |
| Actuarial loss on defined benefit pension schemes | 26(a) | **(30,734)** | (2,909) |
| Gain on available for sale financial investments | | **893** | 660 |
| Fair value gains transferred to the Income Statement | | **(1,120)** | – |
| Goodwill written back on disposal of subsidiary | 16(c) | **449** | – |
| Tax income on items taken directly to equity | 9(a) | **8,597** | 1,155 |
| Share of associate costs charged directly to equity | 15 | **–** | (99) |
| **Net (expense)/income recognised directly in equity** | | **(26,161)** | 3,653 |
| **Total recognised income and expense for the year** | 31 | **(103,434)** | 112 |
| **Attributable to:** | | | |
| Equity holders of the parent | | **(103,434)** | 112 |
| Minority interests | | **–** | – |
| | | **(103,434)** | 112 |

# Consolidated Cash Flow Statement

| | Notes | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating (loss)/profit before restructuring costs | | **(71,722)** | 25,510 |
| Cash outflow relating to restructuring costs | | **(24,913)** | (9,157) |
| **Adjustments for non-cash items** | 32 | **195,298** | 32,858 |
| **Changes in working capital and provisions** | 32 | **(54,299)** | (14,630) |
| **Cash generated from operating activities** | | **44,364** | 34,581 |
| Income tax paid | | **(14,359)** | (6,608) |
| **Net cash inflow from operating activities** | | **30,005** | 27,973 |
| **Cash flows from investing activities** | | | |
| Proceeds from sale of property, plant and equipment | | **94** | – |
| Acquisition of property, plant and equipment | | **(3,701)** | (4,066) |
| Payment to increase investment in associate | | **(485)** | (5,101) |
| Rebate of consideration on RSAI acquisition | | **–** | 3,893 |
| Purchase of intangibles – management contracts | | **(1,249)** | – |
| Purchase of intangibles – software | | **(989)** | – |
| Return of capital from investments | | **132** | – |
| Proceeds from disposal of subsidiaries | | **10** | – |
| Cash transferred on disposal of subsidiary | | **(824)** | – |
| Payments to acquire investments | | **(35)** | – |
| Loan to associate (ISIS EP LLP) | 21 | **(2,500)** | – |
| Expenses of F&CGH Group acquisition | | **(624)** | (11,998) |
| Net cash acquired with subsidiary undertakings | | **–** | 132,791 |
| Investment income from private equity investments | | **5,840** | 16 |
| Investment income from interest | | **3,472** | 1,653 |
| Investment income from dividends | | **32** | 9 |
| **Net cash (outflow)/inflow from investing activities** | | **(827)** | 117,197 |
| **Cash flows from financing activities** | | | |
| Proceeds from issue of share capital | 31 | **1,776** | 822 |
| Drawdown of revolving credit facility from FP Group | | **–** | 5,000 |
| Repayment of revolving credit facility from FP Group | | **–** | (15,000) |
| Proceeds from long-term borrowings | | **–** | 25,000 |
| Interest paid on loans | | **(13,498)** | (11,299) |
| Other interest paid | | **(392)** | (879) |
| Equity dividends paid | 10(a) | **(51,817)** | (16,480) |
| Interest paid on Preference Shares | | **(47)** | (23) |
| Purchase of own shares | | **(87)** | (1,165) |
| **Net cash outflow from financing activities** | | **(64,065)** | (14,024) |
| **Net (decrease)/increase in cash and cash equivalents** | | **(34,887)** | 131,146 |
| Cash and cash equivalents at 1 January | | **181,084** | 49,938 |
| **Cash and cash equivalents at 31 December** | 22 | **146,197** | 181,084 |
| **Cash and cash equivalents** | | | |
| Shareholders | 22 | **118,045** | 133,939 |
| Policyholders | 22 | **28,152** | 47,145 |
| | 22 | **146,197** | 181,084 |

# Accounting Policies

### Basis of preparation

These are the first full Consolidated Financial Statements of F&C Asset Management plc and its subsidiaries (the Group) which have been prepared in accordance with International Financial Reporting Standards (IFRS). The Consolidated Financial Statements are presented in pounds Sterling, rounded to the nearest thousand, except where otherwise indicated.

### Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with IFRS, as adopted by the European Union (EU) as they apply to financial statements of the Group for the year ended 31 December 2005, and those parts of the Companies Act 1985 applicable to companies reporting under IFRS.

### First-time adoption

In line with IFRS 1 'First-time Adoption of International Financial Reporting Standards', an opening IFRS balance sheet has been prepared as at 1 January 2004, the date of the Group's transition to IFRS. To the extent that the IFRS accounting policies differ from those applied under UK GAAP, adjustments to balances reported under UK GAAP have been made.

An explanation of the effect of the transition to IFRS on the reported financial position and financial performance of the Group is provided in note 42 to these financial statements. This includes reconciliations of equity and profit or loss for comparative figures previously reported under UK GAAP to the revised figures reported under IFRS.

The Group has applied its accounting policies under IFRS retrospectively as at the date of transition, subject to the following exemptions, as permitted by IFRS 1:

- Past business combinations have been restated to comply with IFRS 3 'Business Combinations' with effect from 1 July 2002.
- Cumulative foreign exchange differences are deemed to be zero at the date of transition to IFRS.
- IFRS 2 'Share-based Payment' has not been applied to any equity instruments that were granted on or before 7 November 2002.
- Items of property, plant and equipment are carried at the carrying value that was applied under UK GAAP at 1 January 2004.
- All actuarial gains and losses in respect of defined benefit pension arrangements have been recognised in full at the date of transition to IFRS.

The Group has adopted early, from 1 September 2005, the Fair Value Option in IAS 39 'Financial Instruments: Recognition and Measurement' issued by the International Accounting Standards Board in June 2005. The Fair Value Option allows for any financial instrument to be classified upon initial recognition at fair value through profit and loss. This enables the liabilities of the Group's unit linked insurance business to be measured on a basis consistent with the underlying policyholders' assets which are held to meet these obligations.

Previously recognised qualifying financial liabilities were formally designated as fair value through profit or loss, as are newly recognised qualifying financial liabilities going forward. Comparative information has been restated. The Group has opted for the Fair Value Option to prevent the mismatch of unit linked assets and liabilities in respect of F&C Managed Pension Funds Ltd, the Group's insurance subsidiary that would have resulted if measured on a different basis.

The Group has adopted early, from 1 January 2005, the revised version of IAS 19 'Employee Benefits' which includes the amendments resulting from 'Amendment to IAS 19 Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures' issued by the International Accounting Standards Board in December 2004. As a result, additional disclosures are made, providing information about trends in the assets and liabilities in the defined benefit plans and the assumptions underlying the components of the defined benefit cost. Also, the Group has elected to recognise defined benefit plan actuarial gains and losses in full, outside profit or loss, and present them in the Statement of Recognised Income and Expense (SORIE). Comparative information has been restated.

The parent Company has continued to present individual financial statements prepared on a UK GAAP basis as permitted by section 226(2) of, and Schedule 4 to, the Companies Act 1985, adopting the exemption of omitting the profit and loss account and related notes conferred by section 230 of that Act. The parent Company financial statements with its respective accounting policies, are presented on pages 162 to 189.

### Accounting estimates assumptions and judgements

The preparation of the financial statements necessitates the use of estimates, assumptions and judgements. These estimates, assumptions and judgements affect the reported amounts of assets, liabilities and contingent liabilities at the balance sheet date as well as affecting the reported income and expenses for the year. Although the estimates are based on management's best knowledge and judgement of information and financial data, the actual outcome may differ from these estimates. The key assumptions which affect the results for the year and balances as at the year-end are specifically identified, where appropriate, in the notes to the Consolidated Financial Statements.

# Accounting Policies

**Summary of significant accounting policies**

The accounting policies set out below have been applied consistently throughout the Group for the purposes of the consolidated financial statements. They have also been applied in preparing an opening IFRS balance sheet at 1 January 2004 for the purposes of the transition to IFRS and in preparing the Consolidated Income Statement for the year ended 31 December 2004 and for the Balance Sheet on that date, except as permitted by the transitional requirements of IFRS 1 'First-time Adoption of International Financial Reporting Standards'.

**(a) Consolidation**

*(i) Subsidiaries*

Subsidiaries are all entities over which the Group has the power, directly or indirectly, to govern the financial and operating policies so as to obtain benefits from its activities. All subsidiaries follow accounting policies consistent with those of the Group and have coterminous reporting periods.

The Consolidated Financial Statements incorporate the assets, liabilities, results and cash flows of the Company and its subsidiaries. The results of subsidiaries acquired or sold during the period are included in the consolidated results from the date of acquisition or up to the date of disposal. Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions are eliminated in preparing the Consolidated Financial Statements. The financial information of subsidiaries used in preparing the Consolidated Financial Statements is prepared using consistent accounting policies.

Minority interests represent the portion of profit or loss and net assets in subsidiaries not held by the Group and are presented separately in the Income Statement and within equity in the Balance Sheet, separately from parent shareholders' equity.

*(ii) Associates*

Associates are all entities over which the Group has significant influence but not control over the financial and operating policies. Investments in associates are accounted for under the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any impairment loss) identified on acquisition.

Under the equity method of accounting, an investment is included as the cost of the investment plus the Group's share of post-acquisition changes in net assets after deducting any distributions received and any impairment loss. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised. The Group's share of post-tax profits or losses is presented as a single line item in the Income Statement. The Group also recognises directly in equity its share of post-acquisition gains and losses which the associate has recognised directly in equity, which are presented in the SORIE.

The Group's associates follow accounting policies consistent with those of the Group and have coterminous reporting periods.

*(iii) Business combinations*

A business combination is the bringing together of separate entities or businesses into one reporting entity. The result is that one entity, the acquirer, obtains control of one or more entities or businesses.

The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of the acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill.

**(b) Foreign currencies**

The Consolidated Financial Statements are presented in pounds Sterling, the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured in that functional currency.

*(i) Foreign currency transactions*

Transactions in foreign currencies are translated to the functional currency at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the exchange rate ruling at the balance sheet date, and any exchange differences arising are taken to the Income Statement.

Non-monetary assets and liabilities measured at historical cost in a foreign currency are translated using the exchange rate at the date of transaction and are not subsequently restated. Non-monetary assets and liabilities stated at fair value in a foreign currency are translated at the exchange rate at the date the fair value was determined. When fair value movements in assets and liabilities are reflected in the Income Statement, the corresponding exchange movements are also recognised in the Income Statement. Conversely, when fair value movements in assets and liabilities are reflected directly in equity, the corresponding exchange movements are also recognised directly in equity.

*(ii) Foreign operations*

The functional currency of foreign operations is predominantly the Euro.

The assets and liabilities of foreign operations are translated to Sterling at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to Sterling at foreign exchange rates approximating to the rates ruling at the dates of the transactions. Foreign exchange differences arising on translation of foreign operations into Sterling, including related intangible assets, are recognised directly in the Group's Foreign Currency Translation Reserve (FCTR), which is a separate component of equity and reported in the SORIE. These exchange differences are recognised as income or expenses in the period in which the foreign operations are disposed of.

**(c) Revenue recognition**

Asset management fees, investment advisory fees and other revenue generated from the Group's investment management activities are recognised in the Income Statement over the period for which these investment management services are provided.

Initial fees received in advance are taken to the Balance Sheet and amortised over the period of the asset management service. The Group enters into standard contractual terms for all investors. Therefore, the period of provision of asset management services is estimated based upon the Group's experience of the average holding periods of investors. The average holding period is assessed on an annual basis.

The Group has entitlement to earn performance fees from a number of clients where the actual fund performance of clients' assets exceeds defined benchmarks by an agreed level of outperformance in a set time period. Most of the Group's performance fee arrangements are assessed on a calendar year basis. Performance fees are recognised when the quantum of the fee can be estimated reliably, which is when the performance period ends, when this occurs on or before the reporting date, or where there is a period of less than six months remaining to the end of the performance period and there is evidence at the reporting date which suggests that the current performance will be sustainable.

**(d) Leases**

All Group leases are operating leases, being leases where the lessor retains substantially all the risks and rewards of ownership of the leased asset. Rentals paid under operating leases are charged to the Income Statement on a straight-line basis over the lease term. Lease incentives are recognised by the Group as a reduction in the rental expense, allocated on a straight-line basis over the lease term. Accounting policy (s) discusses the recognition of onerous provisions on property leases when the leased space has ceased to be occupied by the Group.

**(e) Fee and commission expenses**

Fee and commission expenses comprise two main elements: costs associated with gaining new asset management contracts and subsequent commission paid to agents. The costs associated with the gaining of contracts are deferred and amortised over the estimated term of the contracts (in line with the treatment of the associated initial fees received), while the subsequent commission paid to agents is expensed as the services are provided.

**(f) Restructuring costs**

Where the Group incurs significant, Board-approved, non-recurring expenditure as a result of a strategic decision which fundamentally changes how the Group operates, then expenditure in relation to the strategic project is separately recognised on the face of the Income Statement as 'Restructuring costs'. While the costs will be recognised within the discrete timeframe of the project, the scale of major strategic initiatives may result in expenditure in respect of the same restructuring initiative straddling more than one financial reporting period. The classification allows shareholders to understand the elements of financial performance in the year so as to facilitate comparison with prior periods and to assess trends in financial performance.

**(g) Finance revenue**

Finance revenue comprises interest, dividends, expected return on pension assets and gains on sale of investments held at amortised cost. Dividend income is recognised when the right to receive payment is established. Interest income is recognised in the Income Statement on an effective yield basis as it accrues.

**(h) Finance costs**

Finance costs comprise interest payable on borrowing, interest on pension liabilities and dividends on Preference Shares. Borrowing costs are recognised in the Income Statement on an effective yield basis.

**(i) Income taxes**

The income tax expense/income disclosed on the face of the Income Statement represents the aggregate of current tax and the movement in deferred tax. Income tax is recognised in the Income Statement for the period, except to the extent that it is attributable to a gain or loss that is recognised directly in equity. In such cases the gain or loss shown in equity is stated separately from the attributable income tax.

*Current tax* is the expected tax payable to the taxation authorities on the taxable profit for the period, using tax rates enacted or substantively enacted at the balance sheet date, and includes any adjustment to tax payable in respect of previous years.

*Deferred tax* is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit, accounted for using the balance sheet liability method.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised, except:

- where the deferred tax asset or liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination that at the time of the transaction affects neither the accounting nor taxable profit or loss; or
- in respect of taxable or deductible temporary differences associated with investments in subsidiaries and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Any income tax expense or income in respect of taxable gains or losses attributable to policyholders falls to be borne by or to the benefit of the Group's unit linked policyholders. As a result, the Directors consider it appropriate to differentiate on the face of the Income Statement between tax attributable to policyholders and that attributable to shareholders.

**(j) Property, plant and equipment**

Property, plant and equipment is stated at cost less accumulated depreciation and accumulated impairment losses.

Expenditure on property, plant and equipment is capitalised on initial recognition. Subsequent expenditure is only capitalised when it is probable that there will be future economic benefits associated with the expenditure which can be measured reliably. All other expenditure is recognised in the Income Statement as an expense as incurred.

Property, plant and equipment is depreciated so as to write off the cost of assets, using the straight-line method, over their estimated useful lives, as follows:

| | | |
|---|---|---|
| Leasehold improvements | – | over 10 years |
| Motor vehicles | – | over 3 years |
| Office furniture & equipment | – | over 3-5 years |
| Computer equipment | – | over 3 years |

Depreciation is recognised as an expense in the Income Statement.

The carrying value of assets and their useful lives are reviewed at each reporting date. If an indication of impairment exists, the assets are written down to their recoverable amount and the impairment is charged to the Income Statement in the period in which it arises.

An item of property, plant and equipment is derecognised upon disposal or when no further future economic benefits are expected from its use. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying value of the asset) is included in the Income Statement in the year the asset is derecognised.

**(k) Intangible assets**

*(i) Goodwill*

Goodwill arising from a business combination is initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets and liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. If the cost of the acquisition is less than the fair value of the net assets, the difference is recognised directly in the Income Statement. Business combinations arising after 1 July 2002 are accounted for under IFRS 3 'Business Combinations' using the purchase method. Where the initial amount of goodwill can only be determined on a provisional basis at the end of the financial reporting period, adjustments are made to the amount of goodwill up to 12 months from the date of acquisition. Other adjustments to goodwill are made for amounts that are contingent on future events and on the realisation of potential benefits of the acquiree's tax loss carry forwards and other deferred tax assets that did not satisfy the criteria for separate recognition on acquisition.

Goodwill is tested annually for impairment or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill was tested for impairment at 1 January 2004 (the date of transition to IFRS) and annually thereafter.

*(ii) Investment management contracts*

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less accumulated amortisation and any accumulated impairment losses.

The useful lives of management contracts are finite and are amortised on a straight line basis over their estimated average contract term, depending on the nature of the contract, with amortisation being charged to the Income Statement. The amortisation period is reviewed at each financial year-end. The estimated useful lives have been assessed as follows:

| | | |
|---|---|---|
| Investment trusts | – | 20 years |
| Insurance | – | 10 years |
| Institutional | – | 10 years |
| Retail | – | 10 years |

(iii) *Other intangible assets*

The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less accumulated amortisation and any accumulated impairment losses. Separately purchased intangible assets have a finite life and are shown at cost less accumulated amortisation and impairment losses. Amortisation is charged to the Income Statement in equal annual instalments, based on the useful economic life of the intangible assets concerned as follows:

| | | |
|---|---|---|
| Software | – | 3 years |
| Licences | – | over the contractual term (3-5 years) |

Subsequent expenditure on capitalised intangible assets is expensed as incurred.

**(l) Impairment**

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. Any impairment arising is recognised in the Income Statement. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes.

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Except for any goodwill impairments which cannot be reversed, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the Income Statement. After such a reversal, the amortisation or depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

**(m) Financial instruments**

When financial instruments are recognised initially they are measured at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

They are classified into the categories described below:

(i) *Financial investments at fair value through profit or loss* include investments that are held for trading purposes or that have been specifically designated as 'at fair value through profit or loss'. They are measured on initial recognition at fair value and carried in the Balance Sheet at fair value. Subsequent to initial recognition, movements in fair value are taken to the Income Statement in the period in which they arise. The following assets and liabilities are classified as *Financial investments at fair value through profit or loss*:

Current assets:

- Financial investments
- Stock of units and shares

Current liabilities:

- Investment contract liabilities

The Group has adopted the Fair Value Option in IAS 39, which enables the liabilities in respect of the Group's unit linked investment contracts to be matched to the fair value of the assets which are held and which are solely attributable to the investment contract policyholders, thus reflecting the contractual entitlement of the policyholders. To do otherwise would result in liabilities differing in value from the attributable assets and hence give rise to a mismatch between assets and liabilities which would not reflect the substance of the financial position.

(ii) *Available for sale financial assets* are also carried at fair value in the Balance Sheet. In respect of unquoted instruments, or where the market for a financial instrument is not active, fair value is established by using recognised valuation methodologies, in accordance with International Private Equity and Venture Capital Valuation Guidelines.

For unquoted investments in early stage enterprises and enterprises with revenues but without significant profits or significant positive cash flows, fair value is determined using the Price of a Recent Investment Method. After an appropriate period, an assessment is made as to whether either the circumstances of the investment have changed such that another valuation methodology is appropriate, and whether there is any evidence of deterioration or strong defensible evidence of an increase in value. In the absence of these indicators fair value is determined to be that reported at the previous balance sheet date.

Unquoted investments with revenues, maintainable profits and/or maintainable cash flows are valued by deriving an Enterprise Value of the underlying business.

Movements in fair value, other than impairment losses and foreign exchange movements on monetary assets, are taken to the fair value reserve in equity until derecognition of the asset, at which time the cumulative amount in this reserve is recognised in the Income Statement. The following assets are classified as *Available for sale*:

Non-current assets

- Other financial investments

The fair value of instruments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; discounted cash flow analysis and option pricing models.

(iii) *Loans and receivables* are measured on initial recognition at fair value plus any incremental costs incurred. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest rate method. Gains and losses are recognised in the Income Statement when loans and receivables are derecognised or impaired, as well as through the amortisation process. The following assets and liabilities are classified as *Loans and receivables*:

Non-current assets:

- Loan to associate

Current assets:

- Trade and other receivables

Non-current liabilities:

- Interest bearing loans and borrowings
- Trade and other payables

Current liabilities:

- Interest bearing loans and borrowings
- Trade and other payables

The Group has adopted "trade date" accounting. Accordingly, financial investments are recognised on the date the Group commits to the purchase of the investments, and are derecognised on the date it commits to their sale.

**Derecognition of financial assets and liabilities**

*Financial assets*

A financial asset or, where applicable, a part of a financial asset, is derecognised when the rights to receive cash flows from the asset have expired.

*Financial liabilities*

A financial liability is derecognised when the obligation under the liability is either discharged or cancelled or expires.

**Impairment of financial assets**

The Group assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

*Assets carried at amortised cost*

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective yield. The carrying amount of the asset shall be reduced and the amount of the loss shall be recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the Income Statement to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

*Assets carried at cost*

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

*Available for sale financial assets*

If an available for sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from equity to the profit or loss. Reversals in respect of equity instruments classified as available for sale are not recognised in the profit or loss. Reversals of impairment losses on debt instruments are reversed through the Income Statement, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the profit or loss.

**(n) Cash and cash equivalents**

Cash and cash equivalents comprise cash balances, deposits held at call with banks and other short-term, highly liquid investments in money market instruments with original maturity dates of three months or less.

**(o) Investment contracts**

The Group sells unit linked pension investment contracts through its insurance subsidiary, F&C Managed Pension Funds Limited (MPF). These unit linked contracts involve both the transfer of a financial instrument and the provision of investment management services. The financial instrument component is classified as a financial liability at fair value through the profit or loss. The financial liability is measured using a valuation technique based on the carrying value of the assets and liabilities that are held to back the contract, adjusted to take account of the effect on the liabilities of discounting for the time value of tax payments on assets sold in the fund. The investment management fees earned from these contracts are accounted for as described in the revenue recognition accounting policy.

Unit linked policyholder assets held by MPF and related policyholder liabilities are carried at fair value, with changes in fair value taken to profit or loss.

Amounts received from and paid to investors under these contracts are accounted for as deposits received or paid and therefore not recorded in the Income Statement. At the balance sheet date the value of these contracts is stated at an amount equal to the fair value of the net assets held to match the contractual obligations.

**(p) Insurance contract liabilities**

Insurance contract liabilities are measured in accordance with actuarial principles and guidance. Any change in the value of the liability is taken to the Income Statement. Where these liabilities are reinsured, the element of the risk reinsured is valued on the same basis as the related liability and is included as an asset in the Balance Sheet. Changes in the value of the asset are taken to the Income Statement. Amounts recoverable under reinsurance contracts are assessed for impairment at each balance sheet date.

**(q) Employee benefits**

*(i) Short-term employee benefits*

Short-term employee benefits are recognised as an undiscounted expense and liability when the employee has rendered services during an accounting period. Short-term compensated absences are recognised in the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences or, in the case of non-accumulating compensated absences, when the absences occur.

*(ii) Profit-sharing and bonus payments*

These are recognised when there is a present legal or constructive obligation to make such payments as a result of past events and a reliable estimate of the obligation can be made.

*(iii) Pension obligations*

*Defined benefit schemes*

The Group operates a number of defined benefit pension arrangements.

These schemes provide benefits based on final pensionable salary. The assets of the funded schemes are held in separate trustee administered funds.

The pension liability recognised in the Balance Sheet is the present obligation of the employer, which is the estimated present value of future benefits that employees have earned in return for their services in the current and prior years, less the value of the plan assets in the schemes. The discount rate of the employees' benefits is the appropriate AA corporate bond yield at the balance sheet date. A qualified actuary performs the calculation annually using the projected unit credit method. The pension costs of the schemes in the Income Statement are analysed into:

- Current service cost, which is the actuarially calculated present value of the benefits earned by the active employees in each period.
- Past service costs, which relate to employee service in prior periods, arise as a result of the introduction of, or improvement to, retirement benefits in the current period and are recognised in the Income Statement on a straight-line basis over the period in which the increase in benefits vest.
- Settlements or curtailments, are recognised in the Income Statement to the extent that they are not allowed for in the actuarial assumptions. Losses on settlements or curtailments are measured at the date on which the employer becomes demonstrably committed to the transaction. Gains on settlements or curtailments are measured at the date on which all parties, whose consent is required, are irrevocably committed.
- The expected return on pension assets is recognised within 'Finance revenue' and the interest on scheme liabilities is recognised in 'Finance costs'.

The actuarial gains and losses, which arise from any new valuation and from updating the previous actuarial valuation to reflect conditions at the balance sheet date, are taken in full to the SORIE for the period.

Where the Group is unable to identify its share of assets and liabilities in multi-employer defined benefit schemes, the Group accounts for these in the same way as for defined contribution schemes.

*Defined contribution schemes*

Contributions made to these schemes are charged to the Income Statement as they become payable in accordance with the rules of the scheme.

*(iv) Other long-term employee benefits*

Other long-term employee benefits are recognised at the discounted present value of the obligation at the balance sheet date. The benefit is determined using actuarial techniques to estimate the amount of benefit employees have earned for their services at the balance sheet date.

*(v) Termination benefits*

Termination benefits are recognised as a liability and an expense when the Group is committed to the termination of employment before the normal retirement date. A commitment to such termination benefits arises when the Group has initiated detailed plans which cannot realistically be withdrawn.

### (r) Share-based payments

The Group operates a number of share scheme arrangements which require to be accounted for as share-based payments.

All grants of shares, share options or other share-based instruments that were granted after 7 November 2002 have been recognised as an expense. The fair values of share-based payment awards are measured using a valuation model applicable to the terms of the awards (Black Scholes, Binomial or Monte Carlo simulation). The fair value is measured by an independent external valuer (Mercer Human Resource Consulting Limited) at the date the award is granted and the expense is spread over the period during which the employees become unconditionally entitled to exercise the awards, known as the vesting period. The cumulative expense recognised in the Income Statement is equal to the estimated fair value of the award multiplied by the number of awards expected to vest. Vesting of awards typically depends upon meeting defined performance criteria such as continued Company service requirements, underlying earnings per share (EPS) targets and/or share price return targets.

Vesting of employee share awards depends upon meeting ''market'' and/or ''non-market related'' performance conditions. The type of vesting criteria affects the calculation of the expense charged to the Income Statement and subsequent adjustments, as follows:

(i) Non-market related conditions are performance criteria not directly linked to Company share price targets, such as EPS targets and/or Company service requirements. The probability of meeting non-market conditions is incorporated into the expense charge via the estimate of the number of awards expected to vest. The total cumulative expense is ultimately ''trued-up'' or ''trued-down'' to reflect the actual number of awards which vest. Therefore, if no awards vest, no cumulative expense charge is ultimately recognised.

(ii) Market related conditions are performance criteria linked to Company share price targets. The probability of meeting market conditions is incorporated into the calculation of the fair value of the award. Should the market-based performance condition not ultimately be met, no ''true up/down'' adjustment is made to reflect this. Therefore, an expense charge is made whether market-based awards ultimately vest or not.

IFRS 2 'Share-based Payment' makes a distinction between awards settled in equity and those settled in cash. Equity-settled awards are charged to the Income Statement with a corresponding credit to equity. Cash-settled awards are charged to the Income Statement with a corresponding credit to liabilities. The estimated fair value of cash-settled awards are remeasured at each reporting date until the payments are ultimately settled.

Awards to employees treated as ''good leavers'' vest immediately and the remaining full expense of the awards is charged to the Income Statement immediately. Good leavers include retirees and involuntary redundancies.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of EPS.

### (s) Provisions

A provision is recognised in the Balance Sheet when the Group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. No provision is established where a reliable estimate of the obligation cannot be made.

Where the Group expects some or all of a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

Where the Group has obligations under property leases and where the space has ceased to be used for the purposes of the business, full provision is made for future net outstanding liabilities under such leases after taking into account the effect of any expected sub-letting arrangements.

### (t) Share capital

When shares are issued, any component that creates a financial liability of the Company or Group is presented as a liability in the Balance Sheet, measured initially at fair value, net of transaction costs and thereafter at amortised cost until extinguished on conversion or redemption.

The remainder of the proceeds on issue is allocated to the equity component and included in shareholders' equity, net of transaction costs.

*Preference share capital*

The Group's issued preference share capital is classified as a liability. It is carried at amortised cost in the Balance Sheet. Preference dividends are recognised in the Income Statement as an interest expense as they accrue.

*Ordinary Share capital*

When Ordinary Shares are repurchased, the amounts of consideration paid, including directly attributable costs, are recognised in the own share reserve included within retained earnings and are classified as treasury shares. Dividends on Ordinary Shares are recognised on the date of payment, or if subject to approval, the date approved by the shareholders.

# Accounting Policies

**(u) Accounting for ESOP Trusts**

The Group has two Employee Share Ownership Plan (ESOP) Trusts which own shares in the Company to enable it to satisfy certain future exercises of share-based awards. The ESOPs are consolidated into the Group's results, with these shares included within retained earnings at cost. Consideration received for such shares is also recognised in retained earnings. No gain or loss is recognised in the performance statements on the purchase, sale, issue or cancellation of equity shares.

**(v) New standards and interpretations not applied**

The International Accounting Standards Board and the International Financial Reporting Interpretations Committee (IFRIC) have issued the following standards and interpretations, relevant to the Group, which have not yet been applied and have an effective date after the date of these financial statements:

| | Effective Date |
|---|---|
| *International Accounting Standards (IAS/IFRS)* | |
| IFRS 4 Insurance Contracts (Amendments to IAS 39 and IFRS 4 – Financial Guarantee Contracts) | 1 January 2006 |
| IFRS 7 Financial Instruments: Disclosures | 1 January 2007 |
| IAS 1 Amendment – Presentation of Financial Statements: Capital Disclosures | 1 January 2007 |
| IAS 39 Amendments to IAS 39 – Transition and Initial Recognition of Financial Assets and Financial Liabilities (Day 1 profits) | 1 January 2006 |
| IAS 39 Cash Flow Hedge Accounting | 1 January 2006 |
| IAS 39 Amendments to IAS 39 and IFRS 4 – Financial Guarantee Contracts | 1 January 2006 |
| *IFRIC* | |
| IFRIC 4 Determining whether an arrangement contains a lease | 1 January 2006 |
| IFRIC 8 Scope of IFRS 2 | 1 May 2006 |
| IFRIC 9 Re-assessment of Embedded Derivatives | 1 June 2006 |

The Directors do not anticipate that the adoption of these standards and interpretations will materially impact the Group's financial statements in the period of initial application. The Group plans to apply the standards and interpretations in the reporting period when they become effective.

Under IFRS 7, the Group will be required to disclose additional information on its financial instruments, their significance, and the nature and extent of their related risks. In particular, more detailed disclosures will be required in connection with the fair values of financial instruments and the Group's risk exposures. As the changes only concern disclosures to be provided, there will be no effect on reported income or net assets.

# Notes to the Consolidated Financial Statements

## 1. Segment reporting

The Group operates as a single asset management business, which does not comprise different business segments, and the Board views the business as a whole as the primary reportable entity.

Although there are several different sources of revenue within the business and distinct distribution channels, and assets under management can be categorised by client type and asset class, the Directors do not consider these to constitute separate business segments within the meaning of IAS 14 'Segment Reporting'. The risks and returns to the Group across these categories are not significantly different, with the fee levels charged reflecting the varying complexities and levels of administration and expertise involved in managing the underlying assets; it is the clients themselves rather than the Group who have the different risk/return profiles. All of the Group's clients are consuming the same service, our only activity – asset management.

The Directors only monitor profitability of the business on a Group-wide basis. Furthermore, geographical considerations aside, the internal operations and management structure are organised on a single overall Group-wide basis, and the basis of remuneration and reward mechanisms are determined in the context of the performance of the whole business.

The Group has given segment information on a geographical basis by location of assets, and in the absence of business segments, has disclosed the geographical segments in the primary reporting format.

By default, primary segment disclosures are also reported for the Group's single business segment – asset management – in the column headed 'Consolidated' in part (a). Secondary format disclosures are given in relation to revenue from external clients by geographical location of clients, as shown in part (b).

The Group is predominantly UK based but has significant operations in three other European countries. The reportable geographical segments are as follows:

- The United Kingdom
- The Netherlands
- Portugal
- The Republic of Ireland

These locations present different risks to the Group, primarily of a legislative and regulatory nature. In order to meet its objectives, and manage risk appropriately, the Group has statutory entities registered in each of these locations. Consequently, the respective statutory entities reflect the reporting which takes place within the Group in that there are identifiable results, assets and liabilities directly attributable to those segments, while representing the broad organisational reporting structure and management of the business.

The reportable geographical segments comprise the legal entities within the Group, registered or incorporated in each of the four respective locations. Details of subsidiary undertakings are given in note 37.

Transfer prices between reportable segments are set on an arm's length basis in a manner similar to transactions with third parties. Segment revenue, segment expense and segment result include transfers between reportable segments. Those transfers are eliminated on consolidation.

During the year, impairment losses have been recognised in respect of management contracts. These intangible assets and their related impairment losses have been associated to geographical segments on the basis of revenues generated from the contracts, proportionately across the various locations. The allocation of the intangible assets' impairment recognised in the Income Statement for the year is shown in part (a).

# Notes to the Consolidated Financial Statements

## 1. Segment reporting (cont'd)

### (a) Geographical segments – by location of assets

| | The United Kingdom | | The Netherlands | | Portugal | | Republic of Ireland | | Other | | Eliminations | | Consolidated | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 (as restated) £000 |
| | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | |
| **Revenue** | | | | | | | | | | | | | | |
| External clients | 233,984 | 170,902 | 52,716 | 7,833 | 12,618 | 2,567 | 3,444 | 974 | 4,203 | 3,527 | – | – | 306,965 | 185,803 |
| Inter-segment sales | 195 | 1,330 | – | – | 1,584 | 1,366 | – | – | – | 13 | (1,779) | (2,709) | – | – |
| **Segment revenue** | 234,179 | 172,232 | 52,716 | 7,833 | 14,202 | 3,933 | 3,444 | 974 | 4,203 | 3,540 | (1,779) | (2,709) | 306,965 | 185,803 |
| **Segment result** | (79,573) | 11,700 | (15,387) | (11,784) | (710) | 3,915 | (2,603) | 116 | 1,966 | 3,535 | (55) | (1,236) | (96,362) | 6,246 |
| Unallocated corporate expenses | | | | | | | | | | | | | – | – |
| **Operating (loss)/profit after restructuring costs** | | | | | | | | | | | | | (96,362) | 6,246 |
| Finance revenue | | | | | | | | | | | | | 15,570 | 4,641 |
| Finance costs | | | | | | | | | | | | | (19,495) | (14,983) |
| Impairment in associates and other financial investments | | | | | | | | | | | | | (5,026) | – |
| Loss on disposal of subsidiary | | | | | | | | | | | | | (672) | – |
| Share of loss of associates | (339) | (318) | – | – | – | – | – | – | – | – | – | – | (339) | (318) |
| Tax income | | | | | | | | | | | | | 29,051 | 873 |
| **Loss for the year** | | | | | | | | | | | | | (77,273) | (3,541) |
| **Other information** | | | | | | | | | | | | | | |
| Segment assets | 1,498,111 | 1,441,979 | 155,348 | 173,797 | 44,651 | 55,892 | 16,643 | 23,500 | 12,026 | 12,036 | (62,054) | (34,751) | 1,664,725 | 1,672,453 |
| Investment in associates | 335 | 4,767 | – | – | – | – | – | – | – | – | – | – | 335 | 4,767 |
| Unallocated corporate assets | | | | | | | | | | | | | 618,876 | 612,184 |
| **Consolidated total assets** | | | | | | | | | | | | | 2,283,936 | 2,289,404 |
| Segment liabilities | (1,198,671) | (1,014,979) | (36,225) | (16,340) | (3,840) | (5,261) | (7,019) | (5,748) | (6) | (4) | 62,054 | 34,751 | (1,183,707) | (1,007,581) |
| Unallocated corporate liabilities | | | | | | | | | | | | | (354,809) | (404,165) |
| **Consolidated total liabilities** | | | | | | | | | | | | | (1,538,516) | (1,411,746) |
| Capital expenditure* (exc. goodwill) | 6,296 | 524,699 | 6 | 73 | – | – | 29 | 18 | – | – | – | – | 6,331 | 524,790 |
| Goodwill acquired (unallocated) | | | | | | | | | | | | | – | 323,915 |
| Depreciation and amortisation | (42,823) | (19,897) | (11,661) | (2,718) | (3,058) | (697) | (955) | (234) | (900) | (205) | – | – | (59,397) | (23,751) |
| Impairment of intangible assets | (70,866) | – | (28,626) | – | (7,522) | – | (2,272) | – | (2,214) | – | – | – | (111,500) | – |
| Non-cash expenses other than depreciation, impairment and amortisation | (52,010) | (35,481) | (976) | 61 | (296) | (25) | (87) | 1 | (1,865) | – | – | – | (55,234) | (35,444) |

* Capital expenditure includes the cots of assets acquired by way of business combination (2004 only).

There were no discontinued operations in 2005 or 2004.

### (b) Revenue by location of clients

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| The United Kingdom | 183,458 | 161,011 |
| The Netherlands | 62,048 | 12,352 |
| Portugal | 23,898 | 3,965 |
| The Republic of Ireland | 13,901 | 877 |
| Other | 23,660 | 7,598 |
| **Consolidated total revenue** | **306,965** | 185,803 |

## 2. Net revenues

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| Investment management fees | **264,403** | 146,597 |
| Performance related management fees | **12,953** | 7,910 |
| **Investment management fees** | **277,356** | 154,507 |
| Interest revenue | **10,370** | 10,310 |
| Dividend revenue | **18,548** | 17,737 |
| **Investment income attributable to policyholders** | **28,918** | 28,047 |
| **Other income** | **691** | 3,249 |
| Renewal commission on open-ended investment products | **(7,911)** | (3,669) |
| Other selling expenses | **(2,984)** | (2,168) |
| **Fee and commission expenses** | **(10,895)** | (5,837) |
| **Total net revenues** | **296,070** | 179,966 |

## 3. Losses on financial instruments carried at fair value through profit or loss

The increase in fair value of investment contract liabilities arises from the following:

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| Net losses on unit linked assets at fair value | **(28,651)** | (27,751) |
| Investment expenses and charges | **1,607** | 2,927 |
| Finance costs | **27** | 6 |
| Tax charges | **559** | 445 |
| Other costs | **50** | – |
| | **(26,408)** | (24,373) |

## 4. Expenses

### (a) Total expenses

Total operating expenses incurred, including restructuring costs, classified by nature, can be summarised as follows:

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| Investment and insurance contracts net expenses | **27,634** | 26,899 |
| Employee benefits and other staff-related expenses | **123,903** | 75,045 |
| Premises expenses | **16,788** | 9,478 |
| Communication and information technology expenses | **13,587** | 7,085 |
| Third party administration expenses | **14,038** | 5,414 |
| Promotional and client servicing expenses | **7,437** | 5,241 |
| Depreciation and amortisation expenses | **59,397** | 23,751 |
| Impairment expenses | **111,500** | 1,988 |
| Other expenses | **18,148** | 18,819 |
| | **392,432** | 173,720 |

### (b) Operating expenses

Operating expenses include the following:

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| Depreciation of owned tangible property, plant and equipment | **3,176** | 2,557 |
| Amortisation of intangible assets – software | **420** | 432 |
| Auditors' remuneration – audit services – UK | **1,287** | 531 |
| Auditors' remuneration – audit services – overseas | **48** | 43 |
| Auditors' remuneration – non-audit services – UK | **887** | 403 |
| Operating lease rentals – land and buildings (sub-leases) | **6,333** | 3,304 |
| Operating lease rentals – land and buildings (head leases) | **4,240** | 3,700 |
| Operating lease rentals – vehicles | **530** | 345 |
| Operating lease rentals – other | **119** | 33 |
| Rentals receivable – operating leases | **(2,257)** | (975) |
| (Gain)/loss on disposals of tangible fixed assets | **(73)** | 40 |
| Foreign exchange losses | **926** | 751 |

Sub-lease rentals of £2,257,000 (2004: £975,000) were received during the year of which £2,134,000 (2004: £975,000) relates to guaranteed payments and £123,000 (2004: £nil) relates to contingent payments.

All amounts within operating lease and sub-lease rental payments relate to minimum lease payments.

## 4. Expenses (cont'd)

### (c) Auditors' remuneration

Fees paid to the Group's auditors, Ernst & Young LLP, are summarised as follows:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Annual audit fees – 2005 | 780 | – |
| Annual audit fees – 2004 | 280 | 574 |
| IFRS conversion project | 275 | – |
| **Statutory audit services** | 1,335 | 574 |
| Further assurance services | 292 | 886 |
| Tax advisory services | 564 | 351 |
| Other non-audit services | 2,840 | 527 |
| **Total non-audit services*** | 3,696 | 1,764 |
| **Total auditors' remuneration** | 5,031 | 2,338 |

* Includes £2,309,000 (2004 – £711,000) which is included within restructuring costs (see note 6a).

During the year to 31 December 2005 non-audit fees of £500,000 (2004 – £650,000) were paid to the auditors for services relating to acquisitions. These fees have been capitalised and are included within expenses of acquisition (see note 16).

The Group's policy on the award of non-audit services to accountancy firms is outlined in the Directors' Report on Corporate Governance. During the year the fees paid by F&C to other accountancy firms for non-audit services were as follows:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| KPMG | 3,441 | 562 |
| PricewaterhouseCoopers | 1,383 | 291 |
| Deloitte & Touche | 17 | 16 |
| | 4,841 | 869 |

In addition to the above, the following fees were paid by OEICs and unit trusts, for which Group companies are the Authorised Corporate Director or Manager, for services provided directly to them:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| PricewaterhouseCoopers | 334 | 246 |

# Notes to the **Consolidated Financial Statements**

## 5. Employee benefits expenses

Total employee benefits expenses including remuneration of the Directors, were:

| | Note | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|---|
| Short-term employee benefits: | | | |
| Salaries and related benefits | | **44,674** | 33,516 |
| Bonus | | **21,770** | 11,176 |
| Wages and salaries | | **66,444** | 44,692 |
| Social Security costs | | **9,687** | 6,444 |
| | | **76,131** | 51,136 |
| Post-employment benefits: | | | |
| Defined contributions scheme expenses | | **3,107** | 4,456 |
| Defined benefits scheme expenses | | **3,419** | 1,526 |
| | | **6,526** | 5,982 |
| **Total of wages and salaries, Social Security costs and post-employment benefits** | | **82,657** | 57,118 |
| Other long-term employee benefits | | **60** | 29 |
| Termination benefits | | **7,627** | 7,085 |
| Share-based payment expenses | 26(b) | **26,344** | 6,783 |
| **Total employee benefits expenses** | | **116,688** | 71,015 |

Included within the above employee benefits expenses is £6,330,000 (2004 – £8,975,000) related to restructuring items as disclosed within note 6a.

The monthly average number of employees (including executive Directors) of the Group during 2005 was 863 (2004 – 604).

## 6. Restructuring costs

### (a) Integration, rationalisation and reorganisation of the business after acquisition of F&C Group (Holdings) Limited

During 2004 the Board initiated a substantial integration, rationalisation and reorganisation of the business after the acquisition of F&C Group (Holdings) Limited (F&CGH Group) on 11 October 2004. This restructuring continued during 2005.

The Directors consider it appropriate to separately disclose the following integration, reorganisation and restructuring costs relating to continuing operations due to the fundamental impact the acquisition had on the management and operational structure of the enlarged Group:

| | 2005<br>£000 | 2004<br>£000 |
|---|---|---|
| Termination and related employee benefits | **6,330** | 8,975 |
| Premises costs | **2,514** | 4,730 |
| Information technology and related costs | **6,081** | 640 |
| Re-branding, administration and client servicing | **2,335** | 364 |
| Consultancy and other costs supporting the restructuring process | **5,145** | 1,635 |
| Impairment of property, plant and equipment | **–** | 1,988 |
| Restructuring costs | **22,405** | 18,332 |
| Tax income in respect of reorganisation costs | **(6,721)** | (5,500) |
| **Net effect of restructuring costs** | **15,684** | 12,832 |

## 6. Restructuring costs (cont'd)

### (b) Operations outsourcing

Following the acquisition of F&CGH Group, Mellon were initially chosen as the preferred investment administration outsource provider of investment operations for the entire Group. As this outsourcing project was expected to change the operating structure of the business, the Directors consider that the restructuring costs associated with outsourcing should be separately disclosed. The Group has subsequently terminated contractual negotiations with Mellon in respect of the former ISIS business. The back office and administration function of the former F&C business continues to use Mellon as an outsource provider.

| | 2005<br>£000 | 2004<br>£000 |
|---|---|---|
| Information technology and related costs | **366** | – |
| Consultancy and other costs supporting the restructuring process | **1,869** | 932 |
| | **2,235** | 932 |
| Tax income in respect of outsourcing costs | **(671)** | (280) |
| **Net effect of operations outsourcing costs** | **1,564** | 652 |

## 7. Finance revenue

| | Note | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|---|
| Bank interest receivable | | **3,365** | 1,699 |
| Other interest receivable | | **1** | 74 |
| Investment income receivable | | **5,840** | – |
| Dividends receivable | | **32** | 9 |
| | | **9,238** | 1,782 |
| Expected return on pension plan assets | 26(a) | **6,332** | 2,859 |
| | | **15,570** | 4,641 |

Investment income receivable primarily represents distributions from interests in private equity investments.

## 8. Finance costs

| | Note | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|---|
| Bank borrowings interest and charges | | **175** | 347 |
| Interest expense payable to Friends Provident group: | | | |
| – £180m term loan | | **10,642** | 10,612 |
| – £50m revolving credit facility | | **434** | 571 |
| – £25m subordinated loan | | **1,466** | 336 |
| – Cumulative Preference Shares | 10(b) | **53** | 32 |
| Interest expense on £9m subordinated loan with Eureko | | **428** | 121 |
| Other interest payable | | **217** | 126 |
| | | **13,415** | 12,145 |
| Interest cost on pension liabilities | 26(a) | **6,080** | 2,838 |
| | | **19,495** | 14,983 |

# Notes to the Consolidated Financial Statements

## 9. Income tax

### (a) Analysis of tax income in the year

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| **Consolidated income statement** | | |
| **Current income tax:** | | |
| UK | **10,817** | 5,802 |
| Overseas | **10,249** | 1,298 |
| Adjustments in respect of previous years | **(1,640)** | 312 |
| **Deferred income tax:** | | |
| Relating to origination and reversal of temporary differences | **(49,810)** | (7,861) |
| Adjustments in respect of previous years | **1,333** | – |
| Transfers from unrecognised tax assets | **–** | (424) |
| **Tax income reported in the consolidated income statement** | **(29,051)** | (873) |
| **Consolidated statement of changes in equity** | | |
| **Deferred and current income tax related to items charged or credited directly to equity:** | | |
| Share-based payments | **672** | (479) |
| (Loss)/gain on financial investments | **(68)** | 198 |
| Actuarial loss on defined benefit pension schemes | **(9,201)** | (874) |
| **Tax income recognised directly in equity** | **(8,597)** | (1,155) |

### (b) Factors affecting the tax income for the year

A reconciliation between the actual tax income and the product of accounting loss multiplied by the Group's domestic tax rate for the years ended 31 December 2005 and 2004 is as follows:

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| Loss before tax | **(106,324)** | (4,414) |
| At the Group's statutory income tax rate of 30.0% (2004: 30.0%) | **(31,897)** | (1,324) |
| Adjustments in respect of previous years | **(307)** | 312 |
| Disallowed expenses | **1,917** | 971 |
| Non-taxable income | **(265)** | (55) |
| Deferred tax asset not previously recognised | **–** | (714) |
| Overseas tax | **634** | (63) |
| Utilisation of unrecognised losses | **(1,309)** | – |
| Share-based payments | **2,176** | – |
| **Tax income reported in the consolidated income statement** | **(29,051)** | (873) |

Deferred income tax details are shown in note 18.

## 10. Dividends

### (a) Ordinary dividends

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Declared and paid during the year** | | |
| Equity dividends on Ordinary Shares: | | |
| Final dividend for 2004: 7.0p (2003: 7.0p) | **32,952** | 10,487 |
| Interim dividend for 2005: 4.0p (2004: 4.0p) | **18,865** | 5,993 |
| | **51,817** | 16,480 |
| **Proposed for approval at the Annual General Meeting (not recognised as a liability as at 31 December)** | | |
| Equity dividends on Ordinary Shares: | | |
| Final dividend for 2005: 7.0p (2004: 7.0p) | **33,381** | 32,914 |

The entitlement to receive dividends (on its holding of F&C shares) held by the Group's ESOPs has been waived by the Trustees.

This has resulted in the following dividends being waived:

| | F&C Group ESOP | | Abacus Trust | |
|---|---|---|---|---|
| | Shares | £000 | Shares | £000 |
| **2004 Dividends** | | | | |
| 2003 Final | 469,700 | 33 | – | – |
| 2004 Interim | 469,700 | 19 | – | – |
| **2005 Dividends** | | | | |
| 2004 Final | 969,700 | 68 | 10,665,706 | 747 |
| 2005 Interim | 890,200 | 36 | 5,791,630 | 232 |

### (b) Non-equity dividends on Cumulative Preference Shares

| | 2005 £000 | 2004 £000 |
|---|---|---|
| **Interest expense during the year** | **53** | 32 |

## 11. Earnings per Share

Basic earnings per share amounts are calculated by dividing net profit/(loss) for the period attributable to ordinary equity holders of the parent by the weighted average number of Ordinary Shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net profit/(loss) for the period attributable to ordinary equity holders of the parent by the weighted average number of Ordinary Shares outstanding during the year plus the weighted average number of Ordinary Shares that would be issued on the conversion of all the dilutive potential Ordinary Shares into Ordinary Shares.

In the opinion of the Directors the profit before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan more accurately reflects the underlying earnings performance of the Group.

**Reconciliation of Earnings per Share**

| | 2005 Basic p | 2005 Diluted p | 2004 (as restated) Basic p | 2004 (as restated) Diluted p |
|---|---|---|---|---|
| Loss per Ordinary Share | **(16.36)** | **(15.77)** | (1.60) | (1.56) |
| Amortisation of intangibles, net of tax | **8.27** | | 6.56 | |
| Cost of the Re-Investment Plan, net of tax | **3.82** | | 1.71 | |
| Restructuring costs, net of tax: | | | | |
| – Reorganisation post acquisition of F&CGH Group | **3.32** | | 5.80 | |
| – Operations outsourcing | **0.33** | | 0.29 | |
| Impairment of intangibles, net of tax | **16.52** | | – | |
| **Earnings per Ordinary Share before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan*** | **15.90** | | 12.76 | |

* Defined as 'underlying earnings per share'

### 11. Earnings per Share (cont'd)

The following reflects the income and share capital data used in the basic and diluted earnings per share calculations:

**Income**

| | Notes | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|---|
| Loss attributable to ordinary equity holders of the parent for basic loss per share | | (77,273) | (3,541) |
| Amortisation of intangibles, net of tax | | 39,061 | 14,533 |
| Cost of the Re-Investment Plan, net of tax | | 18,025 | 3,799 |
| Restructuring costs, net of tax: | | | |
| – Reorganisation post acquisition of F&CGH Group | 6a | 15,684 | 12,832 |
| – Operations outsourcing | 6b | 1,564 | 652 |
| Impairment of intangibles, net of tax | | 78,050 | – |
| **Profit attributable to ordinary equity holders of the parent before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan** | | 75,111 | 28,275 |

**Share capital**

| | 2005 No. | 2004 (as restated) No. |
|---|---|---|
| Weighted average number of Ordinary Shares (excluding treasury shares) for basic loss per share | 472,408,007 | 221,546,388 |
| Dilutive potential Ordinary Shares: | | |
| Weighted average number of 1995 ESOS options exercisable | 3,105 | 4,252 |
| Weighted average number of 2002 ESOS options exercisable | 880,389 | 1,331,840 |
| Weighted average number of Share Save Scheme options exercisable | 278,082 | 493,454 |
| Weighted average number of The Re-Investment Plan options exercisable | 15,210,652 | 3,292,544 |
| Weighted average number of The Long Term Remuneration Plan options exercisable | 986,064 | – |
| Weighted average number of Purchased Equity Plan options exercisable | 206,945 | – |
| **Dilutive potential weighted average number of Ordinary Shares** | 489,973,244 | 226,668,478 |

Certain employees, who have left the Group, are entitled to exercise their 1995 or 2002 Executive Share Options for a defined period in accordance with scheme rules. Where the option prices are below the average share price for the year, these options have been treated as dilutive. The remaining 1995 and 2002 Executive Share Options have not been treated as dilutive during the above years because the performance criteria have not yet been achieved to enable the options to be exercised, except for those options which were dilutive as a result of "good leavers".

Transactions involving Ordinary Shares or potential Ordinary Shares between the reporting date and the date of approval of the Consolidated Financial Statements were as follows: 969,931 share options have been exercised during this period and have been satisfied by the issue of ordinary share capital.

**Potential future dilution**

The Group operates several share-based payment schemes which could potentially dilute basic earnings per share in the future but were not included in the calculation of diluted earnings per share because they were anti-dilutive for the years presented. Note 26(b) discloses the number of awards which are outstanding for each scheme at 31 December 2005.

The share-based payment schemes must meet the relevant performance criteria for each scheme before the exercise of options is possible. The only exception to this is for "good leavers", where there is usually a period of time over which the employees can exercise their options in accordance with the specific treatment of "good leavers" under the rules of each scheme regardless of whether the performance criteria have been met.

The options for all the awards in the 1995 Executive Share Option Scheme vested on 24 March 2006 as the performance criteria had been met. These 2,693,131 options outstanding, at exercise prices between 203.83-455.83p, are now potentially dilutive as settlement would be made by the issue of new shares.

In addition, the options granted on 19 March 2003 under the 2002 Executive Share Option Scheme vested on 24 March 2006 as the performance criteria of the 2002 Executive Share Option Scheme had been met. These 2,729,971 options outstanding, at an exercise price of 139.00p, are now potentially dilutive as settlement would be made by the issue of new shares.

## 12. Property, plant and equipment

| | Leasehold improvements £000 | Motor vehicles £000 | Office furniture and equipment £000 | Computer equipment £000 | Total £000 |
|---|---|---|---|---|---|
| **Cost:** | | | | | |
| At 1 January 2004 (as restated) | 6,538 | 41 | 2,925 | 8,321 | 17,825 |
| Additions on acquisition of F&CGH Group | 1,383 | 117 | 1,127 | 919 | 3,546 |
| Additions | 3,065 | – | 309 | 594 | 3,968 |
| Disposals | – | (57) | – | (54) | (111) |
| At 31 December 2004 (as restated) | 10,986 | 101 | 4,361 | 9,780 | 25,228 |
| Additions | 1,388 | 85 | 153 | 1,901 | 3,527 |
| Disposals | (3,423) | (23) | (2,057) | (2,668) | (8,171) |
| Foreign exchange losses | – | (10) | – | (39) | (49) |
| **At 31 December 2005** | **8,951** | **153** | **2,457** | **8,974** | **20,535** |
| **Depreciation and impairment:** | | | | | |
| At 1 January 2004 (as restated) | 1,393 | 41 | 1,856 | 6,552 | 9,842 |
| Impairment losses | 1,988 | – | – | – | 1,988 |
| Depreciation charge for the year | 629 | 11 | 567 | 1,350 | 2,557 |
| Disposals | – | (17) | – | (54) | (71) |
| At 31 December 2004 (as restated) | 4,010 | 35 | 2,423 | 7,848 | 14,316 |
| Depreciation charge for the year | 975 | 57 | 615 | 1,529 | 3,176 |
| Disposals | (3,423) | (14) | (2,054) | (2,666) | (8,157) |
| Foreign exchange gains | – | (6) | – | (36) | (42) |
| **At 31 December 2005** | **1,562** | **72** | **984** | **6,675** | **9,293** |
| **Net book values:** | | | | | |
| At 31 December 2003 (as restated) | 5,145 | – | 1,069 | 1,769 | 7,983 |
| At 31 December 2004 (as restated) | 6,976 | 66 | 1,938 | 1,932 | 10,912 |
| **At 31 December 2005** | **7,389** | **81** | **1,473** | **2,299** | **11,242** |

There are no restrictions on the Group's title to the above assets and none are pledged as security for liabilities.

The cost of fully depreciated property, plant and equipment which is still in use at 31 December 2005 is £4,185,000 (31 December 2004: £7,598,000).

**Impairment of property, plant and equipment**

In 2004, the leasehold improvements in respect of the Group's former head office at Wood Street, London were impaired after the decision was made to relocate the Group's head office to Exchange House, London.

# Notes to the **Consolidated Financial Statements**

### 13. Goodwill and other intangible assets

| | Note | Goodwill £000 | Management contracts £000 | Other intangible assets – software and licences £000 | Total £000 |
|---|---|---|---|---|---|
| **Cost:** | | | | | |
| At 1 January 2004 (as restated) | | 254,031 | 104,300 | 4,643 | 362,974 |
| Intangibles arising on acquisition of F&CGH Group | 16(b) | 323,915 | 516,940 | 65 | 840,920 |
| Additions | | – | – | 271 | 271 |
| Foreign exchange gains | | – | 4,990 | – | 4,990 |
| At 31 December 2004 (as restated) | | 577,946 | 626,230 | 4,979 | 1,209,155 |
| Additions | | – | 1,249 | 1,555 | 2,804 |
| Disposals | | – | – | (2,359) | (2,359) |
| Foreign exchange losses | | – | (7,630) | (91) | (7,721) |
| **At 31 December 2005** | | **577,946** | **619,849** | **4,084** | **1,201,879** |
| **Amortisation and impairment:** | | | | | |
| At 1 January 2004 (as restated) | | – | 15,645 | 4,041 | 19,686 |
| Amortisation for the year | | – | 20,762 | 432 | 21,194 |
| At 31 December 2004 (as restated) | | – | 36,407 | 4,473 | 40,880 |
| Amortisation for the year | | – | 55,801 | 420 | 56,221 |
| Disposals | | – | – | (2,359) | (2,359) |
| Impairment losses | | – | 111,500 | – | 111,500 |
| Foreign exchange losses | | – | – | (91) | (91) |
| **At 31 December 2005** | | **–** | **203,708** | **2,443** | **206,151** |
| **Net book values:** | | | | | |
| At 31 December 2003 (as restated) | | 254,031 | 88,655 | 602 | 343,288 |
| At 31 December 2004 (as restated) | | 577,946 | 589,823 | 506 | 1,168,275 |
| **At 31 December 2005** | | **577,946** | **416,141** | **1,641** | **995,728** |

Goodwill arose on business combinations and relates to the business as a whole following the fundamental integration, rationalisation and reorganisations which took place after each acquisition. As such, goodwill is not allocated to cash generating units below the overall entity level. Goodwill has been tested for impairment at the balance sheet date, as described below. As from 1 January 2004, the Group's date of transition to IFRS, goodwill is no longer amortised but subject to annual impairment testing. The accumulated impairment losses at 31 December 2005 relating to goodwill were £nil (2004 – £nil).

## 13. Goodwill and other intangible assets (cont'd)

Management contracts predominantly relate to contracts arising from business acquisitions, following the restatement of goodwill on transition to IFRS. Their descriptions, carrying amounts at the year-end, and remaining amortisation periods are as follows:

| | 31 December 2005 | | 31 December 2004 | |
|---|---|---|---|---|
| | Net book values £000 | Remaining amortisation period | Net book values £000 | Remaining amortisation period |
| RSAI insurance contracts | **32,500** | **6 years** | 37,500 | 7 years |
| RSAI retail contracts | **35,295** | **6 years** | 40,725 | 7 years |
| F&C insurance contracts | **108,465** | **9 years** | 124,259 | 10 years |
| F&C institutional contracts | **105,963** | **9 years** | 182,457 | 10 years |
| F&C investment trust contracts | **55,713** | **19 years** | 117,768 | 20 years |
| F&C advisory and sub-advisory contracts | **61,631** | **9 years** | 69,997 | 10 years |
| F&C OEICs | **15,366** | **9 years** | 17,117 | 10 years |
| | **414,933** | | 589,823 | |

The balance of management contracts relates to a private equity fund of funds mandate acquired from Martin Currie Limited during 2005, which has a carrying value of £1,208,000, with 19 years amortisation period remaining.

The accumulated impairment losses at 31 December 2005 relating to management contracts were £111,500,000 (2004 – £nil).

### Impairment testing of goodwill and intangible assets with finite lives

#### Goodwill

The recoverable amount of goodwill has been determined based on a value in use calculation using cash flow projections based on the latest annual financial budget approved by the Board.

The discount rate applied to cash flow projections is 8.9%. This is based on the Group's weighted average cost of capital, calculated as at 31 December 2005, and takes into account the relative risks associated with the Group's various revenue streams.

Revenue projections for the first year equate to the Board-approved budget for 2006. Beyond this, revenues have been projected to grow at 6% per annum which is in line with the Group's long-term view of market growth, and consistent with that experienced over the last 15 years across the markets in which assets are invested. In addition, net new business of £100,000,000 per annum at a fee rate of 60 basis points per annum has been assumed relating to retail funds, based on a conservative estimate of future net inflows and on past experience. Revenues earned from significant contracts with a fixed term are assumed to terminate at the end of the fixed term, with operating costs falling by an amount which assumes associated profit margins of 70%.

Operating costs for the first year of the projection are driven by the budgeted Group profit margin for 2006. Thereafter, costs have been grown at a minimum rate of 3.5% per annum, to accord with estimated future inflation and salary increases, with the margin capped at 45% as a measure of prudence, based on historical performance.

A terminal value has been calculated and added to the calculated net present value in order to ascertain an overall value in use of the business. The recoverable value is then compared to the carrying value of goodwill, management contracts and other intangible assets, net of associated deferred tax liabilities, and property, plant and equipment in order to ascertain whether any impairment exists. The Directors consider the terminal value to reflect fairly the long-term nature of the business and the Board's current view that there is no reason to believe that the business will not continue ad infinitum.

As this annual impairment review of goodwill determined a surplus, no impairment has been recognised in the year in respect of goodwill.

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Carrying amount of goodwill | **577,946** | 577,946 |

# Notes to the Consolidated Financial Statements

**13. Goodwill and other intangible assets (cont'd)**

The key assumptions referred to above, to which the calculated value in use is most sensitive, are as follows:

| | 2005 | 2004 |
|---|---|---|
| Discount rate | 8.9% | 8.5% |
| Revenue growth rate | 6.0% | 6.0% |
| Cost inflation rate | 3.5% | 3.5% |
| Capped operating margin | 45.0% | – |

In order to assess the sensitivity of the key assumptions on the carrying value of goodwill, an analysis was conducted to ascertain the change that would be required to derive a recoverable amount which approximated to the carrying value of goodwill.

The absolute levels of the discount rate, the revenue growth rate or the cost inflation rate which most closely equated to a match in the recoverable amount and carrying value of goodwill were 11.8%, 4.1% and 5.7% respectively.

**Intangible assets with finite lives**

During 2005, due to indifferent investment performance in some areas of the business and some clients withdrawing assets for strategic reasons following changes in their own corporate structure, the business experienced a level of fund outflows which was higher than anticipated and led to certain net new business targets not being met. The level of lost business will have a notable impact on revenues and was significant enough to be considered an indicator of potential impairment of certain intangible assets, namely the related investment management contracts.

In accordance with IAS 36 'Impairment of Assets', a full impairment review of these assets was undertaken. The review resulted in impairment losses being recognised in respect of management contracts as follows:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| F&C investment trust contracts | 56,100 | – |
| F&C institutional contracts | 55,400 | – |
| **Total impairment recognised in the Consolidated Income Statement** | **111,500** | – |

The above contracts relate to the investment trust management contracts and institutional fund management contracts acquired as a result of the business combination of the ISIS and F&CGH Groups on 11 October 2004.

The recoverable amounts of the assets have been determined based on value in use calculations using cash flow projections based on the latest annual financial budget approved by the Board.

The discount rate applied to the cash flow projections is 9.4% for investment trust contracts, 9.4% for institutional contracts with no fixed term, and 8.4% for fixed term institutional contracts. These rates reflect the varying risks and uncertainties inherent in the revenues from the underlying assets, using the Group's weighted average cost of capital of 8.9%, calculated as at 31 December 2005, as a benchmark.

The revenue projections have been grown at 6% per annum, in line with the Group's long-term view of market growth, and consistent with that experienced over the last 15 years across the markets in which the managed assets are invested. The revenue projections also incorporate an estimated loss rate of 5% per annum compounded over the projected period in respect of investment trusts, and 14% per annum for institutional contracts with no fixed term.

Operating costs for the first year of the projections are driven by the budgeted Group profit margin for 2006. Thereafter, costs are driven by the Group's projected operating margins, as determined for the purposes of the goodwill impairment review, with the margin capped at 45% as a measure of prudence, based on historical performance.

Impairment has been determined by comparing the results of the value in use calculations in respect of the remaining contracts at the year-end to the carrying value (cost less aggregate amortisation) of the assets at 31 December 2005, with any deficits arising constituting impairment to be recognised for the year.

There were no indicators of potential impairment of intangible assets with finite lives in respect of the comparative period, and as such, no impairment review was performed for 2004.

## 14. Other financial investments

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Quoted | **27** | 28 |
| Unquoted | **3,370** | 4,167 |
| | **3,397** | 4,195 |

Unquoted investments include the Group's direct investment, co-investments and carried interest entitlement in private equity limited partnerships. These are designated as available for sale investments, as disclosed in note 19(a)(iii).

Included within the unquoted financial investments at 31 December 2005 are £1,285,000 (31 December 2004: £1,854,000) of equity instruments measured at the price of recent investments.

The Group received distributions totalling £4,836,000 (2004: £nil) which comprised £4,704,000 of investment income and £132,000 return of capital.

Included in the movement in unquoted investments during the year is an impairment charge of £469,000 (2004: £nil). Taken together with the impairment losses in respect of associates of £4,557,000, as shown in note 15 below, this gives a total impairment in investments of £5,026,000 in 2005 (2004: £nil).

## 15. Investment in associates

The Group has two investments in associate entities. It has an investment in Cardinal Capital Partners Limited (Cardinal), an alternative investment business involved in hedge funds. F&C acquired a 15% stake in this business during 2004. The other investment is in ISIS EP LLP (LLP), which acquired the private equity business that until 30 June 2005 was owned entirely by the Group. F&C has a 19.99% stake in this business. Further details are given below:

| Name of company | Place of incorporation and operation | Proportion of ownership | Proportion of voting power held | Method used to account for investment |
|---|---|---|---|---|
| ISIS EP LLP | England | 19.99% | 19.99% | Equity method |
| Cardinal Capital Partners Limited | The Republic of Ireland | 15% | 15% | Equity method |

The movements in the aggregate carrying amount of investments in associates is analysed below:

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| At 1 January | **4,767** | – |
| Additions in the year | **509** | 5,101 |
| Share of loss for the year | **(339)** | (318) |
| Foreign exchange (losses)/gains | **(45)** | 83 |
| Share of post-acquisition expenses charged to equity | **–** | (99) |
| Impairment losses | **(4,557)** | – |
| **At 31 December** | **335** | 4,767 |

# Notes to the Consolidated Financial Statements

### 15. Investment in associates (cont'd)

**The Group's share of the aggregate total of assets, liabilities, revenues and profits/(losses) of associates is set out below:**

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Share of associates' balance sheet:** | | |
| Current assets | **1,509** | 1,531 |
| Non-current assets | **121** | 22 |
| Current liabilities | **(795)** | (180) |
| Non-current liabilities | **(500)** | – |
| **Net assets** | **335** | 1,373 |

| | 2005 £000 | 2004 £000 |
|---|---|---|
| **Share of the associates' revenues and losses:** | | |
| Revenues | **1,490** | – |
| Loss | **(339)** | (318) |

**The Group's investment in associates comprises:**

| | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|
| – Group share of net assets | **335** | 1,373 |
| – Loan to associate | **2,500** | – |
| | **2,835** | 1,373 |

#### (a) Investment in ISIS EP LLP

Prior to June 2005, the Group's private equity operation comprised a team of fund managers operating a number of management contracts of limited partnerships and VCTs within the statutory entity ISIS Equity Partners plc (ISIS), a 100% owned subsidiary of the Group. ISIS was also the parent of a number of limited companies which acted as Founder Partner (FP) and General Partners (GP) to these private equity limited partnerships. Neither F&C nor ISIS had any interest in the limited partnerships other than as FP or GP and at no point was either an investor in the limited partnerships.

In June 2005, the ISIS private equity operation comprising net assets of £223,000 was sold to ISIS EP LLP (LLP). The fund management team formerly employed by the F&C Group left to form LLP. Those former employees that did not become members of LLP became employees of LLP. As well as acquiring the companies that acted as GP and FP, all investment management contracts relating to the limited partnerships and VCTs were transferred to LLP.

The consideration received was a nominal amount of cash plus 19.99% of LLP's voting A class ordinary capital. In addition, F&C subscribed £2.5m for non-voting, non-participating B class capital in LLP, in order that LLP had sufficient regulatory capital. The proceeds from the B capital are maintained in a designated bank account by LLP and any bank interest earned on that account accrues to F&C as a dividend on B capital. This investment is classified as a loan to associate.

Despite the fact that the other 80.01% of the A voting capital is held by five LLP members, one of whom holds 40.1% and has significant contractual powers over LLP, the Board consider LLP to be an associate as there is ability to exert significant influence and affect policy and decision making through the appointment of one out of six members of the Management board.

LLP is a private Limited Liability Partnership which is not listed on any public exchange.

### 15. Investment in associates (cont'd)

Under the terms of the Partnership Deed, F&C are entitled to a share of profit from LLP based on a cascade calculation of both a fixed and variable element of any profit arising, after priority has been given to the fixed share of profit attributable to the other members of the partnership. Accordingly, the Group's 19.99% interest in LLP may not equate to the actual profit entitlement in any year.

The investment in LLP has been written down to reflect only the share of profit entitlement for 2005, as the Directors consider that significant doubt exists as to whether future profits will accrue to the Group.

LLP is required to maintain sufficient regulatory capital in order to comply with the Financial Services Authority's (FSA) rules on financial resources requirements. As such, any distribution of profit to investors can only be executed if sufficient regulatory capital will remain after the distribution has been made.

#### (b) Investment in Cardinal Capital Partners Limited

The Group has a 15% interest in Cardinal, which is a hedge fund manager based in Ireland. Cardinal is a private Limited Liability Partnership which is not listed on any public exchange. While the Group holds only 15% of the share capital of Cardinal it is considered that it is possible to exercise significant influence in the operations of the partnership as the Group had board membership, continues to have entitlement to board membership and also has privileged distribution access to Cardinal products in the UK and continental Europe. Consequently, the holding is accounted for as an associate.

The original investment in Cardinal entitled the Group to a 15% equity stake. However, as at 31 December 2004, the Group's share of net assets equated to less than the carrying value of the investment in this associate company, reflecting the goodwill paid for this investment.

During 2005 the Directors made the decision to channel all relevant business through its own inhouse capability and as such no assets were placed with Cardinal for management. As a result of this decision the directors considered it appropriate to fully provide against the investment and as such the investment in Cardinal has been written down to nil (including the goodwill paid) as at 31 December 2005. As a result, an impairment loss of £4,048,000 has been recognised in 2005.

# Notes to the Consolidated Financial Statements

## 16. Acquisition and disposal of subsidiaries

### (a) 2004 – Acquisition of F&C Group (Holdings) Limited (as restated for the implementation of IFRS)

F&C Asset Management plc (previously ISIS Asset Management plc) acquired and gained control of F&C Group (Holdings) Limited and its subsidiaries ('F&CGH Group') on 11 October 2004. The F&CGH Group is a pan-European asset management business. The business combination has been accounted for as an acquisition.

F&C Asset Management plc acquired the share capital of the following companies on acquisition:

| Company | Percentage of issued share capital acquired |
|---|---|
| F&C Group (Holdings) Limited | 100% |
| F&C Portugal Gestao, de Patrimonios SA | 100% |
| F&C Netherlands BV | 100% |
| F&C Ireland Limited | 100% |
| Lackingdon Limited | 100% |
| AF – Investimentos Internacional SA | 100% |
| F&C Alternative Investments (Holdings) Limited (formerly F&C MMP Holdings Limited) | 100% |
| F&C Partners LLP | 60% |
| F&C Group Management Limited (formerly Primrose Street Holdings Limited) | 100% |
| F&C Retail Limited | 100% |
| F&C Holdings Limited | 100% |
| ESN PMG (Services) Limited | 100% |
| F&C Investment Services Limited | 100% |
| F&C (CI) Limited | 100% |
| F&C Private Equity Nominees Limited | 100% |
| F&C Property Investment Management Limited | 100% |
| F&C Property Investment (Services) Limited | 100% |
| F&C Management Limited | 100% |
| F&C Nominees Limited | 100% |
| F&C Investment Management Limited | 100% |
| F&C Overseas Limited | 100% |
| Cerebys Limited | 100% |
| F&C Channel Islands Limited | 100% |
| F&C Unit Management Limited | 100% |
| F&C Management (Jersey) Limited | 100% |
| FCEM Holdings (UK) Limited | 100% |
| F&C Emerging Markets Limited | 100% |
| Latin American Securities Limited | 100% |
| F&C Emerging Markets (India) Limited | 100% |

The F&CGH Group was acquired from Eureko B.V. for an initial consideration of 320,374,763 ordinary shares. The share price on 11 October 2004 was £2.30 and the fair value of the initial consideration was £736,862,000.

## 16. Acquisition and disposal of subsidiaries (cont'd)

The new Ordinary Shares issued by F&C Asset Management plc upon Completion (11 October 2004) were allocated as follows:

(i) 145,365,679 shares were issued to Friends Provident at a price of £2.30 to ensure that Friends Provident maintained a 51% holding in Ordinary Shares on Completion. In return for the new shares Friends Provident paid Eureko Holdings £250,000,000 in cash and issued 92,433,278 new Friends Provident shares to Eureko Holdings.

(ii) 99,283,053 shares were issued to Eureko Holdings at a price of £2.30 on Completion. This issue resulted in Eureko holding just over 20% of the share capital of the Company on Completion.

(iii) 75,726,031 shares were issued to Eureko Holdings at a price of £2.30, which Eureko immediately placed in the market on Completion. This placing ensured that over 25% of Ordinary Shares of the Company were held in public hands on Completion.

In addition, 11,021,961 shares were issued to the Employee Benefit Trust at a price of £2.30. From an accounting perspective, this issue was not considered part of the consideration price, but satisfied the initial rights of F&C executives and staff under the Re-Investment Plan.

Prior to Completion, Friends Provident subscribed for £410,000 of new Preference Shares, allowing Friends Provident to maintain its existing proportionate holding of the nominal share capital of the Company following Completion, as shown in note 30(c).

Under the terms of the Sale and Purchase Agreement (SPA), F&C Asset Management plc was entitled to receive net assets of £65,900,000 (Net Asset Value Target). Following agreement of the Completion Accounts, a £ for £ adjustment was made to the initial consideration, to the extent that the Net Asset Value Target exceeded or fell short by in excess of £1 million, to reflect the agreed net asset position at Completion.

An estimated further consideration of £16,212,000 was outstanding on the acquisition as the net assets per the Completion Accounts were greater than £65,900,000. This additional consideration was due to be settled in cash and was accrued at 31 December 2004.

All inter-company balances between the F&C group and the Eureko B.V. group at Completion were settled in cash outwith the transaction.

The estimated acquisition expenses associated with the transaction, including stamp duty, were £13,200,000 of which £578,000 was accrued at 31 December 2005 (2004: £1,202,000).

The purchase of all the companies in the F&CGH Group was part of the same transaction with Eureko B.V. As a result the fair value table was produced for the entirety of the arrangement as this most accurately reflected the nature of the transaction.

The provisional goodwill arising on the acquisition was capitalised and is required to be tested annually for impairment.

**Effect of acquisition**

As at 31 December 2004, the Directors considered the fair values of the net assets as at the acquisition date to be provisional, until the F&CGH Group Completion Accounts review process was finalised. The values adopted as fair values of the net assets of the acquired companies at the date of acquisition reflected the best estimates available to the Directors at the time of preparation of the accounts for the year ended 31 December 2004.

# Notes to the **Consolidated Financial Statements**

### 16. Acquisition and disposal of subsidiaries (cont'd)

The provisional fair value of the net assets acquired were:

| | Book value on acquisition £000 | Adjustments: Reclassification adjustments (as restated) £000 | Adjustments: Fair value adjustments (as restated) £000 | Provisional fair value to the Group at acquisition, as at 31 December 2004 (as restated) £000 |
|---|---|---|---|---|
| **Non-current assets** | | | | |
| Property, plant and equipment | 3,611 | (65) | – | 3,546 |
| Intangible assets: | | | | |
| – Management contracts | – | – | 516,940 | 516,940 |
| – Other intangible assets | – | 65 | – | 65 |
| Financial investments | 1,424 | – | – | 1,424 |
| Deferred acquisition costs | – | – | 818 | 818 |
| Deferred tax assets | 15,578 | 1,772 | 3,089 | 20,439 |
| **Current assets** | | | | |
| Stock of units and shares | 19 | – | – | 19 |
| Trade and other receivables | 59,708 | – | (3,172) | 56,536 |
| Cash and cash equivalents – shareholders | 133,371 | – | (580) | 132,791 |
| **Non-current liabilities** | | | | |
| Interest bearing loans and borrowings | (9,000) | – | – | (9,000) |
| Pension deficit | (348) | (3,370) | (3,465) | (7,183) |
| Deferred income | (3,631) | – | – | (3,631) |
| Provisions | (2,231) | – | – | (2,231) |
| Deferred tax liabilities | – | – | (155,082) | (155,082) |
| **Current liabilities** | | | | |
| Trade and other payables | (112,139) | 1,598 | (1,311) | (111,852) |
| Deferred income | – | – | (1,149) | (1,149) |
| Net assets acquired | 86,362 | – | 356,088 | 442,450 |
| Goodwill arising | | | | 323,824 |
| **Provisional consideration** | | | | 766,274 |
| **Discharged by:** | | | | |
| Initial consideration – fair value of shares issued | | | | 736,862 |
| Estimated further consideration payable | | | | 16,212 |
| Estimated expenses of acquisition | | | | 13,200 |
| | | | | 766,274 |

There were no provisions for reorganisation or restructuring initiatives included in the liabilities of the acquired entities.

The following specific adjustments were made to reflect the fair value of assets acquired on acquisition:

- The defined benefit pension plan assets of the F&CGH Group were adjusted to reflect their market value at Completion.
- The fair values of the defined benefit pension obligations were amended to reflect the IAS 19 assumptions adopted by the Group.
- Cash and cash equivalent balances were adjusted to reflect the exchange rate at Completion and debtors balances were reduced to their estimated realisable value.
- The increase in creditors reflects obligations of the acquired entities which were considered to exist as at Completion, but which were not reflected in the Completion Accounts.
- Tax adjustments were made to the balances on acquisition to reflect the tax effect of the non-tax fair value adjustments.

As the acquired entities did not constitute a statutory group for the whole period of 2004 prior to the date of the acquisition, it is not practical to present the revenue or profit of the F&CGH Group for the entirety of 2004, as if the acquisition had been effected as at 1 January 2004.

## 16. Acquisition and disposal of subsidiaries (cont'd)

### (b) 2005 – Acquisition of F&C Group (Holdings) Limited

The table at (a) above presents the provisional fair value of the net assets acquired on acquisition of the F&CGH Group as at 31 December 2004.

During 2005, following the review of the Completion Accounts and subsequent agreement with Eureko B.V. regarding adjustments to the purchase consideration, the table below presents the additional adjustments made in 2005 to determine the final fair value of assets acquired on acquisition:

| | Provisional fair value to the Group at acquisition, as at 31 December 2004 (as restated) £000 | Additional fair value adjustments £000 | Final fair value to the Group at acquisition £000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | 3,546 | – | 3,546 |
| Intangible assets: | | | |
| – Management contracts | 516,940 | – | 516,940 |
| – Other intangible assets | 65 | – | 65 |
| Financial investments | 1,424 | 467 | 1,891 |
| Deferred acquisition costs | 818 | – | 818 |
| Deferred tax assets | 20,439 | – | 20,439 |
| **Current assets** | | | |
| Stock of units and shares | 19 | – | 19 |
| Trade and other receivables | 56,536 | (3,027) | 53,509 |
| Current tax recoverable | – | 1,000 | 1,000 |
| Cash and cash equivalents – shareholders | 132,791 | – | 132,791 |
| **Non-current liabilities** | | | |
| Interest bearing loans and borrowings | (9,000) | – | (9,000) |
| Pension deficit | (7,183) | – | (7,183) |
| Deferred income | (3,631) | – | (3,631) |
| Provisions | (2,231) | (3,661) | (5,892) |
| Deferred tax liabilities | (155,082) | – | (155,082) |
| **Current liabilities** | | | |
| Trade and other payables | (111,852) | (8,140) | (119,992) |
| Deferred income | (1,149) | – | (1,149) |
| Net assets acquired | 442,450 | (13,361) | 429,089 |
| Goodwill arising | 323,824 | 91 | 323,915 |
| **Consideration** | 766,274 | (13,270) | 753,004 |
| **Discharged by:** | | | |
| Initial consideration – fair value of shares issued | 736,862 | – | 736,862 |
| Estimated further consideration payable | 16,212 | (13,270) | 2,942 |
| Expenses of acquisition (of which £578,000 is accrued) | 13,200 | – | 13,200 |
| | 766,274 | (13,270) | 753,004 |

IFRS 3 'Business Combinations' requires fair value adjustments to be reflected as if they had been determined as at the date of the acquisition. As a result, the fair value adjustments made during 2005, in respect of balances as at 11 October 2004, have necessitated the restatement of certain balances as at 31 December 2004.

## 16. Acquisition and disposal of subsidiaries (cont'd)

These additional fair value adjustments are explained below:

- Financial investments have been increased to reflect the fair value of the acquired Group's interest in private equity investments.
- Trade and other receivables have been reduced to their estimated realisable values at Completion.
- Provisions have been increased to reflect the Directors' assessment of onerous property contracts and the cost of providing benefits to employees on long-term sickness leave.
- Trade and other payables have been increased to reflect additional obligations of the acquired entities which are considered to exist at 11 October 2004, but which were not fully reflected in the Completion Accounts.
- Adjustments have been made to reflect the tax effect of the non-tax fair value adjustments, together with an additional provision in respect of tax obligations in existence as at 11 October 2004, as a result of the submission of prior period tax computations.
- The additional consideration recognised at 31 December 2004 has been reduced by £13,270,000 to reflect the reduction in the expected total consideration payable for the F&CGH Group. Accordingly, the consideration liability of £16,212,000 disclosed and accrued in the 2004 Annual Report and Accounts has been reduced to £2,942,000 and restated accordingly.

### (c) 2005 – Disposal of subsidiaries

During the year, the Group disposed of several subsidiary companies and incurred the following losses on disposal:

| | 2005<br>£000 | 2004<br>£000 |
|---|---|---|
| Loss on disposal of Baronsmead Ventures Limited | (449) | – |
| Loss on sale of subsidiaries to ISIS EP LLP* | (223) | – |
| | (672) | – |

* ISIS EP LLP is an associate of the Group. Details are given in note 15(a).

## 17. Deferred acquisition costs

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| At 1 January | 10,374 | 8,146 |
| Acquired on acquisition of F&CGH Group | – | 818 |
| Costs deferred in the year | 3,167 | 3,134 |
| Amortisation in the year | (2,181) | (1,724) |
| **At 31 December** | 11,360 | 10,374 |

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| **Split as follows:** | | |
| Non-current assets | 8,342 | 7,808 |
| Current assets | 3,018 | 2,566 |
| **At 31 December** | 11,360 | 10,374 |

## 18. Deferred income tax

Deferred income tax relates to the following:

| | Consolidated balance sheet 31 December 2005 £000 | Consolidated balance sheet 31 December 2004 (as restated) £000 | Consolidated income statement 2005 £000 | Consolidated income statement 2004 (as restated) £000 |
|---|---|---|---|---|
| **Deferred tax assets** | | | | |
| Employee benefits* | **17,127** | 9,447 | **(1,428)** | (4,244) |
| Share-based payments | **9,141** | 2,862 | **(6,950)** | (2,034) |
| Unused tax losses and unused tax income | **4,723** | 13,441 | **8,718** | 4,343 |
| Property, plant and equipment | **1,633** | 2,223 | **590** | (188) |
| Receivables, payables and provisions | **1,459** | 2,250 | **791** | 491 |
| | **34,083** | 30,223 | | |
| **Deferred tax liabilities** | | | | |
| Intangible assets | **(124,480)** | (176,948) | **(50,178)** | (6,229) |
| Revaluation of unrealised fair value gains on available for sale assets | **(625)** | (693) | | |
| Unremitted earnings | **(190)** | – | **190** | – |
| Other short term timing liabilities | **–** | (322) | **(210)** | – |
| | **(125,295)** | (177,963) | | |
| **Deferred tax income** | | | **(48,477)** | (7,861) |

* Includes £14,410,000 (2004: £5,312,000) relating to deferred tax on the defined benefit pension obligations.

The Directors believe it is appropriate to recognise a deferred tax asset because it is considered that it is probable that there will be suitable taxable profits from which the underlying timing differences can be deducted.

Deferred tax has been provided on the unremitted earnings of the Group's foreign operations to the extent that it is planned for these companies to distribute profits in the foreseeable future.

**Factors that may affect future tax charges**

The Group has unrecognised tax losses which arose in the UK of £1,352,000 (2004: £5,716,000) that are available indefinitely for offset against future taxable profits of the companies in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as they cannot be used to offset taxable profits elsewhere in the Group and they have arisen in companies that have been loss making for some time.

## 19. Financial instruments

### (a) Analysis of balance sheet assets

Financial investments held in relation to the activities of the Group's insurance subsidiary have been classified at fair value through profit or loss within current assets.

Stocks of units and shares are held in relation to fund management activities and are classified as held for trading current assets.

Financial investments included within non-current assets are classified as available for sale and are carried at fair value (or amortised cost if fair value cannot be measured reliably). Loans receivable included within non-current assets are carried at amortised cost.

### (i) Designated as fair value through profit or loss

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Financial investments in respect of unit linked contracts | **980,777** | 813,595 |
| Other financial investments | **2,166** | – |
| | **982,943** | 813,595 |

**19. Financial instruments (cont'd)**

| | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|
| **Financial investments in respect of unit linked contracts** | | |
| **Equity securities** | | |
| Listed | **721,192** | 601,962 |
| Unit trusts and OEICs | **1,260** | 724 |
| **Total equity securities** | **722,452** | 602,686 |
| **Debt and fixed income securities** | | |
| Government bonds | **81,780** | 81,554 |
| Other listed fixed interest securities | **94,687** | 61,329 |
| Index linked gilts | **21,225** | 15,279 |
| Participation in pooled investments | **60,633** | 52,747 |
| **Total debt and fixed income securities** | **258,325** | 210,909 |
| **Total financial investments designated as fair value through profit or loss** | **980,777** | 813,595 |

The movements in financial assets designated as fair value through profit or loss in respect of unit linked contracts are as follows:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| At 1 January | **813,595** | 855,188 |
| Additions | **669,668** | 575,515 |
| Sales and redemptions | **(595,157)** | (665,935) |
| Movement in fair value of unrealised gains and losses | **92,671** | 48,827 |
| **At 31 December** | **980,777** | 813,595 |

**Other financial investments**

| | 2005 £000 | 2004 £000 |
|---|---|---|
| At 1 January | **–** | – |
| Additions | **2,166** | – |
| **At 31 December** | **2,166** | – |

Other financial investments are investments in equities made via a trust for the purpose of funding NIC on the Deferred Investment Plan. The provision for NIC is separately recognised.

**Financial instruments relating to unit linked contracts**

The Group's insurance subsidiary provides unit linked pension wrappers which avail clients of a number of benefits from these pooled arrangements. From F&C's perspective, the risks and rewards of managing these assets are the same as other assets under management as the financial risks and rewards attributable to the assets invested also fall to be borne by, or to the benefit of, our clients. Hence, while a number of significant financial instruments are recognised in the Balance Sheet in respect of this subsidiary, the key risk to the Group is the impact of the level of management fees which are earned from this entity which are directly impacted by the underlying value of policyholder assets. While by necessity this Group subsidiary company has some insurance risks, these risks are completely reinsured, thereby negating any ultimate insurance risk to the Group's equity holders.

## 19. Financial instruments (cont'd)

The amounts included in the Consolidated Balance Sheet in respect of assets and liabilities held within unit linked funds are as follows:

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Listed equity securities | **721,192** | 601,962 |
| Unit trusts and OEICs | **1,260** | 724 |
| Debt and other fixed income securities | **197,692** | 158,162 |
| Participation in pooled investments | **60,633** | 52,747 |
| Deferred acquisition costs | **634** | 634 |
| Trade and other receivables | **77** | 1,154 |
| Cash and cash equivalents | **28,152** | 47,145 |
| Trade and other payables | **(2,712)** | (220) |
| **Total unit linked assets less liabilities** | **1,006,928** | 862,308 |

These unit linked assets are matched by the associated insurance contract liabilities disclosed in note 28.

The assets above are all unit linked and held for the sole benefit of the policyholders within F&C Managed Pension Funds Limited. Investment and credit risk in respect of assets and liabilities held within unit linked funds is borne by the policyholders.

### (ii) Designated as held for trading

| | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|
| Stock of units and shares | **676** | 556 |

The Group holds a stock of shares and units in respect of its OEIC and unit trust business. This stock of shares and units is commonly referred to as the 'Manager's Box'. The Group's stock of shares and units is valued using quoted market values. The Group is therefore exposed to market value movements in the value of these assets.

### (iii) Designated as available for sale investments

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Shares – unlisted | **3,370** | 4,167 |
| Shares – listed | **27** | 28 |
| | **3,397** | 4,195 |

Available for sale financial assets consist of investments in ordinary shares and private equity investments.

The fair value of the unlisted available for sale investments has been estimated using a valuation technique based on assumptions that are not supported by observable market prices or rates. The Directors believe that the estimated fair values resulting from the valuation technique which are recorded in the Balance Sheet, and the related realised fair values gains recorded in the Income Statement are reasonable and the most appropriate at the balance sheet date. These investments have no fixed maturity date or coupon rate.

Certain unlisted equity instruments are measured at the price of a recent investment as the fair value of these equity instruments cannot be measured reliably. Details of these investments are disclosed in note 14.

£25,000 (2004: £26,000) of listed shares have a fixed coupon rate of 4.875% and a maturity date in 2007. The shares are stated at market value.

## 19. Financial instruments (cont'd)

### (b) Fair values

Set out below is a comparison by category of carrying amounts and fair values of all the Group's financial instruments that are carried in the financial statements.

| | Carrying amount | | Fair value | |
|---|---|---|---|---|
| | 31 December 2005 | 31 December (as restated) 2004 | 31 December 2005 | 31 December (as restated) 2004 |
| **Financial assets** | | | | |
| Other financial investments | **3,397** | 4,195 | **3,397** | 4,195 |
| Loan to associate | **2,500** | – | **2,430** | – |
| Financial investments at fair value through profit or loss | **982,943** | 813,595 | **982,943** | 813,595 |
| Reinsurance assets | **2,617** | 2,352 | **2,617** | 2,352 |
| Stock of units and shares | **676** | 556 | **676** | 556 |
| Cash and cash equivalents | **146,197** | 181,084 | **146,197** | 181,084 |
| **Financial liabilities** | | | | |
| Interest bearing loans and borrowings: | | | | |
| Revolving credit facilities | **(5,000)** | (5,000) | **(5,000)** | (5,000) |
| Floating rate borrowings | **(34,000)** | (34,000) | **(34,000)** | (34,000) |
| Fixed rate borrowings | **(180,000)** | (180,000) | **(181,080)** | (181,500) |
| Preference Shares (classified as liabilities) | **(800)** | (800) | **(744)** | (800) |
| Investment contract liabilities | **(1,006,928)** | (862,308) | **(1,006,928)** | (862,308) |
| Insurance contract liabilities | **(2,617)** | (2,352) | **(2,617)** | (2,352) |

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the table:

**Securities**

The fair value of listed investments is based on quoted market prices at the balance sheet date without any deduction for transaction costs.

The fair value of unlisted investments have been valued in accordance with International Private Equity and Venture Capital Valuation Guidelines and in accordance with the underlying Limited Partnership Agreements where possible.

**Interest bearing loans and non-equity shares**

The fair value of borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates. The valuations have considered similar issues available in the market and the liquidity of assets and liabilities.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate for a similar instrument at the balance sheet date. Where other pricing models are used, inputs are based on market related data at the balance sheet date.

## 20. Reinsurance assets

| | 31 December 2005 £000 | 31 December (as restated) 2004 £000 |
|---|---|---|
| Reinsurers' share of annuities | **2,617** | 2,352 |
| **Total reinsurance assets** | **2,617** | 2,352 |
| Current reinsurance assets | **2,617** | 2,352 |
| Non-current reinsurance assets | **–** | – |
| **Total reinsurance assets** | **2,617** | 2,352 |

The reinsurance assets relate to annuity business reinsured with FP Pensions Limited.

## 21. Trade and other receivables

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Current:** | | |
| Trade debtors | **24,203** | 6,420 |
| Accrued income | **43,366** | 30,683 |
| Other debtors | **16,520** | 16,989 |
| Prepayments | **5,186** | 8,979 |
| Amounts owed by Eureko group | **3,583** | – |
| | **92,858** | 63,071 |

Trade receivables are non-interest bearing and are generally receivable within 30 days.

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Non-current:** | | |
| Loan to associate | **2,500** | – |

The Group subscribed £2.5 million for non-voting, non-participating B class capital in ISIS EP LLP, an associate company, in order to ensure that ISIS EP LLP has sufficient regulatory capital. These proceeds are held in a designated bank account by ISIS EP LLP and all bank interest earned on that account accrues to the Group as a dividend on B capital. The loan is redeemable on the withdrawal by the Group from ISIS EP LLP and therefore, there is no fixed redemption date for this loan. The Group retains the right to withdraw from the LLP and to require other members of the LLP to immediately purchase all of the Group interest in the LLP. The consideration receivable will be deferred and only receivable by the Group on the third anniversary of the date of withdrawal.

## 22. Cash and cash equivalents

| | 31 December 2005 £000 | 31 December (as restated) 2004 £000 |
|---|---|---|
| **Policyholders** | | |
| Cash at bank and in hand | **4,047** | 2,848 |
| Short-term deposits | **24,105** | 44,297 |
| | **28,152** | 47,145 |
| **Shareholders** | | |
| Cash at bank and in hand | **17,675** | 52,155 |
| Short-term deposits | **100,370** | 81,784 |
| | **118,045** | 133,939 |
| **Total cash and cash equivalents** | **146,197** | 181,084 |

Cash and cash equivalents are held by the Group for the purpose of meeting short-term cash commitments rather than for investment or other purposes. All items above are readily convertible to a known amount of cash and are not subject to significant risk of changes in value.

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods of between one day and no longer than three months depending on the immediate cash requirements of the Group and earn interest at the respective short-term deposit rates. The fair value of cash and cash equivalents at 31 December 2005 is £146,197,000 (2004: £181,084,000).

**Restrictions on use of cash**

The policyholders' cash is not available for use by the Group. These funds are held on behalf of policyholders of unit linked insurance contracts which are consolidated within the results of the Group. At 31 December 2005 this amounted to £28,152,000 (2004: £47,145,000) of the total cash and cash equivalents balance.

**22. Cash and cash equivalents (cont'd)**

**Borrowing facilities**

The Group has various borrowing facilities available to it. The undrawn committed facilities available at the year-end in respect of which all conditions precedent had been met at that date are as follows:

| | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|
| **Expiring in one year or less:** | | |
| Revolving credit facility with Friends Provident | **45,000** | 45,000 |
| Bank overdraft facilities | **2,000** | 6,100 |
| | **47,000** | 51,100 |

**23. Interest bearing loans and borrowings**

The contractual terms of the Group's interest bearing loans and borrowings are as follows:

**Contractual terms**

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Cumulative Preference Shares:<br>– Dividends are set at LIBOR + 2% and are payable each half-year in arrears<br>– Preference Shares' rights are fully described in note 30 | **800** | 800 |
| £180m term loan with Friends Provident Life and Pensions Limited, a subsidiary of Friends Provident plc.<br>– Fixed rate of 5.9125%<br>– Wholly repayable on 1 November 2006 | **180,000** | 180,000 |
| £50m revolving credit facility with Friends Provident plc<br>– £5m drawn down, at 3 month Sterling LIBOR plus 0.6% margin<br>– Any drawdown under this facility is repayable within 3 months but can be rolled over by the borrower into a subsequent drawdown. This option remains until 30 May 2007. | **5,000** | 5,000 |
| £25m subordinated loan with Friends Provident Life and Pensions Limited<br>– At 6 months LIBOR + 1.05%<br>– Wholly repayable on 11 October 2009 | **25,000** | 25,000 |
| £9m subordinated loan with Eureko B.V.<br>– At 6 months LIBOR + 1.05%<br>– Wholly repayable on 11 October 2009 | **9,000** | 9,000 |
| | **219,800** | 219,800 |

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Repayment periods** | | |
| Amounts repayable: | | |
| In one year or less, or on demand | **185,000** | 5,000 |
| In more than one year but not more than two years | **–** | 180,000 |
| In more than two years but not more than five years | **34,000** | 34,000 |
| In more than five years | **800** | 800 |
| | **219,800** | 219,800 |

## 23. Interest bearing loans and borrowings (cont'd)

The £180,000,000 loan falls due for repayment on 1 November 2006. The Board intends to re-finance the loan and is currently at an advanced stage in the process of appointing advisors to support this debt re-financing. In the unlikely circumstances that F&C is unable to re-finance its £180 million loan facility on normal commercial terms in the external market due to market or other factors at the time of re-financing, Friends Provident has given an undertaking to the F&C Board that it would be willing to provide either a facility or a bridging facility until such time as F&C refinances the loan.

For more information about the Group's exposure to interest risk, see note 35.

## 24. Trade and other payables

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Amounts due within one year:** | | |
| Trade creditors | **5,150** | 2,671 |
| Amounts owed to Friends Provident group | **1,900** | 2,405 |
| Amounts owed to Eureko group | **–** | 316 |
| VAT | **1,479** | 767 |
| Social Security and PAYE | **1,292** | 1,989 |
| Other creditors | **25,119** | 18,044 |
| Group relief payable to subsidiary of ISIS EP LLP | **378** | – |
| Accruals | **23,406** | 35,082 |
| | **58,724** | 61,274 |
| **Amounts due outwith one year:** | | |
| Other creditors | **–** | 3 |
| | **–** | 3 |

Trade creditors are non interest bearing and are normally settled in accordance with the individual contractual arrangements.

## 25. Provisions

| | Premises – onerous contracts £000 | Guaranteed product £000 | NIC on share options £000 | Long-term sickness £000 | VAT – launch profits £000 | Long-term service award £000 | Total £000 |
|---|---|---|---|---|---|---|---|
| At 1 January 2004 (as restated) | 3,570 | – | 56 | – | 310 | – | 3,936 |
| Additions on acquisition of F&CGH Group | 4,141 | – | – | 1,751 | – | – | 5,892 |
| Provided during the year | 4,684 | 457 | 274 | – | – | 171 | 5,586 |
| Utilised during the year | (2,248) | – | – | – | – | – | (2,248) |
| Reversed during the year | – | – | – | – | (310) | – | (310) |
| **At 31 December 2004 (as restated)** | 10,147 | 457 | 330 | 1,751 | – | 171 | 12,856 |
| Provided during the year | 5,139 | 14 | 4,452 | – | – | – | 9,605 |
| Provision utilised during the year | (2,195) | (178) | (507) | – | – | (1) | (2,881) |
| Reversed during the year | – | – | – | (91) | – | (66) | (157) |
| **At 31 December 2005** | **13,091** | **293** | **4,275** | **1,660** | **–** | **104** | **19,423** |
| **At 31 December 2005** | | | | | | | |
| Non-current | **9,750** | **227** | **1,387** | **1,492** | **–** | **104** | **12,960** |
| Current | **3,341** | **66** | **2,888** | **168** | **–** | **–** | **6,463** |
| At 31 December 2004 (as restated) | | | | | | | |
| Non-current | 7,952 | 279 | 330 | 1,591 | – | 170 | 10,322 |
| Current | 2,195 | 178 | – | 160 | – | 1 | 2,534 |

### 25. Provisions (cont'd)

**Onerous contracts**

The Group holds all properties under operating leases. This includes a number of vacant and sub-let properties which were either previously occupied by the Group or are partially occupied by the Group. Provision has been made for the residual lease commitments where significant, after taking into account existing and expected sub-tenant arrangements. The remaining terms are for up to 17 years, although a significant element of this provision relates to lease incentive arrangements and is expected to be utilised within 3 years. Assumptions have been made as to whether each leasehold property may be sub-let or assigned in the future. All leases, and the majority of sub-leases, are for minimum guaranteed rentals. One sub-lease involves the possible receipt of contingent rent. Any contingent rent received in excess of the anticipated amount is recognised as income during the period. The provision is subject to uncertainties over time including market rent reviews and break-options within the lease arrangements.

**Guaranteed product**

The provision for the guaranteed product represents the actuarially assessed cost of meeting potential obligations under certain investment products which have a guaranteed payout in the event of death of the investor. This provision is subject to uncertainties in respect of movements in market levels and the death of underlying investors. The underlying investment plan was closed to new investors during 2004.

**NIC on share options**

The provision for National Insurance Contributions (NIC) on share options represents the potential NIC liability in respect of a number of share-based payment schemes operated by the Group. The provision is subject to uncertainties in respect of movements in the Company's share price, the extent to which options lapse and, where eligible, the timing of when employees choose to exercise options. The current element provision for NIC on share options related to awards which are expected to vest within one year. As disclosed in note 19 other financial investments at 31 December 2005 of £2,166,000 (31 December 2004: £nil) can partially offset the NIC liability on the Deferred Investment Plan.

**Long-term service award**

This provision represents the non-current obligation in respect of long-term service benefits to which employees are entitled, including future holiday entitlement and long-term service awards.

**Long-term sickness**

The cost of certain employees who are on long-term absence are self-assured by the Group. The provisions represent the present value of income protection payments due to these individuals.

This provision has been quantified on the assumption that all employees currently on long-term sick leave do not return to the employment of the Group. The discount rate and salary growth assumptions used in each year are identical to those used for the purposes of determining defined benefit pension obligations.

The Group has long-term sickness insurance arrangements which cover the potential absence from work of all current employees.

### 26. Employee benefits

**(a) Pension scheme obligations**

Following the merger with F&C Group (Holdings) Limited in 2004, the Group operates two defined benefit schemes in the United Kingdom and participates in one in Portugal. Both of the UK schemes are closed to new entrants. All new UK employees are eligible to benefit from defined contribution arrangements, which provide greater certainty over the future cost to the Group.

Where the Group is unable to separately identify its share of assets and liabilities in overseas multi-employer defined benefit schemes, then these schemes are accounted for as defined contribution arrangements. Employees in The Netherlands and Ireland participate in multi-employer pension arrangements. The Netherlands scheme is still open to new employees. Plans are currently being finalised to set up separate defined benefit pension schemes in respect of employees in The Netherlands and Ireland including the assessment of any final transfer value receivable from Eureko. These new arrangements will maintain the existing benefits currently enjoyed by employees in these locations and will be funded by the transfer of assets from the current multi-employer schemes.

The Chairman of the Group, Mr R W Jenkins, was awarded pension benefits by F&C Management Limited prior to completion of the merger in respect of his past service to the F&C Group. Mr Jenkins has been awarded a pension of £100,000 per annum, commencing on his 60th birthday. The pension will be indexed in line with the Retail Price Index on 1 January each year from the date of the merger. The Group has not earmarked any assets to date with respect to this liability.

The pension obligations are recognised under non-current liabilities in the Balance Sheet and are stated gross of the related deferred tax asset.

The results of the latest full actuarial valuations were updated at 31 December 2005 by qualified independent actuaries.

## 26. Employee benefits (cont'd)

**Disclosure relating to the Group's defined benefit obligations**

**Plan assets and expected rate of return**

| Plan assets | 31 December 2005 £000 | % | 31 December 2004 (as restated) £000 | % |
|---|---|---|---|---|
| Equities | **85,942** | **74** | 73,568 | 76 |
| Gilts | **14,767** | **13** | 14,738 | 15 |
| Corporate bonds | **12,682** | **11** | 5,567 | 6 |
| Cash | **2,706** | **2** | 2,891 | 3 |
| **Total fair value of plan assets** | **116,097** | **100** | 96,764 | 100 |

The plan assets do not include Ordinary Shares issued by the Company or Friends Provident plc.

Expected long-term rates of return applied to all funded defined benefit obligations are as follows:

| | 31 December 2005 | 31 December 2004 |
|---|---|---|
| Equities | **7.00%** | 7.00% |
| Gilts | **5.00%** | 5.00% |
| Corporate bonds | **4.70%** | 5.30% |
| Cash | **4.00%** | 4.00% |

**Basis used to determine the expected rate of return on plan assets**

To develop the expected long-term rate of return on assets assumption, the Group considered the current level of expected returns on risk free investments (primarily government bonds), the historical level of risk premium associated with the other asset classes in which the portfolio is invested and the expectations for the future returns of each asset class. The expected return for each asset class was then weighted based on the target asset allocation to develop the expected long-term rate of return on assets assumption for the portfolio.

**Mortality assumptions**

The mortality assumptions used for both of the main UK defined benefit schemes at 31 December are:

| | 2005 | 2004 |
|---|---|---|
| Mortality table for males retiring in the future | **PMA92B1965MC – 1** | PMA92base – 3 |
| Mortality table for females retiring in the future | **PFA92B1965MC – 1** | PFA92base – 3 |
| Mortality table for current male pensioners | **PMA92B1935MC – 1** | PMA92base |
| Mortality table for current female pensioners | **PFA92B1935MC – 1** | PFA92base |

**Impact of mortality assumptions**

To demonstrate what these mortality assumptions mean, the expected ages at death of members retiring at age 60 are as follows:

| | 31 December 2005 Years | 31 December 2004 Years |
|---|---|---|
| Expected age at death for a male retiring in the future at age 60 | **88** | 84 |
| Expected age at death for a female retiring in the future at age 60 | **91** | 87 |
| Expected age at death for a current male pensioner aged 60 | **86** | 81 |
| Expected age at death for a current female pensioner aged 60 | **89** | 84 |

### 26. Employee benefits (cont'd)

The table below summarises the cost of providing annuities of £1 per annum (with associated death benefits and pension increases) for members aged 60 based on the assumptions used for the pension disclosures as at 31 December:

**Cost of annuities**

| | 2005 £ | 2004 £ |
|---|---|---|
| Male annuity | **24.70** | 20.40 |
| Female annuity | **25.20** | 20.90 |

These rates assume a monthly payments model with a discount rate of 4.70% (2004: 5.30%) based on the iBoxx over 15 year AA corporate bond index of 4.73% (2004: 5.29%). The rates also assume 2/3rds of the members' benefit will be paid to the spouse, a 5-year guarantee is provided and pensions in excess of GMP will increase by 2.75% per annum.

The mortality rates were strengthened as part of the 31 March 2005 actuarial valuation for the ISIS Asset Management plc Pension Fund. The Directors believe that the strengthened mortality assumptions more accurately reflect the liabilities of the schemes and have adopted the same assumptions for both of the main UK defined benefit schemes.

The UK pension schemes have changed their mortality assumptions to the medium cohort basis for 2005. The mortality assumptions have been projected forward, to take account of future improvements in mortality, using a 'typical' year of birth of 1965 for all future pensioners and 1935 for all current pensioners, rather than on an individual basis.

For 2004, PM/FA92 tables were used for mortality assumptions with no projection forward for future improvements in mortality and rated down by 3 years for future pensioners.

The cost of strengthening the mortality in 2005 was approximately £18,000,000.

The profile of the current membership of defined benefit arrangements in the Group are as follows:

| | 31 December 2005 | | 31 December 2004 | |
|---|---|---|---|---|
| | % of total membership | Average age | % of total membership | Average age |
| Current active members | **22%** | **42** | 24% | 41 |
| Deferred members | **68%** | **41** | 67% | 41 |
| Current pensioners | **10%** | **64** | 9% | 65 |
| | **100%** | | 100% | |

The profile of the liabilities of defined benefit arrangements throughout the Group are as follows:

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Current active members | **51,514** | 42,775 |
| Deferred members | **75,876** | 44,297 |
| Current pensioners | **36,739** | 27,399 |
| | **164,129** | 114,471 |

## 26. Employee benefits (cont'd)

The range of assumptions used to determine benefit obligations are as follows:

| | 31 December 2005 | 31 December 2004 (as restated) |
|---|---|---|
| Discount rate | **4.25% – 4.70%** | 5.25% – 5.30% |
| Rate of salary increase | **2.75% – 4.00%** | 2.75% – 4.00% |
| Rate of inflation increase | **1.75% – 2.75%** | 1.75% – 2.75% |

The range of assumptions used to determine net pension cost for the year are as follows:

| | 2005 | 2004 |
|---|---|---|
| Discount rate | **5.25 – 5.30%** | 5.40 – 5.50% |
| Expected long-term return on plan assets | **5.50 – 6.60%** | 5.50 – 6.60% |
| Rate of salary increase | **2.75 – 4.00%** | 1.75 – 4.00% |

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Change in benefit obligation** | | |
| Benefit obligation at 1 January | **114,471** | 37,453 |
| Foreign exchange movements | **(28)** | – |
| Fair value of obligation on acquisition | **–** | 68,547 |
| Current service cost | **2,905** | 1,526 |
| Interest cost on pension liabilities | **6,080** | 2,838 |
| Members' contributions | **173** | 124 |
| Past service cost* | **514** | – |
| Actuarial (gains)/losses | **42,270** | 4,639 |
| Net transfers (out)/in | **(196)** | 28 |
| Benefits paid | **(2,060)** | (684) |
| **Benefit obligation at 31 December** | **164,129** | 114,471 |

*The past service cost relates to the augmentation of pension entitlement in respect of Mr I Paterson Brown, as disclosed on page 55.

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Analysis of defined benefit obligation** | | |
| Plans that are wholly or partly funded | **161,859** | 112,706 |
| Plans that are wholly unfunded | **2,270** | 1,765 |
| | **164,129** | 114,471 |

## 26. Employee benefits (cont'd)

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Change in plan assets** | | |
| Fair value of plan assets at 1 January | **96,764** | 29,655 |
| Foreign exchange movements | **(27)** | – |
| Fair value of assets on acquisition | **–** | 61,364 |
| Expected return on plan assets | **6,332** | 2,859 |
| Actuarial gains/(losses) | **11,536** | 1,730 |
| Net transfers (out)/in | **(196)** | 28 |
| Employer contributions | **3,575** | 1,688 |
| Member contributions | **173** | 124 |
| Benefits paid | **(2,060)** | (684) |
| **Fair value of plan assets at 31 December** | **116,097** | 96,764 |

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| Funded status | **(48,032)** | (17,707) |
| **Net deficit recognised** | **(48,032)** | (17,707) |

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Components of pension cost** | | |
| Current service cost | **2,905** | 1,526 |
| Past service cost | **514** | – |
| Interest cost on pension liabilities | **6,080** | 2,838 |
| Expected return on pension plan assets | **(6,332)** | (2,859) |
| **Total pension cost recognised in the Income Statement** | **3,167** | 1,505 |

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Pension costs are included in the Income Statement as follows:** | | |
| Operating expenses | **3,419** | 1,526 |
| Finance revenue | **(6,332)** | (2,859) |
| Finance costs | **6,080** | 2,838 |
| **Total pension cost recognised in the Income Statement** | **3,167** | 1,505 |

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Actuarial (gains)/losses immediately recognised in the SORIE** | **30,734** | 2,909 |
| **The cumulative actuarial (gains)/losses recognised in the SORIE** | **33,643** | 2,909 |

| | 2005 £000 | 2004 £000 |
|---|---|---|
| **Actual return on plan assets** | **17,868** | 4,589 |

## 26. Employee benefits (cont'd)

### Five year history

| | 2005 £000 | 2004 (as restated) £000 | 2003* £000 | 2002* £000 | 2001* £000 |
|---|---|---|---|---|---|
| Benefit obligation at 31 December | **(164,129)** | (114,471) | (37,453) | (33,364) | (31,416) |
| Fair value of plan assets at 31 December | **116,097** | 96,764 | 29,655 | 24,833 | 31,980 |
| (Deficit)/surplus | **(48,032)** | (17,707) | (7,798) | (8,531) | 564 |
| **Difference between expected and actual return on plan assets** | | | | | |
| Amount (£000) | **11,536** | 1,730 | 2,168 | (9,116) | (5,879) |
| Percentage of plan assets | **10%** | 2% | 7% | (37%) | (18%) |
| **Experience gains and losses on scheme liabilities** | | | | | |
| Amount (£000) | **(413)** | (500) | 22 | 1,265 | (600) |
| Percentage of scheme liabilities | **–%** | –% | –% | 4% | (2%) |
| **Total gains and losses** | | | | | |
| Amount (£000) | **(30,734)** | (2,909) | 753 | (8,012) | (4,904) |
| Percentage of scheme liabilities | **(19%)** | (3%) | 2% | (24%) | (16%) |

* On an FRS17: Retirement Benefits basis.

The post-retirement deficits by obligation can be summarised as follows:

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| F&C Management Pension Fund | **23,034** | 6,571 |
| ISIS Asset Management Pension Fund | **22,364** | 9,283 |
| F&C Portugal pension obligation | **364** | 88 |
| R W Jenkins pension obligation | **2,270** | 1,765 |
| | **48,032** | 17,707 |

The increase in the deficits has arisen primarily as a result of the strengthening of the mortality assumptions used and the reduction in discount rates between 31 December 2004 and 31 December 2005.

**Pension scheme details**

**ISIS Asset Management plc Pension Fund**

| | |
|---|---|
| Date of last actuarial valuation | 31 March 2005 |
| Scheme Actuary | Mercer Human Resource Consulting Limited |
| Method of valuation | Projected Unit |
| Market value of assets at last valuation date | £33,550,000 |
| Level of funding | 80% |

A contribution schedule was agreed by the Company and trustees in May 2003. The Company has paid contributions of £100,000 per month from May 2003 with an additional payment of £400,000 in May 2003. The Company has agreed to pay monthly contributions of a minimum of one-twelfth of the annual amount of 25% of basic salaries until April 2008. These contributions are subject to review at future actuarial valuations, the next one of which is due no later than 31 March 2008. The results of the 31 March 2005 valuation are currently being considered by the Fund's trustees and the Group. The minimum estimated amounts of contributions expected to be paid into the scheme during the current financial year is £1,200,000.

As the ISIS Asset Management plc Pension Fund is a closed scheme, under the projected unit method the current service cost will tend to increase as a percentage of pensionable salaries as the average age of members increases.

# Notes to the Consolidated Financial Statements

## 26. Employee benefits (cont'd)

**F&C Management Limited Pension Plan**

| | |
|---|---|
| Date of last actuarial valuation | 31 March 2003 |
| Scheme Actuary | Hewitt, Bacon & Woodrow |
| Method of valuation | Projected Unit |
| Market value of assets at last valuation date | £37,300,000 |
| Level of funding | 63% |

A contribution schedule was agreed by the participating Company and trustees in December 2003. The Company has agreed to contribute 22.8% of pensionable salary to the pension fund until June 2007, when a revised schedule of contributions will be agreed. These contributions are subject to review at future actuarial valuations, the next one of which is due no later than 31 March 2006. The estimated amounts of contributions expected to be paid into the scheme during the current financial year is £1,500,000.

As the F&C Management Limited Pension Plan is a closed scheme, under the projected unit method the current service cost will tend to increase as a percentage of pensionable salaries as the average age of members increases.

**Multi-employer defined benefit schemes**

**F&C Portugal**

Certain employees in Portugal participate in the multi-employer scheme Fundo de Pensoes do Grupo Banco Commercial Português. The assets and liabilities of the scheme are separately identifiable.

The Group participates in two other multi-employer defined benefit schemes in Europe. The following schemes are defined benefit schemes but the employers are unable to identify their share of the underlying assets and liabilities. In particular, the assets of the scheme are not separately identifiable as they are managed in totality and F&C's share of these assets has not been determined with Eureko. The employers are accounting for the contributions to the scheme as if they were defined contribution schemes:

**(1) F&C Netherlands BV**

Certain staff in The Netherlands participate in the Achmea Pension Plan.

| | 31 December 2005 | | 31 December 2004 | |
|---|---|---|---|---|
| | £000 | €000 | £000 | €000 |
| Plan deficit | **282,417** | **411,030** | 247,030 | 349,000 |

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | £000 | €000 | £000 | €000 |
| F&C contributions | **639** | **930** | 220 | 315 |

**(2) F&C Ireland Limited**

Certain staff in Ireland participate in the Friends First Retirement and Death Benefits Plan.

| | 31 December 2005 | | 31 December 2004 | |
|---|---|---|---|---|
| | £000 | €000 | £000 | €000 |
| Plan deficit | **4,672** | **6,800** | 3,469 | 4,900 |

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | £000 | €000 | £000 | €000 |
| F&C contributions | **69** | **101** | 17 | 25 |

As a result of the merger of ISIS and F&C in 2004, employees in The Netherlands and Ireland will no longer be able to continue to participate in the existing multi-employer plans. It is expected that new pension arrangements will be set up in Ireland and The Netherlands during 2006. When these new schemes are set up there will be greater certainty over the level of surpluses or deficits in these schemes attributable to the F&C Group. Under the terms of the Sale and Purchase Agreement, the Group has a contractual protection such that the maximum pension deficit it could inherit upon the set-up of the above plans is €500,000. The execution of this contractual obligation is expected to impact the value of the assets transferred to these new, separate schemes.

## 26. Employee benefits (cont'd)

**Cost of defined contribution plans (including restructuring costs)**

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| Group personal pension plans | **2,030** | 1,423 |
| Other defined contribution schemes | **1,077** | 3,073 |
| | **3,107** | 4,496 |

The Group had £163,000 of pension contributions outstanding as at 31 December 2005 (2004: £44,000).

### (b) Share-based payments

The Group operates several share-based payment arrangements as part of its total employee remuneration package. The details of each scheme are disclosed below.

#### (i) 2002 Executive Share Option Scheme

The 2002 Executive Share Option Scheme was activated in March 2003. For each award the exercise price is equal to the average quoted market price of the Company's shares on the three days immediately preceding the date of grant. The vesting period for each award is three years and options are settled by an allotment of shares to individuals. No cash alternative is available.

If the options remain unexercised after a period of 10 years from the date of award, the options expire. Furthermore, options are forfeited if the employee leaves the Group before the options vest. Employees who are deemed "good leavers" are entitled to exercise their options for a period of one year after they leave, dependent on the achievement of performance conditions at their departure date.

The vesting of options granted under the 2002 Executive Scheme will be dependent on the achievement by the Group of specified thresholds of earnings per share, before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan ("underlying EPS"), growth in excess of the growth in the Retail Price Index ("RPI") over a three year performance period commencing on the first day of the accounting period in which the grant was made.

An option will not become exercisable unless the growth in the underlying EPS of the Group over the period exceeds the growth in the RPI over the same period by 9%. Where that 9% target is achieved, one half of the number of ordinary shares forming the option will become exercisable.

For an option to become exercisable in full, the growth in the EPS of the Group over the period must exceed the growth in the RPI over the same period by a minimum of 24%. The number of Ordinary Shares subject to option which will become exercisable will increase on a sliding scale if the growth in the underlying EPS exceeds the growth in the RPI by between 9% and 24% over the performance period. The underlying EPS measure is chosen because it is designed to enable the 2002 Executive Scheme to reward sustained improvement in the Group's financial performance.

The number and weighted average exercise prices (WAEP) of share options are as follows:

| | 2005 No. | 2005 WAEP £ | 2004 No. | 2004 WAEP £ |
|---|---|---|---|---|
| Outstanding at 1 January | **5,411,679** | **1.67** | 4,944,839 | 1.39 |
| Granted during the year | **–** | **–** | 1,826,704 | 2.41 |
| Forfeited during the year | **(258,640)** | **2.31** | (896,018) | 1.76 |
| Exercised during the year | **(1,152,737)** | **1.39** | (463,846) | 1.39 |
| **Outstanding at 31 December** | **4,000,302** | **1.71** | 5,411,679 | 1.67 |
| **Exercisable at 31 December** | **305,142** | **1.90** | 1,618,852 | 1.60 |

The weighted average share price during 2005 was £2.12 (2004: £2.20).

The options exercised during 2005 and 2004 relate to "good leavers".

# Notes to the Consolidated Financial Statements

### 26. Employee benefits (cont'd)

At 31 December 2005 the following options granted under the 2002 Executive Share Option Scheme to acquire Ordinary Shares were outstanding:

| Grant date | No. of options outstanding | Earliest exercise date (assuming performance criteria satisfied) | Exercisable before | Exercise price (p) |
|---|---|---|---|---|
| 19 March 2003 | 2,729,971 | 19 March 2006 | 19 March 2013 | 139.00 |
| 9 March 2004 | 1,270,331 | 9 March 2007 | 9 March 2014 | 240.83 |

The options outstanding at 31 December 2005 have a weighted average full contractual life of 7.6 years (2004 – 8.5 years).

The fair value of services received in return for share options granted is measured by reference to the fair value of share options granted. The estimate of the fair value of options granted is measured based on a Binomial model. The contractual life of the option (10 years) is used as an input into this model. Expectations of early exercise are incorporated into the Binomial model.

The key assumptions which have been used in the Binomial model to ascertain the fair value of options are as follows:

| | 9 March 2004 grant | 19 March 2003 grant |
|---|---|---|
| Fair value at measurement date (per option) | 67.0p | 50.0p |
| Number of options granted | 1,826,704 | 5,238,907 |
| Share price at grant date | 242.0p | 158.0p |
| Exercise price | 240.8p | 139.0p |
| Vesting period | 3 years | 3 years |
| Full term of option | 10 years | 10 years |
| Expected volatility (i) | 36.0% | 37.0% |
| Risk free rate at grant date (ii) | 4.7% | 5.0% |
| Expected dividend yield | 5.5% | 5.5% |
| Early exercise trigger (iii) | 150.0% | 150.0% |
| Expected forfeiture rate (per annum) | 5.0% | 5.0% |
| Probability of meeting EPS hurdle (iv) | 75.0% | 75.0% |

(i) The expected volatility is based on the historic volatility of the Company's share price over a period equal to the term of the option prior to the date of grant, adjusted, if applicable, for any expected changes to future volatility due to trends in the data.

(ii) The risk free rate at grant date is based on UK treasury bonds with an appropriate term.

(iii) Assumption that options will be exercised when market price reaches a fixed percentage of the exercise price.

(iv) The probability of meeting the underlying EPS hurdle has been determined by the Directors' assessment of future performance at the date of award.

The actual final total grant expense is "trued up" during the vesting period and at the end of the vesting period after allowing for actual forfeitures and the outturn on underlying EPS.

## 26. Employee benefits (cont'd)

### (ii) 2002 Share Save Scheme

The 2002 Share Save Scheme is an "all employee share scheme" which was activated in March 2003. The options granted entitle the holders to acquire Ordinary Shares, whether by subscription or purchase, at a price per Ordinary Share determined by the Directors prior to the issue of invitations. The price at which options can be offered cannot be less than 80% of the middle-market quotation of an Ordinary Share at the date of grant. No cash alternative is available.

As part of the application process a participant will require to enter into a savings contract with a savings provider (presently Yorkshire Building Society), in terms of which the participant will agree to make 36 (in the case of a 3-year savings contract) or 60 (in the case of a 5-year contract) monthly savings contributions of a fixed amount. At the end of the savings contract, the participant may choose to apply for repayment of his or her savings contributions, in addition to a tax free bonus.

An option may only be exercised once and normally only during the period of 6 months after the date on which the participant first becomes entitled to repayment of his or her savings contributions plus bonus. The option will lapse after a period of six months following the end of the savings contract.

Employees who are deemed "good leavers" are entitled to exercise their options, for which they have accrued savings to date, for a period of up to six months after they leave.

The number and weighted average exercise prices (WAEP)of share options are as follows:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | No. | WAEP £ | No. | WAEP £ |
| Outstanding at 1 January | **1,345,745** | **1.41** | 942,706 | 1.14 |
| Granted during the year | **527,374** | **1.87** | 610,722 | 1.81 |
| Forfeited during the year | **(363,458)** | **1.56** | (196,761) | 1.37 |
| Exercised during the year | **(111,236)** | **1.30** | (10,922) | 1.19 |
| **Outstanding at 31 December** | **1,398,425** | **1.55** | 1,345,745 | 1.41 |
| **Exercisable at 31 December** | **19,574** | **1.75** | 59,233 | 1.26 |

The weighted average share price during 2005 was £2.12 (2004: £2.20).

The options exercised during 2005 and 2004 relate to "good leavers".

At 31 December 2005 the following options granted under the 2002 Share Save Scheme to acquire Ordinary Shares were outstanding:

| Grant date | No. of options outstanding | Earliest exercise date (assuming performance criteria satisfied) | Exercisable before | Exercise price (p) |
|---|---|---|---|---|
| 9 May 2003 (3 year) | 245,403 | 9 May 2006 | 9 Nov 2006 | 114.0 |
| 9 May 2003 (5 year) | 335,708 | 9 May 2008 | 9 Nov 2008 | 114.0 |
| 19 April 2004 (3 year) | 204,520 | 19 April 2007 | 19 Oct 2007 | 181.0 |
| 19 April 2004 (5 year) | 139,044 | 19 April 2009 | 19 Oct 2009 | 181.0 |
| 29 April 2005 (3 year) | 306,046 | 29 April 2008 | 29 Oct 2008 | 186.6 |
| 29 April 2005 (5 year) | 167,704 | 29 April 2010 | 29 Oct 2010 | 186.6 |

The options outstanding at 31 December 2005 have a weighted average contractual life of 2.8 years (2004 – 3.3 years).

The fair value of services received in return for share options granted is measured by reference to the fair value of share options granted. The estimate of the fair value of options granted is measured based on a Binomial model. The contractual life of the option (3.5 or 5.5 years) is used as an input into this model. Expectations of early exercise are incorporated into the Binomial model.

# Notes to the Consolidated Financial Statements

**26. Employee benefits (cont'd)**

The key assumptions which have been used in the Binomial model to ascertain the fair value of options are as follows:

| | 2005 grant (3 year) | 2005 grant (5 year) | 2004 grant (3 year) | 2004 grant (5 year) |
|---|---|---|---|---|
| Fair value at measurement date (per option) | 49.4p | 51.4p | 54.0p | 56.0p |
| Number of options granted | 339,233 | 188,141 | 350,944 | 259,778 |
| Share price at grant date | 220.25p | 220.25p | 202.0p | 202.0p |
| Exercise price | 186.60p | 186.60p | 181.0p | 181.0p |
| Vesting period | 3 years | 5 years | 3 years | 5 years |
| Full term of option | 3.5 years | 5.5 years | 3.5 years | 5.5 years |
| Expected volatility (i) | 30.0% | 30.0% | 39.0% | 37.4% |
| Risk free rate at grant date (ii) | 4.5% | 4.5% | 4.9% | 5.0% |
| Expected dividend yield | 5.5% | 5.5% | 5.5% | 5.5% |
| Expected forfeiture rate (per annum) | 5.0% | 5.0% | 5.0% | 5.0% |

(i) The expected volatility is based on the historic volatility of the Company's share price over a period equal to the term of the option prior to the date of grant, adjusted, if applicable, for any expected changes to future volatility due to trends in the data.

(ii) The risk free rate at grant date is based on UK treasury bonds with an appropriate term.

The actual final total grant expense is ''trued up'' during the vesting period and at the end of the vesting period after allowing for actual forfeitures.

**(iii) The Re-Investment Plan**

The Re-Investment Plan was a plan established to allow employees previously employed by F&C Group Holdings Group (F&CGH) prior to the merger to voluntarily re-invest one half of their entitlement under the Shadow Equity Plan into Ordinary Shares in F&C Asset Management plc and rights to receive further Ordinary Shares in F&C Asset Management plc. The purpose of the Re-Investment Plan, which was a one-off plan linked to the merger, was to encourage key former F&CGH Group employees to re-invest one half of their proceeds of their vested Shadow Equity Plan entitlement into Investment Shares which will be forfeitable for a period of up to 2 years should the participant voluntarily resign or be dismissed for gross misconduct within 24 months of completion of the merger on 11 October 2004.

**Forfeiture table in relation to ''Investment Shares''**

| Time between 11 October 2004 and voluntary resignation or dismissal | Percentage of shares held in the Re-Investment Plan forfeited |
|---|---|
| Less than 12 months | 100% |
| Between 12 months and 24 months | 50% |
| More than 24 months | Nil |

To encourage re-investment, and in recognition of the fact that the Investment Shares carry forfeiture provisions, after three years participants will receive up to one Matching Share for each Investment Share (subject to continued employment and achievement of performance conditions). One third of Matching Shares have no performance criteria, while the remaining two-thirds vest in line with the following schedule.

The performance condition, described below, is based on growth in underlying EPS of the Group. This measure was chosen by the Board for its transparency to participants and to incentivise Executives to deliver the benefits of the merger.

| Underlying EPS growth 2003 – 2006 | Percentage becoming unconditional |
|---|---|
| PI + 9% or less cumulative over three years | Nil |
| PI + 24% or more cumulative over three years | 100% |
| In between points | Straight-line pro-rata between 0% and 100% |

(Where PI stands for an appropriate index of price inflation – the Retail Price Index (RPI)).

For levels of underlying EPS performance between those shown in the table above, the number of Matching Shares awarded will vary on a straight line basis between the minimum and maximum level shown.

The cash-settled element of the awards is based on dividends payable on the shares during the vesting period, prior to becoming unconditional, being notionally re-invested in F&C Asset Management plc shares. Once the award shares vest, the value of the notional shares is paid to the employee in cash.

## 26. Employee benefits (cont'd)

The number of investment shares and matching share awards are as follows:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Investment Shares No. | Matching Shares No. | Investment Shares No. | Matching Shares No. |
| Outstanding at 1 January | **11,021,991** | **11,021,991** | – | – |
| Granted during the year | **–** | **–** | 11,021,991 | 11,021,991 |
| Forfeited during the year | **(836,054)** | **(955,538)** | – | – |
| Exercised during the year | **(5,560,311)** | **(532,712)** | – | – |
| **Outstanding at 31 December** | **4,625,626** | **9,533,741** | 11,021,991 | 11,021,991 |

The exercise price for all awards is 0.0p.

The weighted average share price during 2005 was £2.12 (2004 – £2.20).

During 2005 the initial tranche of Investment Shares vested. All Matching Shares exercised during 2005 relate to "good leavers".

At 31 December 2005 the following awards granted under the Re-Investment Plan were outstanding:

| Grant date | No. of awards outstanding | Earliest vesting date (assuming performance criteria satisfied) |
|---|---|---|
| 11 Oct 2004<br>Investment shares | 4,625,626 | 11 October 2006 |
| 11 Oct 2004<br>Matching shares | 9,533,741 | 11 October 2007 |

The awards outstanding at 31 December 2005 have a weighted average contractual life of 1.5 years (2004 – 2.1 years).

The fair value of services received in return for share awards granted is measured by reference to the fair value of share awards granted. No valuation model was used as awards were granted at full market value. Part of the Re-Investment Plan awards will be settled in equity shares and part in cash. The cash element relates to the value of accrued dividends at the date of vesting.

The key assumptions which have been used in the model to ascertain the fair value of awards are as follows:

| | Investment | | | | Matching | | | |
|---|---|---|---|---|---|---|---|---|
| | 1 year | | 2 years | | Basic | | Performance | |
| | Equity | Cash | Equity | Cash | Equity | Cash | Equity | Cash |
| Fair value at measurement date (per award) | 217.69p | 12.31p | 206.04p | 23.96p | 195.02p | 34.98p | 195.02p | 34.98p |
| Number of awards granted | 5,510,996 | | 5,510,995 | | 3,673,997 | | 7,347,994 | |
| Share price at grant date | 230.0p | | 230.0p | | 230.0p | | 230.0p | |
| Exercise price | 0.0p | | 0.0p | | 0.0p | | 0.0p | |
| Vesting period | 1 year | | 2 years | | 3 years | | 3 years | |
| Full term of awards | 1 year | | 2 years | | 3 years | | 3 years | |
| Risk free rate at grant date(i) | 4.74% | | 4.74% | | 4.74% | | 4.74% | |
| Expected dividend yield | 5.5% | | 5.5% | | 5.5% | | 5.5% | |
| Probability of meeting EPS hurdle (ii) | N/A | | N/A | | N/A | | 87.5% | |
| Expected forfeiture rate (per annum) | 5.0% | | 5.0% | | 5.0% | | 5.0% | |

**26. Employee benefits (cont'd)**

(i) The risk free rate at grant date is based on UK treasury bonds with an appropriate term.

(ii) The probability of meeting the underlying EPS hurdle has been made by the Directors' assessment of future performance at the date of award.

The actual final total grant expense is "trued up" during the vesting period and at the end of the vesting period after allowing for actual forfeitures and the outturn on underlying EPS.

**(iv) The Long-Term Remuneration Plan (LTRP)**

The LTRP is the primary long term incentive arrangement of the F&C Asset Management plc Group. Awards of these options are at the discretion of the Board.

Vesting of the Ordinary Shares that are currently the subject of an award under the LTRP will be dependent upon specified performance conditions and conditions of continued service. The performance conditions applied to the LTRP are determined by the Board and are measured over a three year performance period. 50% of any award relates to the achievement of total shareholder return (TSR) targets and 50% of the award relates to real underlying EPS growth as set out as follows:

| **TSR target (applying to 50% of any award)**<br>**The Group's TSR relative to FTSE 250** | **Percentage of award vesting** |
|---|---|
| Below Median | Nil |
| Median | 35% |
| Upper Quartile | 100% |

| **Underlying EPS target (applying to 50% of any award)**<br>**Growth in Group's EPS over three year performance period** | **Percentage of award vesting** |
|---|---|
| Below PI + 9% | Nil |
| PI + 9% | 50% |
| PI + 24% or higher | 100% |

(Where PI stands for an appropriate index of price inflation – the Retail Price Index (RPI)).

The TSR target is dependent upon the TSR of the Group compared to the TSR of the other companies who formed the FTSE 250 Index at the start of each performance period (the comparator companies) over a three year performance period commencing on the first day of the accounting period in which the award was made. In order to determine how much of an award will vest, the Remuneration Committee compares the TSR of the Group with that of the companies that constituted the FTSE 250 Index published by the London Stock Exchange plc immediately before the date of the award. At the end of the performance period, the Group and each of the comparator companies (the comparator list) are listed and ranked in accordance with their TSR over the performance period. The number of Ordinary Shares which vest would depend upon the ranking of the Group in the comparator list in accordance with the vesting table above, described as follows. For below median TSR performance no awards would vest; for TSR performance between the median and upper quartile (125th and 63rd position in the comparator list index) awards would vest on a straight line basis between 35% for median and 100% for upper quartile. The TSR measure reflects the movement in the value of shares plus any dividends declared during the relevant period. It was therefore chosen as the performance measure for the LTRP as it is directly related to movements in shareholder value.

For levels of both TSR and underlying EPS performance between those shown in the tables above, any award that vests under the LTRP will vary on a straight line basis between the minimum and maximum levels shown.

The cash-settled element of the awards is based on dividends payable on the shares during the vesting period (prior to becoming unconditional) being notionally re-invested in the F&C Asset Management plc shares. Once the award shares vest, the value of the notional shares is paid to the employee in cash.

The number of share awards are as follows:

| | **2005**<br>**No.** | **2004**<br>**No.** |
|---|---|---|
| Outstanding at 1 January | **6,375,904** | – |
| Granted during the year | **–** | 6,375,904 |
| Forfeited during the year | **(422,916)** | – |
| **Outstanding at 31 December** | **5,952,988** | 6,375,904 |

No awards were exercisable at 31 December 2005 or 31 December 2004.

The exercise price for all awards is 0.0p.

No awards were exercised during 2005 or 2004.

## 26. Employee benefits (cont'd)

At 31 December 2005 the following awards granted under the LTRP were outstanding:

| Grant date | No. of awards outstanding | Earliest exercise date (assuming performance criteria satisfied) | Exercise price (p) |
|---|---|---|---|
| 15 Nov 2004 | 5,952,988 | 15 Nov 2007 | 0.0p |

The awards outstanding at 31 December 2005 have a weighted average contractual life of 1.9 years (2004 – 2.9 years).

The fair value of services received in return for share options granted is measured by reference to the fair value of share awards granted. The estimate of the fair value of awards granted is measured at full market value for the EPS criteria and no model is used. Monte Carlo Simulation is used to value the TSR criteria. The contractual life of the award (3 years) is used as an input into this model. The value of dividend payments have been separated as these are settled in cash.

The key assumptions which have been used in the models to ascertain the fair value of 2004 awards are as follows:

| | 2004 grant – TSR | | 2004 grant – EPS | |
|---|---|---|---|---|
| | Equity | Cash | Equity | Cash |
| Fair value at measurement date (per award) | 147.39p | 26.44p | 203.7p | 36.54p |
| Number of awards granted | 3,187,952 | | 3,187,952 | |
| Share price at grant date | 240.25p | | 240.25p | |
| Exercise price | 0.0p | | 0.0p | |
| Vesting period | 3 years | | 3 years | |
| Full term of award | 3 years | | 3 years | |
| Expected volatility(i) | 38.0% | | N/A | |
| Risk free rate at grant date(ii) | 4.74% | | N/A | |
| Expected dividend yield | 5.5% | | N/A | |
| EPS performance hurdle | N/A | | 75.0% | |
| Expected forfeiture rate | 5.0% | | 5.0% | |

(i) The expected volatility is based on the historic volatility of the Company's share price over a period equal to the term of the option prior to the date of grant, adjusted, if applicable, for any expected changes to future volatility due to trends in the data.

(ii) The risk free rate at grant date is based on UK treasury bonds with an appropriate term.

The actual final total grant expense is "trued up", either during the vesting period and at the end of the vesting period, after allowing for actual forfeitures and the outturn on underlying EPS.

**26. Employee benefits (cont'd)**

**(v) Share Incentive Plan**

During 2005, 100 ''free'' Share Incentive Plan shares were awarded to all employees of the Group who applied for them.

795 employees were granted 100 free shares, without conditions. Awards were therefore settled in equity as they do not have a vesting period.

Awards were granted on 21 June 2005 at a share price of £1.95.

The expense associated with this award was £156,000.

**(vi) Purchased Equity Plan**

The Purchased Equity Plan operates in conjunction with the discretionary bonus scheme and is intended to encourage shareholding by management and employees of the Group by providing for:

- The compulsory purchase of shares using annual bonus above a threshold level; and
- Voluntary purchase of shares using annual bonus, with associated Matching Shares.

Under the terms of the Purchased Equity Plan, participation can arise in one of two ways:

- On an annual basis eligible employees who are awarded in a financial year an aggregate bonus in excess of a threshold level of £75,000 will be required to defer one third of the element exceeding £75,000 (prior to 24 February 2006: one third of aggregate bonus) into shares (Compulsory Purchased Equity) subject to continued service for three years; and
- As and when determined by the Board, eligible employees may be invited to elect to defer into shares any remaining proportion of their gross cash bonus not subject to deferral on a compulsory basis for three years (subject to a minimum deferral of £1,500) (Voluntary Purchased Equity).

To encourage participants to defer their bonus on a voluntary basis, a matching award will be made for Voluntary Purchased Equity. The matching award will provide for a maximum of one share for each two shares received as Voluntary Purchased Equity. Vesting of any matching award is dependent on the satisfaction of performance conditions and continued service. The performance conditions will relate to real underlying EPS growth measured over a three year period as set out below.

| Growth in the Group's EPS* over three year performance period | Matching Purchased Equity award for each Voluntary Purchased Equity share purchased |
|---|---|
| Below PI + 9% | NIL |
| PI + 9% | 1 for 4 |
| PI + 24% or higher | 1 for 2 |

* EPS is calculated by reference to underlying earnings of the Group and will exclude amortisation and impairment of intangible assets, restructuring costs, and the cost of the Re-Investment Plan.

(Where PI stands for an appropriate index of price inflation – the Retail Price Index (RPI)).

### 26. Employee benefits (cont'd)

For levels of underlying EPS performance between those shown in the table, the Matching Purchased Equity award will vary on a straight line basis between the minimum and maximum levels shown.

The Compulsory Purchased Equity will not benefit from any form of matching award and is subject to forfeiture in the event that the employee leaves the Group for any reason (other than as a "good leaver") in the three year retention period.

Invitations to participate in the Voluntary Purchased Equity element of the plan are at the discretion of the Board and will only be offered when the Board considers it appropriate to do so. There were no Voluntary Purchased Equity awards during the year.

The cash-settled element of the awards is based on dividends payable on the shares during the vesting period (prior to becoming unconditional) being notionally re-invested in F&C Asset Management plc shares. Once the award shares vest, the value of the notional shares is paid to the employees in cash.

The first awards under the Purchased Equity Plan were made in the current year. The number of share awards are as follows:

| | 2005 Awards No. |
|---|---|
| Outstanding at 1 January | – |
| Granted during the year | 750,091 |
| Forfeited during the year | (35,688) |
| Exercised during the year | (29,978) |
| **Outstanding at 31 December** | **684,425** |

No awards were exercisable at 31 December 2005.

The exercise price for all awards is 0.0p.

The awards exercised during 2005 relate to "good leavers".

At 31 December 2005 the following awards granted under the Purchased Equity Plan to acquire Ordinary Shares were outstanding:

| Grant date | No. of awards outstanding | Earliest vesting date (assuming performance criteria satisfied) | Exercise price (p) |
|---|---|---|---|
| 24 March 2005 | 684,425 | 24 March 2008 | 0.0p |

The awards outstanding at 31 December 2005 have a weighted average contractual life of 2.3 years (2004 – n/a).

**26. Employee benefits (cont'd)**

No valuation model is required as awards are granted at full market value. The value of dividend payments are separated out, as these are settled in cash.

The key assumptions which have been used to ascertain the fair value of awards are as follows:

| | 2005 award Compulsory purchased equity Equity | 2005 award Compulsory purchased equity Cash |
|---|---|---|
| Fair value at measurement date (per award) | **197.98p** | **35.52p** |
| Number of awards granted | **750,091** | |
| Share price at grant date | **233.50p** | |
| Exercise price | **0.0p** | |
| Vesting period | **3 years** | |
| Full term of award | **3 years** | |
| Expected forfeiture rate (per annum) | **5.0%** | |

**(vii) 1995 Executive Share Option Scheme**

IFRS 2 'Share-based Payment' is only applied to grants of shares, share options or other equity instruments that were granted after 7 November 2002 and had not yet vested before 1 January 2005 (i.e. the effective date of IFRS 2).

The 1995 Executive Share Option Scheme last granted options before 7 November 2002 and is not therefore subject to the full effects of IFRS 2 in terms of recognising an expense in profit or loss. The standard does, however, require certain disclosures to be made in respect of this scheme.

The 1995 Executive Share Option Scheme is an unapproved share option scheme, where participation was entirely at the discretion of the Directors. The lifespan of the 1995 Executive Share Option Scheme is ten years from the date on which it was approved by shareholders and accordingly no further options can be granted under the Scheme after 1 September 2005. The vesting period is three years. Options are settled by grant of shares to individuals. No cash alternative is available.

If the options remain unexercised after a period of 10 years from the date of grant, the options expire. Furthermore, options are forfeited if the employee leaves the Group before the options vest. Employees who are deemed "good leavers" are entitled to exercise their options for a period of one year after they leave, regardless of whether the vesting requirements have been met.

The option price shall not be less than the market value of a share on the dealing day (or averaged over the three dealing days) before the option is granted.

The exercise of options granted under the 1995 Executive Scheme will be dependent on the achievement by the Company of specified thresholds of earnings per share before amortisation and impairment of intangible assets, restructuring costs and the cost of the Re-Investment Plan. Options cannot be exercised before the third anniversary of the date of the grant. Thereafter they can be exercised (in whole or in part) only when the EPS percentage increase in each 3 consecutive years exceeds the RPI by at least 2% per annum.

## 26. Employee benefits (cont'd)

The number and weighted average exercise prices (WAEP)of share options are as follows:

| | 2005 No. | 2005 WAEP £ | 2004 No. | 2004 WAEP £ |
|---|---|---|---|---|
| Outstanding at 1 January | **3,612,317** | **2.58** | 4,032,113 | 2.58 |
| Forfeited during the year | **(757,817)** | **2.46** | (336,910) | 2.69 |
| Exercised during the year | **(81,369)** | **2.14** | (82,886) | 2.13 |
| Expired during the year | **(80,000)** | **2.31** | – | – |
| **Outstanding at 31 December** | **2,693,131** | **2.64** | 3,612,317 | 2.58 |
| **Exercisable at 31 December** | **343,257** | **2.29** | 687,592 | 2.41 |

The weighted average share price during 2005 was £2.12 (2004: £2.20).

The options exercised during 2005 relate to "good leavers".

At 31 December 2005 the following options granted under the 1995 Executive Share Option Scheme to acquire Ordinary Shares were outstanding:

| Grant date | No. of options outstanding | Date vested | Exercisable before | Exercise price (p) |
|---|---|---|---|---|
| 9 June 1998 | 730,028 | 24 March 2006 | 9 June 2008 | 203.83 |
| 16 July 1999 | 781,834 | 24 March 2006 | 16 July 2009 | 232.50 |
| 28 April 2000 | 642,029 | 24 March 2006 | 28 April 2010 | 214.00 |
| 20 October 2000 | 18,740 | 24 March 2006 | 20 October 2010 | 320.17 |
| 1 March 2001 | 520,500 | 24 March 2006 | 1 March 2011 | 455.83 |

The options outstanding at 31 December 2005 have a weighted average contractual life of 3.8 years (2004 – 4.8 years).

**Summary of share-based payment schemes**

The Group recognised total expenses, excluding National Insurance Contributions, related to share-based payment schemes as follows:

| | Note | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|---|
| 2002 ESOS (2003 grant) | | **809** | 561 |
| 2002 ESOS (2004 grant) | | **363** | 213 |
| 2002 Share Save scheme (2003 grant) | | **73** | 122 |
| 2002 Share Save scheme (2004 grant) | | **42** | 54 |
| 2002 Share Save scheme (2005 grant) | | **39** | – |
| The Re-investment Plan (2004 grant) | | **21,328** | 5,428 |
| The Long-Term Remuneration Plan (2004 grant) | | **3,099** | 405 |
| Purchased Equity Plan (2005 grant) | | **436** | – |
| Share Incentive Plan – 100 free shares | | **155** | – |
| **Total share-based payment expenses** | 5 | **26,344** | 6,783 |

## 26. Employee benefits (cont'd)

| | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|
| **Total carrying amount of cash-settled liabilities** | **3,214** | 562 |

The total expense recognised during the year in respect of share-based payment schemes is as follows:

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| Equity – settled | **24,216** | 6,221 |
| Cash – settled | **2,128** | 562 |
| **Total share-based payment expenses** | **26,344** | 6,783 |

## 27. Deferred income

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| At 1 January | **15,751** | 8,193 |
| Acquired on acquisition of F&CGH Group | **–** | 4,780 |
| Income deferred in the year | **4,924** | 4,712 |
| Amortisation in the year | **(2,645)** | (1,934) |
| **At 31 December** | **18,030** | 15,751 |

| | 31 December 2005 £000 | 31 December (as restated) 2004 £000 |
|---|---|---|
| **Split as follows:** | | |
| Non-current liabilities | **14,351** | 10,752 |
| Current liabilities | **3,679** | 4,999 |
| | **18,030** | 15,751 |

## 28. Investment contract liabilities

Investment contract liabilities in respect of policyholder investments at the start and end of the year and an analysis of movements during the year is as set out below:

| | 2005<br>£000 | 2004<br>(as restated)<br>£000 |
|---|---|---|
| Liability as at 1 January | **862,308** | 884,690 |
| Contributions received | **170,529** | 65,715 |
| Investment return applied | **165,369** | 90,454 |
| Charges levied | **(4,260)** | (3,032) |
| Repayments | **(194,904)** | (190,394) |
| Movement in reinsurance ceded | **7,886** | 14,875 |
| **Liability as at 31 December** | **1,006,928** | 862,308 |

All investment contract liabilities have been disclosed as due within one year as this is considered to be appropriate to the rights of policyholders who have the right to withdraw their investments at short notice.

The fair value of unit linked investment contracts is the number of units allocated to policyholders in each of the unit linked funds multiplied by the unit price of those funds at the balance sheet date.

The fund assets and liabilities used to determine the unit prices at the balance sheet date are valued on a basis that is consistent with their measurement basis in the Consolidated Balance Sheet.

## 29. Insurance contract liabilities

Insurance contract liabilities include life assurance liabilities in respect of lifetime guarantees provided with certain investment products and annuity liabilities in respect of pension investment contracts where the investor has retired. These liabilities and related reinsurance balances at the start and end of the year, together with an analysis of movements in the year, are set out below:

| | 2005 | | | 2004 (as restated) | | |
|---|---|---|---|---|---|---|
| **Insurance contract liabilities** | **Gross £000** | **Reinsurance £000** | **Net £000** | **Gross £000** | **Reinsurance £000** | **Net £000** |
| At 1 January | **2,352** | **2,352** | **–** | 2,443 | 2,443 | – |
| Claims paid | **(152)** | **(152)** | **–** | (156) | (156) | – |
| Change in economic assumptions | **125** | **125** | **–** | 25 | 25 | – |
| Change in mortality assumptions | **194** | **194** | **–** | – | – | – |
| Unwind interest rate at start of year | **104** | **104** | **–** | 117 | 117 | – |
| Other changes in year | **(6)** | **(6)** | **–** | (77) | (77) | – |
| **At 31 December** | **2,617** | **2,617** | **–** | 2,352 | 2,352 | – |

A liability adequacy test was carried out at policy level and resulted in no additional provision for either 2004 or 2005. No significant gain or loss arose on reinsurance contracts incepted in 2004 or 2005.

# Notes to the **Consolidated Financial Statements**

### 29. Insurance contract liabilities (cont'd)

**Assumptions**

The principal assumptions used in determining the insurance contract liabilities and the reinsurers' share of these liabilities and the process adopted to arrive at these assumptions are as follows:

| Mortality rates | 2005 | 2004 |
|---|---|---|
| Annuities in payment | **70-101% PM/FA92(i)** | 95% PM/FA92U2005(ii) |

(i) Projected thereafter using 95% of the average of medium cohort improvement factors for males (71.25% for females) subject to a minimum annual rate of improvement of 0.5%.

(ii) Plus additional 0.5% per annum for Group, males only, from the valuation date onwards.

Due to the small number of annuity policies, the mortality assumptions reflect recent experience of the reinsurer together with an allowance for future mortality improvement. Experience analysis for mortality is performed annually by the reinsurer.

**Discount rate**

The discount rate used is 4.02% (2004: 4.50%) based on current fixed interest gross redemption yields, with a prudent adjustment for risk.

### 30. Share capital

**(a) Ordinary share capital of 0.1p**

| | 31 December 2005 Number of shares | 31 December 2005 £000 | 31 December 2004 Number of shares | 31 December 2004 £000 |
|---|---|---|---|---|
| **Authorised:** | | | | |
| **Equity interests** | | | | |
| Ordinary Shares of 0.1p | **800,000,000** | **800** | 800,000,000 | 800 |
| Deferred Shares of 0.1p | **100,000,000** | **100** | 100,000,000 | 100 |
| **Allotted, issued and fully paid:** | | | | |
| **Equity interests** | | | | |
| Ordinary Shares of 0.1p | **483,434,237** | **484** | 482,200,131 | 482 |

| | No. of Ordinary Shares 2005 | No. of Ordinary Shares 2004 |
|---|---|---|
| Issued at 1 January | **482,200,131** | 150,256,675 |
| Share options exercised during the year | **1,234,106** | 546,732 |
| Shares issued in respect of the acquisition of F&CGH Group: | | |
| – shares issued by way of consideration | **–** | 320,374,763 |
| – shares issued to Abacus Trust | **–** | 11,021,961 |
| **Issued at 31 December** | **483,434,237** | 482,200,131 |

The holders of Ordinary Shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

### 30. Share capital (cont'd)

During the year the following share options were exercised, in line with the rules of the appropriate scheme, and Ordinary Shares allotted:

| Exercise date | Executive Share Option Scheme | No. of Ordinary Shares | Exercise price (p) |
|---|---|---|---|
| 5 Jan 2005 | 1995 | 5,000 | 203.83 |
| 5 Jan 2005 | 2002 | 40,000 | 139.00 |
| 6 Jan 2005 | 2002 | 109,711 | 139.00 |
| 6 Jan 2005 | 1995 | 34,112 | 214.00 |
| 12 Jan 2005 | 2002 | 86,474 | 139.00 |
| 19 Jan 2005 | 2002 | 20,000 | 139.00 |
| 28 Jan 2005 | 2002 | 48,000 | 139.00 |
| 28 Jan 2005 | 1995 | 4,845 | 203.83 |
| 9 Feb 2005 | 2002 | 135,518 | 139.00 |
| 18 Feb 2005 | 2002 | 5,582 | 139.00 |
| 18 Feb 2005 | 1995 | 3,706 | 232.50 |
| 18 Feb 2005 | 1995 | 3,706 | 214.00 |
| 29 Mar 2005 | 2002 | 40,796 | 139.00 |
| 6 Apr 2005 | 2002 | 30,215 | 139.00 |
| 14 Apr 2005 | 2002 | 70,000 | 139.00 |
| 19 Apr 2005 | 2002 | 30,000 | 139.00 |
| 11 May 2005 | 2002 | 8,206 | 139.00 |
| 11 May 2005 | 1995 | 30,000 | 214.00 |
| 5 July 2005 | 2002 | 17,986 | 139.00 |
| 4 Aug 2005 | 2002 | 44,691 | 139.00 |
| 16 Aug 2005 | 2002 | 39,208 | 139.00 |
| 24 Aug 2005 | 2002 | 20,000 | 139.00 |
| 9 Sept 2005 | 2002 | 36,870 | 139.00 |
| 12 Oct 2005 | 2002 | 316,545 | 139.00 |
| 25 Oct 2005 | 2002 | 9,353 | 139.00 |
| 2 Dec 2005 | 2002 | 43,582 | 139.00 |
| | | **1,234,106** | |

### 30. Share capital (cont'd)

The Group held the following shares in Employee Share Option Plan (ESOP) trusts. These are categorised as own shares, as a deduction from shareholders' funds:

| | 31 December 2005 No. | 31 December 2004 No. |
|---|---|---|
| F&C Group ESOP Trustee Limited | **890,200** | 969,700 |
| Abacus Trust | **5,673,904** | 11,021,961 |
| | **6,564,104** | 11,991,661 |

The aggregate nominal value of own shares held by ESOPs at 31 December 2005 was £7,000 (31 December 2004: £12,000). The market value of these shares at 31 December 2005 was £11,635,000 (31 December 2004: £29,499,000).

During the year, the Company purchased 104,780 of its own Ordinary Shares (2004: 500,000) of 0.1p to satisfy the exercises of awards granted under the share save scheme in respect of ''good leavers''. The cost of this to the Company, after exercise price monies paid by the former employees was £87,000 (2004: £1,156,000). The consideration paid for the shares was £223,000 (2004: £1,156,000).

#### (b) Deferred Shares of 0.1p each

| | 2005 £000 | 2004 £000 |
|---|---|---|
| At 1 January | **–** | – |
| Allotment of Deferred Shares on acquisition | **–** | 100 |
| Cancellation of Deferred Shares | **–** | (100) |
| **At 31 December** | **–** | – |

#### (c) Cumulative Preference Shares of £1 each

| | 31 December 2005 | | 31 December 2004 | |
|---|---|---|---|---|
| **Authorised, allotted, issued and fully paid** | Number of shares | £000 | Number of shares | £000 |
| At 1 January | **800,000** | **800** | 390,000 | 390 |
| Preference Shares issued during the year | **–** | **–** | 410,000 | 410 |
| **At 31 December** | **800,000** | **800** | 800,000 | 800 |

The issued Cumulative Preference Shares are classified as financial liabilities. The key terms and conditions relating to these Preference Shares are as follows:

– Dividends on the Cumulative Preference Shares are paid in priority to any payment of dividend on any other class of shares.

– On a return of assets on liquidation, the assets of the Company available for distribution shall be applied first in repaying the holders of the Cumulative Preference Shares the amounts paid up or credited as paid up on such shares, together with any arrears of the fixed dividend.

– Holders of Cumulative Preference Shares are entitled to one vote in instances where the fixed dividend is six months in arrears or in the event that a resolution put to the meeting varies or impacts the rights and privileges attached to these shares.

The terms of the Cumulative Preference Shares confer the right to receive a variable rate dividend on the amount paid up or credited as paid up on the Cumulative Preference Shares at the rate of 2% per annum above the London Inter-Bank Offer Rate (LIBOR) expressed as a rate per annum at the commencement of each half-yearly dividend payment period.

## 31. Reserves

### Reconciliation of movement in reserves

| | Ordinary share capital £000 | Deferred share capital £000 | Share premium account £000 | Merger reserve £000 | Foreign currency translation reserve[1] £000 | Fair value reserve[1] £000 | Special distr-ibutable reserve[1] £000 | Other reserves[1] £000 | Retained earnings £000 | Minority interests £000 | Total equity £000 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Balance at 1 January 2004 (as restated) | 150 | – | 2,795 | 117,891 | – | 1,155 | 18,513 | 3 | 10,777 | – | 151,284 |
| Items reported in the Consolidated Statement of Recognised Income and Expense | – | – | – | – | 4,846 | 463 | – | (99) | (5,098) | – | 112 |
| Share capital allotted on exercise of options | 1 | – | 821 | – | – | – | – | – | – | – | 822 |
| Share capital issued to Abacus Trust | 11 | – | 25,340 | – | – | – | – | – | (25,351) | – | – |
| Share capital issued as consideration | 320 | – | – | 736,542 | – | – | – | – | – | – | 736,862 |
| Purchase of own shares | – | – | – | – | – | – | – | – | (1,164) | – | (1,164) |
| Capitalisation of merger reserve | – | 100 | 99,900 | (100,000) | – | – | – | – | – | – | – |
| Cancellation of Deferred Shares | – | (100) | – | – | – | – | 100 | – | – | – | – |
| Conversion of share premium account | – | – | (99,900) | – | – | – | 99,900 | – | – | – | – |
| Final dividend 2003 paid | – | – | – | – | – | – | – | – | (10,487) | – | (10,487) |
| Interim dividend 2004 paid | – | – | – | – | – | – | – | – | (5,993) | – | (5,993) |
| Realised element of merger reserve to offset amortisation of intangible assets | – | – | – | (4,679) | – | – | – | – | 4,679 | – | – |
| Transfer from special distributable reserve in relation to dividends | – | – | – | – | – | – | (16,480) | – | 16,480 | – | – |
| Share-based payment charges | – | – | – | – | – | – | – | – | 6,222 | – | 6,222 |
| **Balance at 31 December 2004 (as restated)** | 482 | – | 28,956 | 749,754 | 4,846 | 1,618 | 102,033 | (96) | (9,935) | – | 877,658 |
| Items reported in the Consolidated Statement of Recognised Income and Expense | **–** | **–** | **–** | **449** | **(4,246)** | **(159)** | **–** | **–** | **(99,478)** | **–** | **(103,434)** |
| Share capital allotted on exercise of options | **2** | **–** | **1,774** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **1,776** |
| Purchase of own shares | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(87)** | **–** | **(87)** |
| Final dividend 2004 paid | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(32,952)** | **–** | **(32,952)** |
| Interim dividend 2005 paid | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(18,865)** | **–** | **(18,865)** |
| Realised element of merger reserve to offset amortisation and impairment of intangible assets | **–** | **–** | **–** | **(144,057)** | **–** | **–** | **–** | **–** | **144,057** | **–** | **–** |
| Transfer from special distributable reserve in relation to dividends | **–** | **–** | **–** | **–** | **–** | **–** | **(51,817)** | **–** | **51,817** | **–** | **–** |
| Share-based payment charges | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **21,822** | **–** | **21,822** |
| Partners' capital injected | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **2** | **2** |
| Partners' drawings in advance of profits | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(500)** | **(500)** |
| **Balance at 31 December 2005** | **484** | **–** | **30,730** | **606,146** | **600** | **1,459** | **50,216** | **(96)** | **56,379** | **(498)** | **745,420** |

Cumulative defined pension scheme actuarial gains/(losses) recognised as at 31 December 2005 are £33,643,000 which are included in retained earnings (31 December 2004 – £2,909,000). See note 26(a)

(1) The total of foreign currency translation reserve, fair value reserve, special distributable reserve and other reserves constitutes 'Other reserves' as disclosed in the Consolidated Balance Sheet and amounts to £52,179,000 (2004: £108,401,000).

## 31. Reserves (cont'd)

**Nature and purpose of reserves**

**Share premium account**

The share premium account is used to record the issue of share capital above par value. This reserve is not distributable and can only be reduced with court approval.

**Merger reserve**

The merger reserve is used to record share premium on shares issued by way of consideration in respect of acquisitions. The realised element of the merger reserve can be used to offset amortisation and impairment of intangible assets charged to the Income Statement. This reserve is not distributable.

**Foreign currency translation reserve**

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

**Fair value reserve**

This reserve records fair value changes on available for sale investments until the investments are derecognised.

**Special distributable reserve**

The special distributable reserve was created with the cancellation of share premium. This reserve may be used by the Group for the purchase of its own shares or to fund future dividend payments.

**Other reserves:**

– **Capital redemption reserve**

  The capital redemption reserve is created on cancellation of share capital. This reserve is not distributable.

– **Non-distributable reserve – associate**

  Comprises the Group's share of associate expenses which are written off to share premium.

**Retained earnings**

Retained earnings comprises:

– all realised gains and losses recognised through the Income Statement less dividend distributions;

– actuarial gains and losses recognised in the pension liability;

– deferred tax on actuarial gains and losses;

– transactions relating to equity-settled share-based payments, and all deferred tax movements on share-based payments reflected through equity; and

– the purchase and sale of own shares.

This reserve is distributable.

## 32. Notes to the Cash Flow Statement

### (a) Analysis of cash flow statement movements

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Adjustments for non-cash items:** | | |
| Impairment of property, plant and equipment | – | 1,988 |
| Depreciation of property, plant and equipment | **3,176** | 2,557 |
| Amortisation of intangible assets | **56,221** | 21,194 |
| Impairment of intangible assets | **111,500** | – |
| Unrealised foreign exchange gains and losses | – | 297 |
| (Gain)/loss on sale of property, plant and equipment | **(73)** | 40 |
| Share-based payment expenses | **24,474** | 6,782 |
| | **195,298** | 32,858 |
| **Changes in working capital and provisions:** | | |
| (Increase)/decrease in trade and other receivables | **(40,757)** | 35,729 |
| Increase/(decrease) in trade and other payables | **5,014** | (71,147) |
| Increase in other assets (stock of units and shares) | **(120)** | (42) |
| Decrease in other liabilities | **(488)** | (393) |
| Increase in investment contract liabilities | **157,389** | 15,800 |
| Decrease in investment contract reinsurance | **(23,686)** | (52,747) |
| Increase in insurance contract liabilities | **899** | 55 |
| Decrease in insurance contract reinsurance | – | (55) |
| (Decrease)/increase in employee benefits | **(5,377)** | 169 |
| Increase in deferred acquisition costs | **(986)** | (1,410) |
| Increase in deferred income | **1,564** | 2,778 |
| Pension contributions paid less pension operating profit charge | **156** | (195) |
| Increase in provisions for liabilities and charges | **5,823** | 145 |
| (Increase)/decrease in financial investments | **(153,730)** | 56,683 |
| | **(54,299)** | (14,630) |

### (b) Acquisition of F&C Group (Holdings) Group ('F&CGH Group')

Full details of the acquisition can be found in note 16.

The acquisition on 11 October 2004 was financed primarily by the issue of shares totalling £736,862,000 at fair value. Although there is an estimated further consideration payable at 31 December 2005 of £2,942,000 (31 December 2004: £16,212,000) no cash has been remitted in respect of the acquisition.

Cash payments of £624,000 have been made in 2005 (2004: £11,998,000) in respect of expenses of acquisition of F&CGH Group.

The Group received cash and cash equivalents of £132,791,000 as the fair value at the date of acquisition.

### (c) Disposal of subsidiaries

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Proceeds from disposals (settled in cash) | **10** | – |
| **Net assets/(liabilities) of subsidiaries disposed of:** | | |
| Investments | **3** | – |
| Trade and other receivables | **1,762** | – |
| Current tax recoverable | **221** | – |
| Cash and cash equivalents | **824** | – |
| Trade and other payables | **(2,577)** | – |
| Goodwill | **449** | – |
| | **682** | – |
| **Loss on disposal of subsidiaries** | **672** | – |

### 32. Notes to the Cash Flow Statement (cont'd)

**(d) Property, plant and equipment**

During the period the Group acquired property, plant and equipment with an aggregate cost of £3,527,000 (2004: £3,968,000). Cash payments of £3,701,000 (2004: £4,066,000) were made to purchase property, plant and equipment during the year.

**(e) Cash and cash equivalents**

See note 22 for details of cash and cash equivalent balances, a description of cash and cash equivalents, restrictions on use of cash and details of borrowing facilities.

### 33. Contingencies

**Contingent liabilities:**

**(a) Shareholding in F&C Group Management Limited (formerly Primrose Street Holdings Limited)**

In December 2000, when Eureko agreed to acquire 90% of the issued share capital of F&C Group (Holdings) Limited from Hypo Vereins-Bank, approximately 73% of the ordinary issued shares of F&C Group Management Limited, a subsidiary company, were held in the form of two bearer share warrants which could not be located prior to the completion of the sale (the ''old Share Warrants'').

Since a bearer share warrant issued by a company entitles the bearer to the shares specified in the share warrant, there is a risk that a third party holding the old Share Warrants may claim that it is entitled to the specified shares in F&C Group Management Limited. If a third party were successful in establishing a claim in relation to the old Share Warrants, F&C Group (Holdings) Limited could be liable to indemnify F&C Group Management Limited under the original indemnity arrangements, which could, as set out below, have a material adverse effect on the F&C Asset Management Group's business, results of operations and/or financial condition.

Although there is a possibility that a third party may seek to establish that it is entitled to the shares specified in the old Share Warrants, the Directors have been informed that Eureko has been advised that the prospect of a third party succeeding in such a claim is remote.

Under the terms of the Sale and Purchase Agreement (in respect of the Merger), Eureko Holdings has given a specific indemnity (guaranteed by Eureko) to F&C Asset Management plc in respect of losses arising in relation to the old share warrants in F&C Group Management Limited (including in respect of the indemnity granted by F&C Group (Holdings) Limited to F&C Group Management Limited) which is capped at approximately £432 million.

**(b) European court case – VAT on investment trust management fees**

In a current European court case, a UK investment trust is seeking to establish that management services to UK investment trusts should be a VAT exempt supply, rather than a taxable supply in accordance with current UK VAT law. If this case were successful, a number of Group companies, in common with other relevant fund managers in the UK, would face claims from those investment trusts to which they have supplied services for repayment of the VAT they have charged to them. The AITC (a party to the above litigation) has indicated that it believes claims dating back as far as 1990 may be lodged with fund managers by investment trusts. Companies in the F&C Group can submit repayment claims to HM Revenue and Customs, but only dating back as far as 2001, being the maximum time period permitted. The Group has begun to receive protective claims from a number of its investment trust clients and has lodged protective claims with HM Revenue and Customs. At present, the Directors are not able to judge the likelihood that the VAT court case will be successful, nor are they able to quantify the claims that may be received or the extent to which such claims could be mitigated and therefore, are not able to quantify the potential liability.

**Contingent assets:**

During 2005 Banco Commercial Portugues S.A. (BCP), a Group client, withdrew approximately €2 billion of assets which were managed by the Group under the terms of long-term agreements. The Group is currently negotiating with BCP to obtain compensation to which it is contractually entitled. As settlement negotiations are at an early stage, the Group has not yet received the final valuations from the external advisers who have been appointed to support F&C and therefore the potential asset cannot be quantified.

## 34. Commitments

### Operating leases

The Group had the following future minimum rentals payable in respect of non-cancellable operating leases and other contracts at the year-end:

| | Premises | | Other | |
|---|---|---|---|---|
| | 31 December 2005 £000 | 31 December 2004 £000 | 31 December 2005 £000 | 31 December 2004 £000 |
| Within one year | **124** | 1,284 | **–** | 46 |
| After one year but not more than five years | **5,103** | 822 | **1,658** | 1,194 |
| More than five years | **144,061** | 154,771 | **–** | – |
| | **149,288** | 156,877 | **1,658** | 1,240 |

The Group holds all properties under operating leases.

### Sub-lease receivables

Future minimum rentals receivable under non-cancellable operating leases at the year-end are as follows:

| | Premises | |
|---|---|---|
| | 31 December 2005 £000 | 31 December 2004 £000 |
| Within one year | **31** | – |
| After one year but not more than five years | **6,910** | 8,120 |
| More than five years | **13,408** | 2,893 |
| | **20,349** | 11,013 |

One property receives a contingent lease payment based on a percentage of revenue in addition to a minimum lease payable. The maximum amount receivable under this arrangement is £216,000 per annum.

### Onerous lease provisions

The Group has onerous lease provisions as detailed in note 25.

### Capital commitments

The amounts contracted for in terms of capital expenditure, but not provided for in the financial statements at 31 December 2005, amount to £266,000 (31 December 2004 – £1,216,000).

## 35. Financial risk management objectives and policies

### (a) Strategy in using financial instruments

The Group's risk management framework and the processes for identifying risks across the Group, including strategic and operational risks, are described in the Directors' Report on Corporate Governance on pages 32 to 45. These processes include identification and control of financial risks.

As an asset management business, the Directors consider it appropriate to differentiate between those financial risks which directly impact the Group and those which indirectly impact the Group due to the risks borne by our clients and the subsequent impact on the Group's revenues.

**Shareholder earnings risk through client assets**

As an active fund manager we are responsible for managing assets in accordance with the mandates specified by our respective clients. The assets managed by the Group are subject to varying degrees of financial risks (market, credit and liquidity). While these risks could result in financial loss or gain through a change in asset value, these risks and rewards are fully borne by, or fall to the benefit of, our clients.

However, as the majority of the Group's asset management fees are quantified as a percentage of assets under management (generally on a quarterly or monthly basis), the Group's revenues are impacted by movements in client assets which are caused by the exposure to financial risks. As a result of the direct link of revenues to the value of client assets, our interests are aligned to those of our clients. Indeed, a number of client mandates provide for the Group to potentially earn performance fees, in addition to the base management fee, where the performance of a fund has exceeded defined benchmarks for a set period of time.

A key risk to our business is that of poor investment performance. A key role of the Head of Investments is to monitor the performance of investment professionals. This ongoing process will, where considered necessary, include the selective upgrade of the quality of our investment teams.

The key components of financial risk to which our clients are exposed are:

– *Market risk* – the risk of loss arising from changes in the values of, or income from, assets. Market risks include equity and property risk, foreign exchange risk and interest rate risk.

– *Credit risk* – the risk of loss due to the default of a company, individual or country, or a change in investors' risk appetite.

– *Liquidity risk* – the risk of loss because a firm, although solvent, either does not have sufficient financial resources available to it in order to meet its obligations as they fall due, or can secure them only at excessive cost.

The Group does not hedge its revenue exposure to market risks arising from movements in the value of client assets.

**Corporate financial risk strategy**

F&C adopts a low risk approach to treasury management and financial risks in relation to shareholder equity, endeavouring to ensure that its capital is managed and preserved appropriately and financial risks are managed as appropriate.

The Group treasury operations are managed by the Finance function within parameters defined by the Board. The regulatory capital and treasury position of the Group are reported to the Board on a regular basis.

The Group is exposed to a number of financial risks in the normal course of its business. The policy adopted is designed to manage risk and recognises that treasury management operations are specifically not treated as a profit centre. The key aspects of this policy and its implementation are detailed below:

- The Board Reserved List prohibits the establishment of borrowing facilities without the prior approval of the Board.
- Placing of funds on deposit will be short term (maximum term 90 days) to ensure such balances are eligible for inclusion as regulatory capital.
- Deposits may only be placed with counterparties approved by the F&C Credit Committee and the Board set the appropriate limit of exposure to any one counterparty.
- The Group does not use a hedging strategy to manage financial risks. As such, the Board Reserved List prohibits the use of derivatives including futures, options and forward contracts, in respect of own funds, without prior Board approval.
- Foreign currency exposure is managed to reduce the risk and impact of movements in exchange rates by the repatriation of surplus foreign currency into Sterling. Surplus currency balances are defined as being the level of cash which exceeds the regulatory capital and working capital requirements of the relevant foreign operations.

### 35. Financial risk management objectives and policies (cont'd)

The Directors give careful consideration to the appropriate funding structure for financing all acquisitions including the capacity to fund anticipated restructuring activity.

The overall objective of shareholder liquidity risk management is to ensure that there is sufficient liquidity over short (up to one year) and medium time horizons to meet the needs of the business. This includes liquidity to cover, among other things, operating expenses, servicing debt and equity capital as well as working capital to fund the Group's day-to-day requirements.

The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial assets which are exposed to interest rate movements.

#### (b) Analysis of financial risks

The Group's direct exposure to each category of financial risk is given below. As the financial risks and rewards of the assets attributable to the unit linked investment contracts fall to be borne by, or to the benefit of, policyholders rather than the equity holders of the Company, no further risk disclosures are given.

#### (i) Market risks

***Equity risk***

The Group has exposure to the movements in the market value of equities and property funds held by the Group's defined benefit schemes. In addition, the value of gilts and corporate bonds held by the scheme are impacted by movements in interest rates. The value of pension plan assets, which are subject to market risks, is disclosed in note 26.

The value of defined benefit pension obligations are quantified and discounted using corporate bond rates. Movements in these rates can have a significant impact on the pension liabilities and hence the quantum of the Group's pension deficit.

The only other assets where any direct market risk arises is in relation to the stock of units and shares held in open ended funds managed by the Group. The Group's box management policy specifically limits the overall magnitude of the box and the amount which may be held in any single fund to £1,500,000 and £50,000 respectively.

***Currency risk***

Currency risk is the risk that the value of a financial instrument will fluctuate because of changes in foreign exchange rates. The Group's objective is to minimise the impact of exchange rate movement by repatriation of excess funds to Sterling. The following monetary assets and liabilities of the Group were exposed to currency movement at 31 December:

| | Net foreign currency monetary assets/(liabilities) | | | | |
|---|---|---|---|---|---|
| | Euro | US Dollar | Yen | Other | Total |
| **Functional currency of Group operations** | **£000** | **£000** | **£000** | **£000** | **£000** |
| **2005 Sterling** | | | | | |
| **– equity holder** | **256,522** | **1,220** | **43** | **–** | **257,785** |
| **– policy holder** | **–** | **–** | **–** | **295,742** | **295,742** |
| 2004 Sterling | | | | | |
| – equity holder | 328,604 | 2,862 | 44 | (8) | 331,502 |
| – policy holder | – | – | – | 209,575 | 209,575 |

## 35. Financial risk management objectives and policies (cont'd)

***Interest rate risk***

**Year ended 31 December 2005**

The following table sets out the carrying amount, by maturity, of the Group's financial instruments that are exposed to interest rate risk:

| Fixed rate | Within 1 year £000 | 1-2 years £000 | 2-3 years £000 | 3-4 years £000 | 4-5 years £000 | More than 5 years £000 |
|---|---|---|---|---|---|---|
| Financial investments in respect of unit linked contracts | 176,467 | – | – | – | – | – |
| Financial investments – quoted | – | 25 | – | – | – | – |
| £180,000,000 Term Loan | (180,000) | – | – | – | – | – |

| Floating rates | Within 1 year £000 | 1-2 years £000 | 2-3 years £000 | 3-4 years £000 | 4-5 years £000 | More than 5 years £000 |
|---|---|---|---|---|---|---|
| Financial investments in respect of unit linked contracts | 21,225 | – | – | – | – | – |
| Loan to associate | 2,500 | – | – | – | – | – |
| Cash and cash equivalents | 146,197 | – | – | – | – | – |
| £50,000,000 revolving credit loan | (5,000) | – | – | – | – | – |
| £25,000,000 subordinated loan | – | – | – | (25,000) | – | – |
| £9,000,000 subordinated loan | – | – | – | (9,000) | – | – |
| £800,000 Cumulative Preference Shares | – | – | – | – | – | (800) |

**Year ended 31 December 2004**

| Fixed rate | Within 1 year £000 | 1-2 years £000 | 2-3 years £000 | 3-4 years £000 | 4-5 years £000 | More than 5 years £000 |
|---|---|---|---|---|---|---|
| Financial investments in respect of unit linked contracts | 142,883 | – | – | – | – | – |
| Financial investments – quoted | – | – | 26 | – | – | – |
| £180,000,000 term loan | – | (180,000) | – | – | – | – |

| Floating rates | Within 1 year £000 | 1-2 years £000 | 2-3 years £000 | 3-4 years £000 | 4-5 years £000 | More than 5 years £000 |
|---|---|---|---|---|---|---|
| Financial investments in respect of unit linked contracts | 15,279 | – | – | – | – | – |
| Cash and cash equivalents | 181,084 | – | – | – | – | – |
| £50,000,000 revolving credit loan | (5,000) | – | – | – | – | – |
| £25,000,000 subordinated loan | – | – | – | – | (25,000) | – |
| £9,000,000 subordinated loan | – | – | – | – | (9,000) | – |
| £800,000 Cumulative Preference Shares | – | – | – | – | – | (800) |

Interest on financial instruments classified as floating rate is repriced at intervals of less than one year.

Interest on financial instruments classified as fixed rate is fixed until the maturity of the instrument.

The other financial instruments of the Group that are not included in the above tables are non-interest bearing and are therefore not subject to interest rate risk. The rates applicable to interest bearing loans and borrowings are given in note 23.

## 35. Financial risk management objectives and policies (cont'd)

### (ii) Credit risk

Credit risk includes investment credit risk, counterparty risks, deposit and loan risks and country risk. As an asset management business which derives revenues which are based on a percentage of client assets under management, our exposure to default of clients is considered to be relatively low. However, due to the scale of some of our larger clients, the Group is exposed to a concentration of credit risk to the extent of the timing difference between the recognition of income for services rendered and the timing of receipt of management fees from clients. The quantum of accrued revenue and trade debtors at each balance sheet date is given in note 21. The specific concentration of risk from clients where trade debtors and accrued income for any one client or group of connected clients is £1,000,000 or more at either 31 December 2004 or 2005 is given below.

| | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|
| Included in trade debtors and accrued income: | | |
| – Amounts due from Friends Provident plc Group | **3,113** | 534 |
| – Amounts due from the Achmea Group | **5,967** | 6,586 |
| – Resolution Life plc | **3,283** | – |
| – RSA plc | **1,000** | 3,451 |
| – OEIC's : Management fees | **3,140** | 2,505 |
| Other debtors: | | |
| – OEIC's : Debtor in respect of liquidated units | **6,950** | 1,832 |
| Loan receivable: | | |
| – Loan to associate | **2,500** | — |
| | **25,953** | 14,908 |

The Board treasury policy limits the exposure to any one counterparty (in respect of cash and cash equivalents) to £25 million, recognising that each counterparty used has been approved by the F&C Credit Committee. There is no net credit risk in relation to client assets as this risk is borne fully by the clients concerned.

### (iii) Liquidity risk

The treasury policy set by the Board only allows financial assets attributable to equity holders to be invested in low risk deposits or money market instruments where the risk of capital loss is extremely low.

The Group utilises the experience and skills of its dealing team to obtain the best interest rate, recognising the expected maturity dates are aligned to the Group's working capital requirements and that no deposit can be placed for a period of 90 days or more, as this would not be eligible to count towards the regulatory capital of the entity to which it relates.

The Group also has various borrowing facilities available to it. The undrawn committed facilities available at 31 December 2004 and 2005 are given in note 22.

The Group's £180 million term loan falls due for repayment on 1 November 2006. As highlighted in the Chief Executive's Report, the Board is at an advanced stage of appointing advisers to facilitate the refinancing of this debt.

## 36. Insurance risk management

The Group's insurance contracts are all annuity contracts which guarantee payment during the lifetime of the annuitant at a specified level or with a specified escalation factor. They are all 100% reinsured to Friends Provident Pensions Limited.

The only risk that the Group is subject to in respect of these contracts is the credit risk of the reinsurer. Given the small amount at risk (£2,617,000 at 31 December 2005; £2,352,000 at 31 December 2004) this is not considered significant.

### 37. Subsidiary undertakings

The principal entities controlled by the parent undertaking are as follows:

| | Percentage interest and voting rights | Country of registration or incorporation | Nature of business |
|---|---|---|---|
| **(i) United Kingdom** | | | |
| FP Asset Management Holdings Limited(1) | 100 | England | Holding company |
| F&C Property Asset Management plc (formerly F&C Property Services Limited)(1) | 100 | England | Property investment management |
| Friends' Provident Unit Trust Managers Limited(1) | 100 | England | OEIC investment management |
| F&C Asset Management Services Limited(1) | 100 | England | Employee service company |
| ISIS Equity Partners Holdings Limited(1) | 100 | England | Holding company |
| ISIS Investment Manager plc(1) | 100 | England | Investment management |
| F&C Managed Pension Funds Limited(1) | 100 | England | Insurance management |
| F&C Treasury Limited(1) | 100 | England | Treasury management company |
| F&C Group (Holdings) Limited(1) | 100 | England | Holding company |
| F&C Group ESOP Trustee Limited(1) | 100 | Scotland | ESOP Trustee |
| ISIS Investment Trusts Business Limited(1) | 100 | Scotland | Investment Trust management |
| FP Fund Managers Limited(2) | 100 | England | Investment management |
| F&C Asset Managers Limited(2) | 100 | England | Investment management |
| F&C Property Limited (formerly F&C Property Asset Management plc)(2) | 100 | England | Property investment management |
| ISIS Equity Partners plc(3) | 100 | England | Private Equity investment management |
| F&C Property Investments Limited(4) | 100 | England | Property investment management |
| F&C Fund Management Limited(4) | 100 | England | OEIC investment management |
| ISIS Investment Management Limited(4) | 100 | England | Investment management |
| WAM Holdings Limited(5) | 100 | England | Holding company |
| Cerebys Limited(6) | 100 | England | Derivative investment company |
| F&C Unit Management Limited(6) | 100 | England | OEIC investment management |
| FCEM Holdings (UK) Limited(6) | 100 | England | Holding company |
| F&C (CI) Limited(7) | 100 | England | Private Equity investment company |
| F&C Investment Services Limited(7) | 100 | England | Investment management |
| F&C Management Limited(7) | 100 | England | Investment management |
| F&C Property Investment Management Limited(7) | 100 | England | Property investment management |
| F&C Alternative Investments (Holdings) Limited(8) | 100 | England | Investment holding company |
| F&C Group Management Limited(8) | 100 | England | Holding company |
| F&C Emerging Markets Limited(9) | 100 | England | Investment management |
| F&C Holdings Limited(10) | 100 | England | Holding company |
| F&C Partners LLP(11) | 60 | England | Hedge investment management |
| F&C Private Equity Nominees Limited(12) | 100 | England | Private Equity investment company |

## 37. Subsidiary undertakings (cont'd)

| | Percentage interest and voting rights | Country of registration or incorporation | Nature of business |
|---|---|---|---|
| **(ii) Overseas** | | | |
| Ivory & Sime (Japan) KK[(1)] | 100 | Japan | Investment management |
| Ivory & Sime (Bermuda) Limited[(1)] | 100 | Bermuda | Investment management |
| F&C Channel Islands Limited[(6)] | 100 | Jersey | Employee services company |
| F&C Management (Jersey) Limited[(6)] | 100 | Jersey | Investment management |
| F&C Netherlands B.V.[(8)] | 100 | The Netherlands | Investment management |
| F&C Ireland Limited[(8)] | 100 | Republic of Ireland | Investment management |
| F&C Luxembourg (formerly AF-Investimentos Internacional, S.A.)[(8)] | 100 | Luxembourg | Investment management |
| F&C Portugal Gestao de Patrimonios S.A.[(8)] | 100 | Portugal | Investment management |

(1) Owned by F&C Asset Management plc

(2) Owned by FP Asset Management Holdings Limited

(3) Owned by ISIS Equity Partners Holdings Limited

(4) Owned by WAM Holdings Limited

(5) Owned by F&C Treasury Limited

(6) Owned by F&C Management Limited

(7) Owned by F&C Holdings Limited

(8) Owned by F&C Group (Holdings) Limited

(9) Owned by FCEM Holdings (UK) Limited

(10) Owned by F&C Group Management Limited

(11) Owned by F&C Alternative Investments (Holdings) Limited

(12) Owned by F&C (CI) Limited

The above information has been supplied only for undertakings principally affecting the results and assets of the Group.

### 38. Related party transactions

In the ordinary course of business, the Company and its subsidiary undertakings carry out transactions with related parties, as defined by IAS 24 'Related Party Disclosures'. Material transactions for the year are set out below.

The principal subsidiary undertakings of the Company are shown in note 37 and its interests in associates are shown in note 15. During the year, the Group entered into the following transactions with related parties.

#### (a) Compensation of key management personnel of the Group

In aggregate these are set out below:

| | 2005 £000 | 2004* (as restated) £000 |
|---|---|---|
| Short-term employee benefits | **7,828** | 4,173 |
| Post-employment benefits | **1,299** | 563 |
| Termination benefits | **2,256** | 1,679 |
| Share-based payments: | | |
| – recurring arrangements | **–** | 376 |
| – Re-Investment Plan | **7,002** | – |
| **Total** | **18,385** | 6,791 |

* The compensation for 2004 only relates to the period from 11 October 2004 to 31 December 2004 where key management joined the Group as part of the F&CGH Group acquisition.

Where key management personnel participate in defined benefit pension schemes which have been accounted for as such under IAS 19, the amount included as compensation reflects the current service or past service cost, and where applicable, past service cost, for the relevant year. Where key management personnel are members of multi-employer defined benefit arrangements or defined contribution schemes, the compensation shown reflects the contributions payable for each year.

The share-based payments disclosed in the table above reflect the value of any share-based payments vesting during the year. This is quantified as the aggregate of cash payments plus the fair value of shares on the date of vesting (excluding any consideration payable on exercise) of such share-based payment awards.

The amounts above include the following payments:

Sir David Kinloch resigned as the Chairman of the Company on 11 October 2004. His fees as Chairman of the Company were paid to Caledonia Investments plc.

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Fees | **–** | 57 |

The following Non-Executive Directors' fees of K Satchell and B W Sweetland were paid to Friends Provident plc in respect of 2004. B W Sweetland retired from the Company and his position as Non-Executive Director on 24 January 2005. Fees in respect of 2005 have been waived by Friends Provident, as disclosed on page 54.

| | 2005 £000 | 2004 £000 |
|---|---|---|
| K Satchell | **–** | 26 |
| B W Sweetland | **–** | 26 |
| | **–** | 52 |

#### (b) Transactions with key management personnel of the Group

Company dividends paid to key management are as follows:

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| Ordinary dividends paid | **60** | 48 |

## 38. Related party transactions (cont'd)

### (c) Transactions and balances with related parties

**Related party transactions with the Friends Provident Group (FP Group)**

Friends Provident plc is the parent undertaking and ultimate controlling party of the F&C Group.

Transactions with related parties during 2005 and 2004 and outstanding balances with these parties as at 31 December 2005 and 31 December 2004 are given below, by each group of related parties:

Companies within the F&C Group provide investment management services to companies in the FP Group and are entitled to receive management fees in line with the contractual terms of relevant investment management agreements.

Companies within the FP Group provide, under the Shared Services Agreement, services in respect of accounting, investment accounting and other professional services. The FP Group also provides services reasonably required by F&C. Fees are paid monthly in arrears. The Shared Services Agreement is terminable on six months' written notice by either party. The investment management agreements with the FP Group are terminable with twelve months notice, but revert to long-term contracts of between 5 and 10 years if Friends Provident's shareholding in the Company were to fall below 50%.

| | Total invoiced and accrued during 2005 £000 | Outstanding at 31 December 2005 £000 | Total invoiced and accrued during 2004 (as restated) £000 | Outstanding at 31 December 2004 (as restated) £000 |
|---|---|---|---|---|
| **Management fees** | | | | |
| Management fees invoiced to the FP Group during the year | **35,085** | **1,964** | 35,430 | 534 |
| The amount outstanding at 31 December is included within trade debtors and accrued income | | | | |
| **Shared services and administration services** | | | | |
| Shared service invoices billed and accrued by the FP Group during the year | **589** | **10** | 841 | 58 |
| Administration service invoices billed and accrued by the FP Group during the year | **842** | **–** | 1,296 | 381 |
| The amount outstanding at 31 December is included within accruals | | | | |
| **Other recharges** | | | | |
| Other recharges to the FP Group during the year | **46** | **–** | 205 | (339) |
| The amount outstanding at 31 December is included within trade debtors | | | | |
| Other recharges from the FP Group during the year | **439** | **–** | 58 | – |
| The amount outstanding at 31 December is included within accruals | | | | |
| Other recharges includes charges made to or from the FP Group for premises, staff costs and other related expenditure | | | | |
| **Dividends and interest payable** | | | | |
| Ordinary dividends | **27,268** | **–** | 11,084 | – |
| Dividends on Preference Shares | **53** | **27** | 32 | 20 |
| Loan interest | **12,542** | **1,317** | 11,519 | 1,727 |
| The amount outstanding at 31 December is included within amounts owed to FP Group (note 24) | | | | |
| **Other transactions** | | | | |
| Net investment in property funds | **925** | **–** | (8,759) | – |
| Annuity reinsurance | **152** | **(15)** | 156 | – |

Net investment in property funds represent amounts invested through the Property Fund of Friends Provident Life Assurance Limited, a subsidiary undertaking of Friends Provident plc.

The Group's insurance contracts are all annuity contracts and are 100% reinsured to Friends Provident Pensions Limited, a subsidiary undertaking of Friends Provident plc.

## 38. Related party transactions (cont'd)

**Inter-company balances with the FP Group**

At 31 December 2005, the Group owed £1,900,000 (2004 – £2,405,000) to the FP Group.

**OEICs and private equity SPVs**

Where the FP Group controls an F&C managed OEIC or private equity SPV, they are required to consolidate them and hence the investment management fees received by F&C are related party transactions.

| | Total invoiced and accrued during 2005 £000 | Outstanding at 31 December 2005 £000 | Total invoiced and accrued during 2004 (as restated) £000 | Outstanding at 31 December 2004 (as restated) £000 |
|---|---|---|---|---|
| Investment management fees | **9,653** | **794** | 9,032 | 737 |
| Carried interest receipts | **1,120** | **–** | – | – |

**Loans due to the FP Group**

The following loans were due to the FP Group at 31 December:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Friends Provident Life and Pensions Limited | **205,000** | 205,000 |
| Friends Provident plc | **5,000** | 5,000 |
| | **210,000** | 210,000 |

The loans are unsecured and their contractual terms are shown in note 23.

**Related party transactions with Eureko B.V.**

Following the acquisition of F&C Group (Holdings) Limited, Eureko holds in excess of 20% of the Ordinary Shares of the Company and is entitled to Board representation. Consequently, transactions between the F&C Group and Eureko or its subsidiary companies are considered to be related party transactions for the period since 11 October 2004.

Companies within the F&C Group provide investment management services to the Eureko Group. F&C Group has entitlement to receive management fees in line with the contracted terms of relevant investment management agreements.

Companies within the Eureko Group provide, under the Transitional Services Agreement, services in respect of investment accounting and other administration services.

## 38. Related party transactions (cont'd)

| | Total invoiced and accrued during 2005 £000 | Outstanding at 31 December 2005 £000 | Total invoiced and accrued during 2004 £000 | Outstanding at 31 December 2004 £000 |
|---|---|---|---|---|
| **Shared services and administrative services received from:** | | | | |
| Friends First | **178** | **10** | 18 | 83 |
| Achmea Group | **1,948** | **202** | – | 141 |
| The amount outstanding at 31 December is included within trade creditors and accruals | | | | |
| **Management fees invoiced and accrued by the Group during the year:** | | | | |
| Achmea Group | **36,178** | **6,047** | 13,227 | 6,586 |
| Friends First | **5,179** | **766** | 563 | 829 |
| Imperio | **325** | **29** | 207 | 123 |
| Interamerican | **85** | **–** | 107 | 30 |
| The amount outstanding at 31 December is included within trade debtors and accrued income | | | | |
| **Dividends and loan interest payable to Eureko B.V.:** | | | | |
| Ordinary dividends | **10,921** | **–** | – | – |
| Loan interest | **428** | **122** | 121 | 121 |

**Subordinated loan due to Eureko B.V.**

At the year-end, the Group had an unsecured subordinated loan of £9,000,000 with Eureko B.V., as disclosed in note 23.

**Amounts owed from/to Eureko**

At 31 December 2005, the Group was owed £3,583,000 from Eureko B.V. and its subsidiaries. At 31 December 2004 the Group owed £316,000 to Eureko B.V. and its subsidiaries.

**Related party transactions with associates**

**Cardinal Capital Partners Limited**

There were no related party transactions during the current or prior year. The share of losses in 2005 is £674,000 (2004: £318,000).

**ISIS EP LLP**

ISIS EP LLP has been an associate of the Group since 1 July 2005. Consequently, transactions between the Group and ISIS EP LLP are considered to be related party transactions for the period from this date.

The consideration received by the Group on the transfer of its private equity business to ISIS EP LLP was £1. Subscription monies of £200 were paid to ISIS EP LLP for A class capital, providing entitlement to future profit share. The net assets of the former Group subsidiaries sold to ISIS EP LLP amounted to £223,000 at the date of disposal.

| **Amounts charged by the Group to ISIS EP LLP** | Total invoiced and accrued during 2005 £000 | Outstanding at 31 December 2005 £000 |
|---|---|---|
| Shared service costs | **500** | **500** |
| Other recharges | **136** | **134** |
| Profit share receivable | **335** | **335** |
| Group relief payable to subsidiary of ISIS EP LLP | **(378)** | **(378)** |

The Group has subscribed £2,500,000 for non-voting, non-participating B class capital in ISIS EP LLP. This is disclosed as a loan, and full details of the terms and conditions are disclosed in note 21.

## 38. Related party transactions (cont'd)

**Post-employment benefit plans**

The Group operates and participates in several post-employment benefit plans as detailed in note 26(a).

The Group contributed amounts to the defined benefit and defined contribution plans and had amounts outstanding at 31 December each year as follows:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Employer contributions £000 | Outstanding at 31 December £000 | Employer contributions £000 | Outstanding at 31 December £000 |
| F&C Management Limited Pension Fund | 1,579 | – | 450 | – |
| ISIS Asset Management plc Pension Fund | 1,200 | – | 1,200 | – |
| F&C Portugal[1] | 796 | – | 38 | – |
| F&C Netherlands[2] | 639 | – | 220 | – |
| F&C Ireland[3] | 69 | – | 17 | – |

[1] incorporated within the Fundo de Pensões do Grupo Banco Comercial Português scheme.
[2] incorporated within the Achmea Pension Plan.
[3] incorporated within the Friends First Retirement and Death Benefits Plan.

In addition to the above, the Group has an unfunded obligation to provide the Chairman, R W Jenkins, with a pension as detailed in note 26(a).

The Group manages the assets of the F&C Management Limited Pension Fund and the ISIS Asset Management plc Pension Fund. The assets of these schemes totalled £114,144,000 at 31 December 2005 (31 December 2004: £95,493,000). In addition, the Group manages £698,135,000 (31 December 2004: £595,668,000) of investments in respect of Friends Provident's main defined benefit pension scheme. The Group received the following investment management fees from these schemes:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Fees receivable £000 | Outstanding at 31 December £000 | Fees receivable £000 | Outstanding at 31 December £000 |
| F&C Management Limited Pension Fund | 72 | – | 8 | – |
| ISIS Asset Management plc Pension Fund | 157 | – | 135 | – |
| Friends Provident Pension Scheme | 725 | – | 635 | – |

## 39. Subsequent events

**Expected loss of F&C Latin American Investment Trust**

On 10 March 2006 an announcement was made by one of the Group's investment trust clients, F&C Latin American Trust PLC (the Trust), that following the resignation of the Trust's nominated manager from the Group, the Trust Board decided to appoint a new manager, further details of which have still to be announced.

While the exact timing of the termination of the management contract is uncertain, it is expected to be imminent, however, all management and administrative fees will continue to be received by the Group up to 8 May 2006, the date of the Trust's Annual General Meeting and continuation vote.

Annualised revenues from this Trust for 2006 are approximately £3.1million.

The expected loss of this business constitutes an indicator of potential impairment in the related intangible asset which was recognised as part of the F&C acquisition, and as such, an impairment review of the investment trust management contracts will be undertaken in 2006. This review will re-assess the carrying value of the relevant assets, including their estimated remaining economic life, and determine whether any further impairment will arise.

## 39. Subsequent events (cont'd)

**Withdrawal of Resolution plc funds**

As previously communicated to shareholders, the Group were advised during 2005 that Resolution Life had initiated plans to internalise the management of their assets. The Group subsequently reached agreement with Resolution that compensation of £27 million would be received following the withdrawal of the funds, representing a rebate of consideration paid for these contracts as part of the original acquisition. Since 31 December 2005, Resolution have withdrawn the majority of the £19.9 billion funds remaining as at 31 December 2005 and, as such, have triggered the payment of the £27 million compensation, which will be received by the Group in April 2006.

The total annualised revenue on all Resolution funds lost, including the £5.2 billion of funds lost during 2005, amounts to some £27 million.

As these contracts are recognised as intangible assets, the agreed compensation was assumed receivable in the calculations to assess whether the assets had been impaired. No impairment arose in respect of these contracts.

## 40. Consolidated supervision

The Group is not subject to the regulatory consolidated capital requirements of the Financial Services Authority.

## 41. Parent undertaking and controlling party

In the opinion of the Directors, the Group's ultimate parent undertaking and controlling party is Friends Provident plc. Friends Provident plc is incorporated in England and Wales. Copies of the Friends Provident Group Financial Statements can be obtained from the Company Secretary, Pixham End, Dorking, Surrey RH4 1QA.

## 42. Explanation of transition to IFRS

**Accounting policies**

As stated in the accounting policies, these are the Group's first consolidated financial statements prepared in accordance with IFRS. These accounting policies have been applied in preparing the financial statements for the year ended 31 December 2005, the comparative information presented in these financial statements for the year ended 31 December 2004 and in the preparation of an opening Balance Sheet at 1 January 2004 (the Group's date of transition).

In preparing its opening IFRS Balance Sheet, the Group has adjusted amounts reported previously in financial statements prepared in accordance with its previous basis of accounting (UK GAAP). An explanation of how the transition from previous GAAP to IFRS has affected the Group's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany them.

# Notes to the Consolidated Financial Statements



### Table A1

**Summary reconciliation of changes in equity as at 1 January 2004 and 31 December 2004**

| | Note | 1 January 2004 £m | 31 December 2004 £m |
|---|---|---|---|
| **UK GAAP equity (as previously reported)** | | 129.1 | 818.7 |
| Dividends | (i) | 10.5 | 32.9 |
| Reversal of goodwill amortisation | (ii) | 23.1 | 56.8 |
| Amortisation of intangible assets (management contracts) | (ii) | (10.9) | (25.4) |
| Share-based payments | (iii) | 0.3 | 1.6 |
| Consolidation of Employee Benefit Trusts | (iv) | – | (7.6) |
| Fair value of financial investments | (v) | 1.2 | 1.6 |
| Accounting for share of loss of associate | (vi) | – | (0.4) |
| Reclassification of preference shares to liabilities | (vii) | (0.4) | (0.8) |
| Lease incentives | (viii) | (0.7) | (0.9) |
| Revenue | (ix) | (0.5) | (1.6) |
| Employee benefits | (x) | (0.4) | (0.5) |
| Foreign exchange movements | (xi) | – | 3.3 |
| IFRS – increase in equity | | 22.2 | 59.0 |
| **IFRS equity** | | **151.3** | **877.7** |

**Table A2**

**Summary reconciliation of changes in profit/(loss) after tax for the year ended 31 December 2004**

| | | Year ended 31 December 2004 £m |
|---|---|---|
| **UK GAAP loss after tax (as previously reported)** | | (19.4) |
| Reversal of goodwill amortisation | (ii) | 33.7 |
| Amortisation of intangible assets (management contracts) | (ii) | (14.5) |
| Share-based payments | (iii) | (1.3) |
| Accounting for share of loss of associate | (vi) | (0.3) |
| Lease incentives | (viii) | (0.2) |
| Revenue | (ix) | (1.1) |
| Employee benefits | (x) | (0.1) |
| Foreign exchange movements | (xi) | (0.3) |
| IFRS – increase in profit | | 15.9 |
| **IFRS loss after tax** | | **(3.5)** |

**Notes to the reconciliation of equity and profit as presented in tables A1 and A2, above, and B1 to C5 below**

Details of the IFRS adjustments are set out below.

*(i)* *Dividends (IAS 10)*

Dividends declared after the period end in respect of the period to the balance sheet date were previously recognised in that period. Under IFRS this is no longer the case and as a result retained earnings at each balance sheet date are increased and current liabilities are decreased by the amount of these declared dividends. These amounted to £10.5m at 1 January 2004 and £32.9m as at 31 December 2004.

*(ii)* *Business combinations (IFRS 3)*

The Group has applied IFRS 3 to all business combinations since 1July 2002. Accordingly, the Group has revised the measurement of certain assets to fair value at the date of the business combination in which they were acquired. Additionally, from 1 January 2004 (1 July 2002 in respect of the RSAI acquisition), goodwill is no longer amortised under IFRS, but is tested annually for impairment.

As a result of the above adjustments, the goodwill amortisation charge was reversed by £33.7m for the year ended 31 December 2004. The cumulative impact of these goodwill adjustments on equity amounted to £23.1m as at 1 January 2004 and £56.8m as at 31 December 2004.

The impact of amortising intangible assets (management contracts) has reduced equity by £10.9m at 1 January 2004. In addition, the amortisation charge (net of tax) of £14.5m for the year ended 31 December 2004 has cumulatively reduced equity by £25.4m as at 31 December 2004.

# Notes to the **Consolidated Financial Statements**

**Notes to the reconciliation of equity and profit as presented in tables A1 and A2, above, and B1 to C5 below (cont'd)**

IFRS requires intangible assets acquired as part of a business combination to be separately identified. As a result of the restatement of previous acquisitions £104.3m of goodwill recognised in respect of the RSAI acquisition was reclassified as an intangible asset (management contracts) as at 1 January 2004. In addition, a deferred tax liability of £31.3m and a corresponding increase in goodwill was recognised. The intangible assets are being amortised over their expected useful lives. The deferred tax liability is being released to the Income Statement as the amortisation of management contracts is recognised. The restatement of the F&CGH Group business combination during 2004 also resulted in £516.9m of intangible management contracts being recognised together with the associated deferred tax liability of £155.1m. The following tables summarise the Balance Sheet movements (for each period) in respect of goodwill, management contracts and deferred tax, as a result of the adoption of IFRS:

| | Goodwill £m | Management contracts £m | Deferred tax liability* £m |
|---|---|---|---|
| **UK GAAP balances – as at 1 January 2004** | 303.9 | – | – |
| Reversal of goodwill amortisation charge for previous periods | 23.1 | – | – |
| Recognition of intangible assets – management contracts | (104.3) | 104.3 | – |
| Recognition of deferred tax liability on management contracts | 31.3 | – | (31.3) |
| Amortisation of management contracts in respect of prior periods | – | (15.6) | – |
| Release of deferred tax in respect of amortisation of management contracts | – | – | 4.7 |
| **Net impact of all adjustments, as shown in table B2** | (49.9) | 88.7 | (26.6) |
| **IFRS balances as at 1 January 2004** | 254.0 | 88.7 | (26.6) |

| | Goodwill £m | Management contracts £m | Deferred tax liability* £m |
|---|---|---|---|
| **UK GAAP balances – as at 31 December 2004** | 955.6 | – | – |
| Reversal of cumulative goodwill amortisation charge | 56.8 | – | – |
| Recognition of intangible assets – management contracts (RSAI) | (104.3) | 104.3 | – |
| Recognition of intangible assets – management contracts (F&CGH Group) | (516.9) | 516.9 | – |
| Recognition of deferred tax liability on management contracts (RSAI) | 31.3 | – | (31.3) |
| Recognition of deferred tax liability on management contracts (F&CGH Group) | 155.1 | – | (155.1) |
| Cumulative amortisation of management contracts | – | (36.4) | – |
| Release of deferred tax in respect of amortisation of management contracts | – | – | 10.9 |
| Exchange gain | – | 5.0 | (1.5) |
| Net impact of other IFRS on net assets acquired | 0.2 | – | – |
| Impact of subsequent fair value adjustments | 0.1 | – | – |
| **Net impact of all adjustments, as shown in table C4** | (377.7) | 589.8 | (177.0) |
| **IFRS balances as at 31 December 2004** | 577.9 | 589.8 | (177.0) |

* This movement only reflects the deferred tax impact of IFRS 3.

*(iii)* *Share-based payments (IFRS 2)*

The Group applied IFRS 2 to its active share-based payment arrangements, except for equity-settled share-based payment arrangements granted before 7 November 2002. The Group accounted for these share-based payment arrangements at intrinsic value under UK GAAP. This has been adjusted to fair value to be consistent with IFRS 2.

The effect of accounting for equity-settled share-based payment transactions at fair value is to increase losses after tax by £1.3m for the year ended 31 December 2004.

The adoption of IFRS 2 is equity-neutral for equity-settled transactions (excluding deferred tax). Cash-settled transactions reduce net assets by the movement in the provision for the period (net of deferred tax). The impact of these IFRS adjustments is to increase equity by £0.3m as at 1 January 2004, and by £1.6m as at 31 December 2004.

**Notes to the reconciliation of equity and profit as presented in tables A1 and A2, above, and B1 to C5 below (cont'd)**

*(iv)* *Consolidation (IAS 27)*

Consistent with UK GAAP, employee benefit trusts have been consolidated and investments in Group shares treated as treasury shares. Deferred tax of £7.6m which was recognised under UK GAAP, has been derecognised under IFRS, reducing equity by £7.6m at 31 December 2004 as under IAS 12 (Income Tax), the deferred tax asset accumulates over the vesting period and has been accounted for as part of the IFRS 2 adjustments explained above.

IAS 27 requires the consolidation of like items of the Income Statement and Balance Sheet on a line by line basis. Under UK GAAP, F&C Managed Pension Funds Limited (MPF), the Group's insurance subsidiary, was not consolidated on a line by line basis. Specifically, the Income Statement reflected the net surplus on the Technical Account within other income and the Balance Sheet reflected the aggregate amounts of insurance assets and liabilities attributable to policyholders as a single asset and a single liability of equal amount. The IFRS adjustments shown therefore reflect the appropriate classifications of consolidating MPF on a line by line basis in both the Income Statement and the Balance Sheet for each period. There is no change to the previously reported profit or equity for any period as a result of these reclassifications.

*(v)* *Fair value of financial investments (IAS 39)*

In accordance with IAS 39, other financial investments (available for sale) are recognised and measured at their fair value with adjustments to fair value taken directly to equity.

The effect of measuring the Group's private equity investments at fair value is to increase other financial investments by £1.6m and £2.3m at 1 January 2004 and 31 December 2004 respectively. The equity increase of these adjustments, after recognising deferred tax, amounts to £1.2m as at 1 January 2004 and £1.6m as at 31 December 2004.

*(vi)* *Associates (IAS 28)*

IAS 28 requires the Group to recognise its share of the after tax results of associates. Under UK GAAP, this investment was carried at cost and no adjustment was made to the carrying value of investments unless any impairment existed.

As a result, equity has been reduced by £0.1m to reflect the Group's share of associate set-up expenses which were charged directly to reserves. In addition, the recognition of the Group's share of losses has reduced equity by £0.3m as at 31 December 2004.

*(vii)* *Preference shares (IAS 32)*

Under UK GAAP, Preference Shares were classified as share capital. IAS 32, Financial Instruments, requires this class of share capital, which attracts a pre-determined rate of dividends, to be classified as a liability. The impact of this reclassification is to reduce net assets by £0.4m as at 1 January 2004 and by £0.8m as at 31 December 2004.

*(viii)* *Lease incentives (IAS 17)*

Under UK GAAP, the Group amortised leasehold incentives over the period to the date of the first rent review. Under IAS 17, lease incentives are required to be amortised over the period of the lease.

This change reduces profit after tax by £0.2m for the year ended 31 December 2004.

The cumulative reduction in equity as a result of this adjustment amounts to £0.7m as at 1 January 2004 and £0.9m as at 31 December 2004.

*(ix)* *Revenue (IAS 18)*

Under IAS 18, when the outcome of a transaction involving the rendering of services can be estimated reliably, revenue associated with the transaction should be recognised by reference to the stage of completion of the transaction at the balance sheet date. The guidance issued in the appendix to IAS 18 on the application of this principle states that revenues earned on investment management contracts, and related incremental costs associated with such contracts, should be recognised over the life of the contract.

In line with standard industry practice, the Group has previously recognised front end fees and associated costs on the initiation of the contract. Under IAS 18 such revenues and associated costs have been spread over the estimated average life of the contract.

These changes reduce equity by £0.5m as at 1 January 2004 and by £1.6m as at 31 December 2004.

The impact of this treatment is to reduce profits after tax by £1.1m for the year ended 31 December 2004.

# Notes to the **Consolidated Financial Statements**

**Notes to the reconciliation of equity and profit as presented in tables A1 and A2, above, and B1 to C5 below (cont'd)**

(x) *Employee benefits (IAS 19)*

Employee benefit adjustments have been made in accordance with IAS 19 to reflect the short-term employee benefits (accrued holiday entitlement) and long-term employee service benefits not recognised under UK GAAP. The combined impact on profit after tax of these adjustments is to reduce profits by £0.1m for the year ended 31 December 2004. The cumulative impact of employee benefit adjustments amount to a reduction in equity of £0.4m as at 1 January 2004 and £0.5m as at 31 December 2004.

Under UK GAAP (FRS 17), the pension deficit recognised on the Balance Sheet was stated net of the associated deferred tax asset. Under IFRS, the tax asset has been reclassified to be shown within deferred tax. As a result of these adjustments, the pension deficit and the deferred tax asset have increased by £2.3m as at 1 January 2004 and by £5.4m as at 31 December 2004.

(xi) *Foreign exchange movements (IAS 21)*

Under UK GAAP, an exchange gain was recognised on translation of a financial asset. Under IFRS, this gain recognised was reversed, resulting in an increase in loss of £0.3m for the year ended 31 December 2004. In addition, foreign currency gains in respect of intangible management contracts relating to foreign operations, have increased equity by £3.5m as at 31 December 2004. The net impact of the above adjustments is to increase equity by £3.2m as at 31 December 2004.

(xii) *Fair value adjustments (IFRS 3)*

As a result of changes to the fair value of the net assets acquired on acquisition of the F&CGH Group, and a reduction in the accrued consideration payable, a number of Balance Sheet adjustments have been made. These are explained in note 16.

(xiii) *Intangible assets (IAS 38)*

Under UK GAAP capitalised software and licence costs were included within property, plant and equipment. In compliance with IAS 38, these have been reclassified as ''other intangible assets''. The net book value of amounts reclassified were £0.6m as at 1 January 2004 and £0.5m as at 31 December 2004.

## TABLE B1

### Balance Sheet as at 1 January 2004 – effect of IAS 1 'Presentation of Financial Statements' on UK GAAP balances

| | UK GAAP balances in UK GAAP format £000 | Assets £000 | Liabilities £000 | UK GAAP balances in IFRS format £000 | |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | **Non-current assets** |
| Intangible fixed assets | 303,898 | – | – | 303,898 | Goodwill |
| Tangible fixed assets | 8,585 | – | – | 8,585 | Property, plant and equipment |
| Other investments | 7 | – | – | 7 | Other financial investments |
| Insurance assets attributable to unit linked policyholders | 848,905 | (848,905) | – | – | |
| | – | – | – | – | Deferred acquisition costs |
| | – | 3,255 | – | 3,255 | Deferred tax assets |
| **Total fixed assets** | **1,161,395** | | | **315,745** | **Total non-current assets** |
| **Current assets** | | | | | **Current assets** |
| | – | – | – | – | Financial investments |
| | – | 848,905 | – | 848,905 | Insurance and other assets |
| Stock of units and shares | 495 | – | – | 495 | Stock of units and shares |
| Debtors | | | | | |
| Within one year | 43,132 | – | – | 43,132 | Trade and other receivables |
| After more than one year | 3,255 | (3,255) | – | – | |
| | – | – | – | – | Deferred acquisition costs |
| | – | – | – | – | Cash and cash equivalents – policyholders |
| Cash at bank and in hand | 25,770 | – | – | 25,770 | Cash and cash equivalents – shareholders |
| **Total current assets** | **72,652** | | | **918,302** | **Total current assets** |
| | | | | **1,234,047** | **Total assets** |
| **Creditors (amounts falling due within one year)** | | | | | **Liabilities** |
| | | | | | **Non-current liabilities** |
| | – | – | (180,000) | (180,000) | Interest bearing loans and borrowings |
| Current tax | (588) | – | 588 | – | |
| Proposed ordinary dividend | (10,485) | – | 10,485 | – | |
| Other creditors | (55,602) | – | 55,600 | (2) | Other creditors |
| | – | – | (3,936) | (3,936) | Provisions |
| | – | – | (5,459) | (5,459) | Pension deficit |
| | – | – | – | – | Deferred income |
| | – | – | (292) | (292) | Deferred tax liabilities |
| | | | | **(189,689)** | **Total non-current liabilities** |
| **Net current assets** | **5,977** | | | | |
| **Total assets less current liabilities** | **1,167,372** | | | | |
| | | | | | **Current liabilities** |
| **Insurance liabilities attributable to unit linked policyholders** | (848,905) | – | – | (848,905) | Investment contract liabilities |
| | – | – | – | – | Insurance contract liabilities |
| **Creditors (amounts falling due outwith one year)** | (180,002) | – | 165,002 | (15,000) | Interest bearing loans and borrowings |
| | – | – | (30,792) | (30,792) | Trade and other payables |
| | – | – | (9,500) | (9,500) | Employee benefits |
| **Provisions for liabilities and charges** | (3,918) | – | 3,918 | – | |
| **Deferred income** | – | – | – | – | Deferred income |
| | – | – | (588) | (588) | Current tax payable |
| | – | – | (10,485) | (10,485) | Ordinary dividend payable |
| **Net assets excluding pension deficit** | **134,547** | | | | |
| **Pension deficit** | (5,459) | – | 5,459 | – | |
| **Net assets including pension deficit** | **129,088** | | | | |
| | | | | **(915,270)** | **Total current liabilities** |
| | | | | **(1,104,959)** | **Total liabilities** |
| **Capital and reserves** | | | | | **Equity attributable to equity holders of the parent** |
| Called up Ordinary Share capital | (150) | – | – | (150) | Share capital |
| Share premium account | (2,795) | – | – | (2,795) | Share premium account |
| Other reserves – Merger reserve | (117,891) | – | – | (117,891) | Merger reserve |
| – Other reserves | (8,031) | – | – | (8,031) | Other reserves |
| Profit and loss account | 169 | – | – | 169 | Retained earnings |
| Called up Preference Share capital | (390) | – | – | (390) | Preference Share capital |
| **Shareholders' funds** | | | | | |
| Equity | (128,698) | | | | |
| Non-equity | (390) | | | | |
| **Total shareholders' funds** | **(129,088)** | – | – | **(129,088)** | **Total equity** |
| | | | | **(1,234,047)** | **Total liabilities and equity** |

# Notes to the Consolidated Financial Statements

**TABLE B2**

**Balance Sheet as at 1 January 2004 – measurement effect of other IFRS on UK GAAP balances**

| | UK GAAP balances in IFRS format £000 | Dividends IAS10 £000 | Lease Incentives IAS17 £000 | Revenue IAS18 £000 | Employee Benefits IAS19 £000 | Consolidation IAS27 £000 | Intangibles IAS38 £000 | Financial Instruments IAS39/32 £000 | Share Based Payments IRFS2 £000 | Goodwill & Management Contracts IFRS3 £000 | IFRS £000 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | | | |
| **Non-current assets** | | | | | | | | | | | |
| Property, plant and equipment | 8,585 | – | – | – | – | – | (602) | – | – | – | 7,983 |
| Intangible assets: | | | | | | | | | | | |
| – Goodwill | 303,898 | – | – | – | – | – | – | – | – | (49,867) | 254,031 |
| – Management contracts | – | – | – | – | – | – | – | – | – | 88,655 | 88,655 |
| – Other intangible assets | – | – | – | – | – | – | 602 | – | – | – | 602 |
| | 303,898 | – | – | – | – | – | 602 | – | – | 38,788 | 343,288 |
| Other financial investments | 7 | – | – | – | – | – | – | 1,649 | – | – | 1,656 |
| Deferred acquisition costs | – | – | – | 5,531 | – | 633 | – | – | – | – | 6,164 |
| Deferred tax assets | 3,255 | – | 93 | 204 | 2,511 | – | – | – | 336 | – | 6,399 |
| **Total non-current assets** | **315,745** | **–** | **93** | **5,735** | **2,511** | **633** | **–** | **1,649** | **336** | **38,788** | **365,490** |
| **Current assets** | | | | | | | | | | | |
| Financial investments | – | – | – | – | – | 855,188 | – | – | – | – | 855,188 |
| Reinsurance assets | 848,905 | – | – | – | – | (846,498) | – | – | – | – | 2,407 |
| Stock of units and shares | 495 | – | – | – | – | – | – | – | – | – | 495 |
| Trade and other receivables | 43,132 | – | – | – | – | 10,558 | – | – | – | – | 53,690 |
| Deferred acquisition costs | – | – | – | 1,981 | – | – | – | – | – | – | 1,981 |
| Cash and cash equivalents | | | | | | | | | | | |
| – policyholders | – | – | – | – | – | 26,961 | – | – | – | – | 26,961 |
| – shareholders | 25,770 | – | – | – | – | (2,793) | – | – | – | – | 22,977 |
| | 25,770 | – | – | – | – | 24,168 | – | – | – | – | 49,938 |
| **Total current assets** | **918,302** | **–** | **–** | **1,981** | **–** | **43,416** | **–** | **–** | **–** | **–** | **963,699** |
| **Total assets** | **1,234,047** | **–** | **93** | **7,716** | **2,511** | **44,049** | **–** | **1,649** | **336** | **38,788** | **1,329,189** |
| **Liabilities** | | | | | | | | | | | |
| **Non-current liabilities** | | | | | | | | | | | |
| Interest bearing loans and borrowings | (180,000) | – | – | – | – | – | – | (390) | – | – | (180,390) |
| Trade and other payables | (2) | – | – | – | – | – | – | – | – | – | (2) |
| Provisions | (3,936) | – | – | – | – | – | – | – | – | – | (3,936) |
| Pension deficit | (5,459) | – | – | – | (2,339) | – | – | – | – | – | (7,798) |
| Deferred income | – | – | – | (6,841) | – | – | – | – | – | – | (6,841) |
| Deferred tax liabilities | (292) | – | – | – | – | – | – | (496) | – | (26,597) | (27,385) |
| **Total non-current liabilities** | **(189,689)** | **–** | **–** | **(6,841)** | **(2,339)** | **–** | **–** | **(886)** | **–** | **(26,597)** | **(226,352)** |
| **Current liabilities** | | | | | | | | | | | |
| Investment contract liabilities | (848,905) | – | – | – | – | (35,151) | – | – | – | – | (884,056) |
| Insurance contract liabilities | – | – | – | – | – | (3,041) | – | – | – | – | (3,041) |
| Interest bearing loans and borrowings | (15,000) | – | – | – | – | – | – | – | – | – | (15,000) |
| Trade and other payables | (30,792) | – | (796) | – | – | (5,839) | – | – | – | – | (37,427) |
| Employee benefits | (9,500) | – | – | – | (572) | – | – | – | – | – | (10,072) |
| Deferred income | – | – | – | (1,352) | – | – | – | – | – | – | (1,352) |
| Current tax payable | (588) | – | – | – | – | (16) | – | – | – | – | (604) |
| Ordinary dividend payable | (10,485) | 10,485 | – | – | – | – | – | – | – | – | – |
| **Total current liabilities** | **(915,270)** | **10,485** | **(796)** | **(1,352)** | **(572)** | **(44,047)** | **–** | **–** | **–** | **–** | **(951,552)** |
| **Total liabilities** | **(1,104,959)** | **10,485** | **(796)** | **(8,193)** | **(2,911)** | **(44,047)** | **–** | **(886)** | **–** | **(26,597)** | **(1,177,904)** |
| **Equity attributable to equity holders of the parent** | | | | | | | | | | | |
| Share capital | (150) | – | – | – | – | – | – | – | – | – | (150) |
| Share premium account | (2,795) | – | – | – | – | – | – | – | – | – | (2,795) |
| Merger reserve | (117,891) | – | – | – | – | – | – | – | – | – | (117,891) |
| Other reserves | (8,031) | (10,485) | – | – | – | – | – | (1,155) | – | – | (19,671) |
| Retained earnings | 169 | – | 703 | 477 | 400 | – | – | – | (335) | (12,192) | (10,778) |
| Preference Share capital | (390) | – | – | – | – | – | – | 390 | – | – | – |
| **Total equity attributable to equity holders of the parent** | **(129,088)** | **(10,485)** | **703** | **477** | **400** | **–** | **–** | **(765)** | **(335)** | **(12,192)** | **(151,285)** |
| Minority interest | – | – | – | – | – | – | – | – | – | – | – |
| **Total equity** | **(129,088)** | **(10,485)** | **703** | **477** | **400** | **–** | **–** | **(765)** | **(335)** | **(12,192)** | **(151,285)** |
| **Total liabilities and equity** | **(1,234,047)** | **–** | **(93)** | **(7,716)** | **(2,511)** | **(44,047)** | **–** | **(1,651)** | **(335)** | **(38,789)** | **(1,329,189)** |

Rounding differences of up to £2,000 result in minor imbalances within specific adjustments but have no impact on the primary statements.

## TABLE C1

### Income Statement for the year ended 31 December 2004 – effect of IAS 1 'Presentation of Financial Statements' on UK GAAP balances

| | UK GAAP balances in UK GAAP format £000 | Revenues £000 | Amortisation of goodwill £000 | Other expenses £000 | Preference shares £000 | UK GAAP balances in IFRS format £000 | |
|---|---|---|---|---|---|---|---|
| | | | | | | | **Revenues** |
| **Group turnover – continuing operations** | 153,239 | (1,827) | – | – | – | 151,412 | Investment management fees |
| | – | – | – | – | – | – | Investment income attributable to policyholders |
| | – | 2,526 | – | – | – | 2,526 | Other income |
| | | | | | | **153,938** | **Total revenues** |
| Selling expenses | (4,066) | – | – | – | – | (4,066) | Fee and commission expenses |
| **Net revenue** | **149,173** | | | | | **149,872** | **Net revenues** |
| **Administrative expenses** | | | | | | | **Operating expenses** |
| | – | – | – | – | – | – | Losses on financial instruments carried at fair value through profit or loss. |
| | – | – | – | – | – | – | Dealing costs on investment contract assets. |
| Expenses, excluding amortisation of goodwill and Re-Investment Plan costs | (96,075) | – | (33,739) | – | – | (129,814) | Operating expenses |
| Amortisation of goodwill | (33,739) | – | 33,739 | – | – | – | |
| Re-investment Plan costs | (4,583) | – | – | – | – | (4,583) | Re-Investment Plan costs |
| | – | – | – | – | – | – | Amortisation of intangible assets – Management contracts |
| Total administrative expenses | **(134,397)** | | | | | **(134,397)** | **Total operating expenses** |
| Other operating income | 699 | (699) | – | – | – | – | |
| **Group operating profit – continuing operations** | **15,475** | | | | | **15,475** | **Operating profit before restructuring costs** |
| **Exceptional items – continuing operations** | | | | | | | **Restructuring costs** |
| Reorganisation costs post acquisition of F&CGH Group | (18,332) | – | – | – | – | (18,332) | Reorganisation costs post acquisition of F&C GH Group |
| Restructuring: Operations outsourcing | (932) | – | – | – | – | (932) | Operations outsourcing |
| | **(3,789)** | | | | | **(3,789)** | **Operating loss after restructuring costs** |
| Interest and investment income receivable | 2,223 | – | – | 2,848 | – | 5,071 | Finance revenue |
| Other finance expenditure | (10) | – | – | 10 | – | – | |
| Interest payable | (12,222) | – | – | (2,858) | (32) | (15,112) | Finance costs |
| | – | – | – | – | – | – | Share of loss of associates |
| **Loss on ordinary activities before taxation** | **(13,798)** | | | | | **(13,830)** | **Loss before tax** |
| | – | – | – | – | – | – | Tax – Policyholders |
| Tax on loss on ordinary activities | (5,613) | – | – | – | – | (5,613) | Tax – Shareholders |
| **Loss on ordinary activities after taxation** | **(19,411)** | | | | | | |
| Dividend on Cumulative Preference Shares | (32) | – | – | – | 32 | – | |
| **Loss attributable to ordinary shareholders** | **(19,443)** | | | | | **(19,443)** | **Loss after tax** |
| | | | | | | | **Attributable to:** |
| | | | | | | (19,443) | Equity holders of the parent |
| | | | | | | – | Minority interests |
| | | | | | | **(19,443)** | **Loss for the period** |
| | | | | | | | **Memo – dividends** |
| Interim dividend 2004 | (5,993) | – | – | – | – | (5,993) | Interim dividend 2004 |
| Proposed final dividend 2004 | (32,914) | – | – | – | – | (32,914) | Proposed final dividend |
| Adjustment to 2003 final dividend | (2) | – | – | – | – | (2) | Adjustment to 2003 final dividend |
| **Retained loss for the year transferred from reserves** | **(58,352)** | | | | | | |

# Notes to the **Consolidated Financial Statements**

## TABLE C2

### Income Statement for the year ended 31 December 2004 – measurement effect of other IFRS on UK GAAP balances

| | UK GAAP balances in IFRS format £000 | Lease Incentives IAS17 £000 | Revenue IAS18 £000 | Employee Benefits IAS19 £000 | Foreign Exchange IAS21 £000 | Consolidation IAS27 £000 | Associates IAS28 £000 | Share Based Payments IFRS2 £000 | Goodwill & Management Contracts IFRS3 £000 | IFRS £000 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Revenues** | | | | | | | | | | |
| Investment management fees | 151,412 | – | 1,936 | – | – | 1,159 | – | – | – | 154,507 |
| Investment income attributable to policyholders | – | – | – | – | – | 28,047 | – | – | – | 28,047 |
| Other income | 2,526 | – | 1,243 | – | – | (520) | – | – | – | 3,249 |
| **Total revenues** | **153,938** | – | 3,179 | – | – | 28,686 | – | – | – | **185,803** |
| Fee and commission expenses | (4,066) | – | (1,724) | – | – | (47) | – | – | – | (5,837) |
| **Net revenues** | **149,872** | – | 1,455 | – | – | 28,639 | – | – | – | **179,966** |
| **Operating expenses:** | | | | | | | | | | |
| Losses on financial instruments carried at fair value through profit or loss | – | – | – | – | – | (24,373) | – | – | – | **(24,373)** |
| Dealing costs on investment contract assets | – | – | – | – | – | (2,526) | – | – | – | **(2,526)** |
| Operating expenses | (129,814) | (221) | (3,002) | (184) | (297) | (600) | – | (988) | 33,739 | (101,367) |
| Re-Investment Plan costs | (4,583) | – | – | – | – | – | – | (845) | – | (5,428) |
| Amortisation of intangible assets – management contracts | – | – | – | – | – | – | – | – | (20,762) | (20,762) |
| **Total operating expenses** | **(134,397)** | (221) | (3,002) | (184) | (297) | (27,499) | – | (1,833) | 12,977 | **(154,456)** |
| **Operating profit before restructuring costs** | 15,475 | (221) | (1,547) | (184) | (297) | 1,140 | – | (1,833) | 12,977 | 25,510 |
| **Restructuring costs:** | | | | | | | | | | |
| – Re-organisation costs post acquisition of F&CGH Group | (18,332) | – | – | – | – | – | – | – | – | (18,332) |
| – Operations outsourcing | (932) | – | – | – | – | – | – | – | – | (932) |
| **Operating (loss)/profit after restructuring costs** | **(3,789)** | (221) | (1,547) | (184) | (297) | 1,140 | – | (1,833) | 12,977 | **6,246** |
| Finance revenue | 5,071 | – | – | – | – | (430) | – | – | – | 4,641 |
| Finance costs | (15,112) | – | – | (1) | – | 130 | – | – | – | (14,983) |
| Share of loss of associates | – | – | – | – | – | – | (318) | – | – | (318) |
| **Loss before tax** | **(13,830)** | (221) | (1,547) | (185) | (297) | 840 | (318) | (1,833) | 12,977 | **(4,414)** |
| Tax – Policyholders | – | – | – | – | – | (445) | – | – | – | (445) |
| Tax – Shareholders | (5,613) | 27 | 464 | 56 | – | (394) | – | 549 | 6,229 | 1,318 |
| | (5,613) | 27 | 464 | 56 | – | (839) | – | 549 | 6,229 | 873 |
| **Loss after tax** | **(19,443)** | (194) | (1,083) | (129) | (297) | 1 | (318) | (1,284) | 19,206 | **(3,541)** |
| **Attributable to:** | | | | | | | | | | |
| Equity holders of the parent | (19,443) | (194) | (1,083) | (129) | (297) | 1 | (318) | (1,284) | 19,206 | (3,541) |
| Minority interests | – | – | – | – | – | – | – | – | – | – |
| **Loss for the period** | **(19,443)** | (194) | (1,083) | (129) | (297) | 1 | (318) | (1,284) | 19,206 | **(3,541)** |

## TABLE C3

### Balance Sheet as at 31 December 2004 – effect of IAS 1 'Presentation of Financial Statements' on UK GAAP balances

| | UK GAAP balances in UK GAAP format £000 | Assets £000 | Liabilities £000 | Reserves £000 | UK GAAP balances in IFRS format £000 | |
|---|---|---|---|---|---|---|
| **Fixed assets** | | | | | | **Non-current assets** |
| Intangible fixed assets | 955,593 | – | | | 955,593 | Goodwill |
| | – | – | – | – | – | Intangible assets – Management contracts |
| Tangible fixed assets | 11,417 | – | – | – | 11,417 | Property, plant and equipment |
| | – | – | – | – | – | Other intangible assets |
| | – | – | – | – | – | Investment in associates |
| Other investments | 6,814 | – | – | – | 6,814 | Other financial investments |
| Insurance assets attributable to unit linked policyholders | 811,957 | (811,957) | – | – | – | |
| | | | | | – | Deferred acquisition costs |
| | – | 29,213 | – | – | 29,213 | Deferred tax assets |
| **Total fixed assets** | **1,785,781** | | | | **1,003,037** | **Total non-current assets** |
| **Current assets** | | | | | | **Current assets** |
| | – | – | – | – | – | Financial investments |
| | – | 811,957 | – | – | 811,957 | Reinsurance assets |
| Stock of units and shares | 556 | – | – | – | 556 | Stock of units and shares |
| Debtors – amounts falling due: | | | | | | |
| Within one year | 61,794 | – | – | – | 61,794 | Trade and other receivables |
| After more than one year | 29,213 | (29,213) | – | – | – | |
| | – | – | – | – | – | Deferred acquisition costs |
| | – | – | – | – | – | Cash and cash equivalents – policyholders |
| Cash at bank and in hand | 137,171 | – | – | – | 137,171 | Cash and cash equivalents – shareholders |
| **Total current assets** | **228,734** | | | | **1,011,478** | **Total current assets** |
| | | | | | **2,014,515** | **Total assets** |
| **Creditors (amounts falling due within one year)** | | | | | | **Liabilities** |
| | | | | | | **Non-current Liabilities** |
| | – | – | (214,000) | – | (214,000) | Interest bearing loans and borrowings |
| Current tax | (7,390) | – | 7,390 | – | – | |
| Proposed ordinary dividend | (32,914) | – | 32,914 | – | – | |
| Other creditors | (104,461) | – | 104,458 | – | (3) | Trade and other payables |
| | – | – | (6,650) | – | (6,650) | Provisions |
| | – | – | (12,333) | – | (12,333) | Pension deficit |
| | – | – | (3,452) | – | (3,452) | Deferred income |
| | – | – | (322) | – | (322) | Deferred tax liabilities |
| | | | | | **(236,760)** | **Total non-current liabilities** |
| **Net current assets** | **83,969** | | | | | |
| **Total assets less current liabilities** | **1,869,750** | | | | | |
| | | | | | | **Current liabilities** |
| **Insurance liabilities attributable to unit linked policyholders** | (811,957) | – | – | – | (811,957) | Investment contract liabilities |
| | – | – | – | – | – | Insurance contract liabilities |
| | – | – | (5,000) | – | (5,000) | Interest bearing loans and borrowings |
| **Creditors (amounts falling due outwith one year)** | (214,003) | – | 149,427 | – | (64,576) | Trade and other payables |
| | – | – | (34,170) | – | (34,170) | Employee benefits |
| **Provisions for liabilities and charges** | (9,346) | – | 6,972 | – | (2,374) | Provisions |
| **Deferred income** | (3,452) | | 2,737 | – | (715) | Deferred income |
| | – | – | (7,390) | – | (7,390) | Current tax payable |
| | – | – | (32,914) | – | (32,914) | Proposed ordinary dividend |
| **Net assets excluding pension deficit** | **830,992** | | | | | |
| **Pension deficit** | (12,333) | – | 12,333 | – | – | |
| **Net asset including pension deficit** | **818,659** | | | | | |
| | | | | | **(959,096)** | **Total current liabilities** |
| | | | | | **(1,195,856)** | **Total liabilities** |
| **Capital and reserves** | | | | | | **Equity attributable to equity holders of the parent** |
| Called up Ordinary Share capital | (482) | – | – | – | (482) | Share capital |
| Share premium account | (28,956) | – | – | – | (28,956) | Share premium account |
| Other reserves – Merger reserve | (737,207) | – | – | – | (737,207) | Merger reserve |
| Other reserves | (69,119) | – | – | – | (69,119) | Other reserves |
| Profit and loss account | 17,905 | – | – | – | 17,905 | Retained earnings |
| Called up Preference Share capital | (800) | – | – | – | (800) | Preference share capital |
| **Shareholders' funds** | | | | | | |
| Equity | (817,859) | | | | | |
| Non-equity | (800) | | | | | |
| **Total shareholders' funds** | **(818,659)** | | | | **(818,659)** | **Total equity** |
| | | | | | **(2,014,515)** | **Total liabilities and equity** |

# Notes to the Consolidated Financial Statements

## Table C4

### Balance Sheet as at 31 December 2004 – measurement effect of other IFRS on UK GAAP balances

| | UK GAAP Balances in IFRS format | Dividends | Lease Incentives | Revenue | Employee Benefits | Foreign Exchange | Consoli-dation | Associates | Intangibles | Financial Instru-ments | Share Based Payments | Goodwill & Manage-ment Contracts | Fair Value Adjust-ments* | IFRS |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | IAS10 | IAS17 | IAS18 | IAS19 | IAS21 | IAS27 | IAS28 | IAS38 | IAS39 | IFRS2 | IFRS3 | | |
| | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 | £000 |
| **Assets** | | | | | | | | | | | | | | |
| **Non-current assets** | | | | | | | | | | | | | | |
| Property, plant and equipment | 11,417 | – | – | – | – | – | – | – | (506) | – | – | – | 1 | 10,912 |
| Intangible assets | | | | | | | | | | | | | | |
| – Goodwill | 955,593 | – | (21) | 231 | 37 | – | – | – | – | – | – | (377,986) | 92 | 577,946 |
| – Management contracts | – | – | – | – | – | – | – | – | – | – | – | 589,823 | – | 589,823 |
| – Other intangible assets | – | – | – | – | – | – | – | – | 506 | – | – | – | – | 506 |
| | 955,593 | – | (21) | 231 | 37 | – | – | – | 506 | – | – | 211,837 | 92 | 1,168,275 |
| Other financial investments | 6,814 | – | – | – | – | – | – | (5,398) | – | 2,312 | – | – | 467 | 4,195 |
| Investment in associates | – | – | – | – | – | (215) | – | 4,982 | – | – | – | – | – | 4,767 |
| Deferred acquisition costs | – | – | – | 7,808 | – | – | – | – | – | – | – | – | – | 7,808 |
| Deferred tax assets | 29,213 | – | 110 | 768 | 5,545 | – | (7,605) | – | – | – | 2,192 | – | – | 30,223 |
| **Total non-current assets** | **1,003,037** | **–** | **89** | **8,807** | **5,582** | **(215)** | **(7,605)** | **(416)** | **–** | **2,312** | **2,192** | **211,837** | **560** | **1,226,180** |
| **Current assets** | | | | | | | | | | | | | | |
| Financial investments | – | – | – | – | – | – | 813,595 | – | – | – | – | – | – | 813,595 |
| Reinsurance assets | 811,957 | – | – | – | – | – | (809,605) | – | – | – | – | – | – | 2,352 |
| Stock of units and shares | 556 | – | – | – | – | – | – | – | – | – | – | – | – | 556 |
| Trade and other receivables | 61,794 | – | – | – | – | – | 4,304 | – | – | – | – | – | (3,027) | 63,071 |
| Deferred acquisition costs | – | – | – | 1,932 | – | – | 634 | – | – | – | – | – | – | 2,566 |
| Cash and cash equivalents | | | | | | | | | | | | | | |
| – policyholders | – | – | – | – | – | – | 47,145 | – | – | – | – | – | – | 47,145 |
| – shareholders | 137,171 | – | – | – | – | – | (3,232) | – | – | – | – | – | – | 133,939 |
| | 137,171 | – | – | – | – | – | 43,913 | – | – | – | – | – | – | 181,084 |
| **Total current assets** | **1,011,478** | **–** | **–** | **1,932** | **–** | **–** | **52,841** | **–** | **–** | **–** | **–** | **–** | **(3,027)** | **1,063,224** |
| **Total assets** | **2,014,515** | **–** | **89** | **10,739** | **5,582** | **(215)** | **45,236** | **(416)** | **–** | **2,312** | **2,192** | **211,837** | **(2,467)** | **2,289,404** |
| **Liabilities** | | | | | | | | | | | | | | |
| **Non-current Liabilities** | | | | | | | | | | | | | | |
| Interest bearing loans and borrowings | (214,000) | – | – | – | – | – | – | – | – | (800) | – | – | – | (214,800) |
| Trade and other payables | (3) | – | – | – | – | – | – | – | – | – | – | – | – | (3) |
| Provisions | (6,650) | – | – | – | (170) | – | – | – | – | – | – | – | (3,502) | (10,322) |
| Pension deficit | (12,333) | – | – | – | (5,374) | – | – | – | – | – | – | – | – | (17,707) |
| Deferred income | (3,452) | – | – | (7,300) | – | – | – | – | – | – | – | – | – | (10,752) |
| Deferred tax liabilities | (322) | – | – | – | – | – | – | – | – | (694) | – | (176,947) | – | (177,963) |
| **Total non-current liabilities** | **(236,760)** | **–** | **–** | **(7,300)** | **(5,544)** | **–** | **–** | **–** | **–** | **(1,494)** | **–** | **(176,947)** | **(3,502)** | **(431,547)** |
| **Current liabilities** | | | | | | | | | | | | | | |
| Investment contract liabilities | (811,957) | – | – | – | – | – | (50,351) | – | – | – | – | – | – | (862,308) |
| Insurance contract liabilities | – | – | – | – | – | – | (2,352) | – | – | – | – | – | – | (2,352) |
| Interest bearing loans and borrowings | (5,000) | – | – | – | – | – | – | – | – | – | – | – | – | (5,000) |
| Trade and other payables | (64,576) | – | (987) | – | – | – | (841) | – | – | – | – | – | 5,130 | (61,274) |
| Provisions | (2,374) | – | – | – | – | – | – | – | – | – | – | – | (160) | (2,534) |
| Employee benefits | (34,170) | – | – | – | (599) | – | – | – | – | – | (562) | – | – | (35,331) |
| Deferred income | (715) | – | – | (4,999) | – | – | 715 | – | – | – | – | – | – | (4,999) |
| Current tax payable | (7,390) | – | – | – | – | – | (11) | – | – | – | – | – | 1,000 | (6,401) |
| Ordinary dividend payable | (32,914) | 32,914 | – | – | – | – | – | – | – | – | – | – | – | – |
| **Total current liabilities** | **(959,096)** | **32,914** | **(987)** | **(4,999)** | **(599)** | **–** | **(52,840)** | **–** | **–** | **–** | **(562)** | **–** | **5,970** | **(980,199)** |
| **Total liabilities** | **(1,195,856)** | **32,914** | **(987)** | **(12,299)** | **(6,143)** | **–** | **(52,840)** | **–** | **–** | **(1,494)** | **(562)** | **(176,947)** | **2,468** | **(1,411,746)** |
| **Equity attributable to equity holders of the parent** | | | | | | | | | | | | | | |
| Share capital | (482) | – | – | – | – | – | – | – | – | – | – | – | – | (482) |
| Share premium account | (28,956) | – | – | – | – | – | – | – | – | – | – | – | – | (28,956) |
| Merger reserve | (737,207) | – | – | – | – | – | – | – | – | – | – | (12,547) | – | (749,754) |
| Other reserves | (69,119) | (32,914) | – | – | – | (1,352) | – | 98 | – | (1,618) | – | (3,496) | – | (108,401) |
| Retained earnings | 17,905 | – | 897 | 1,560 | 562 | 1,568 | 7,604 | 318 | – | – | (1,630) | (18,849) | – | 9,935 |
| Preference share capital | (800) | – | – | – | – | – | – | – | – | 800 | – | – | – | – |
| **Total equity attributable to equity holders of the parent** | **(818,659)** | **(32,914)** | **897** | **1,560** | **562** | **216** | **7,604** | **416** | **–** | **(818)** | **(1,630)** | **(34,892)** | **–** | **(877,658)** |
| Minority interest | – | – | – | – | – | – | – | – | – | – | – | – | – | – |
| **Total equity** | **(818,659)** | **(32,914)** | **897** | **1,560** | **562** | **216** | **7,604** | **416** | **–** | **(818)** | **(1,630)** | **(34,892)** | **–** | **(877,658)** |
| **Total liabilities and equity** | **(2,014,515)** | **–** | **(90)** | **(10,739)** | **(5,581)** | **216** | **(45,236)** | **416** | **–** | **(2,312)** | **(2,192)** | **(211,839)** | **2,468** | **(2,289,404)** |

*Relating to the acquisition of F&CGH Group.
Rounding differences of up to £2,000 result in minor imbalances within specific adjustments but have no impact on the primary statements.

### Table C5

**Cash Flow Statement for the year ended 31 December 2004 – effect of IFRS adjustments**

| | UK GAAP Year ended 31 December 2004 £000 | Consolidation IAS 27 £000 | IFRS Year ended 31 December 2004 £000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating profit before restructuring costs | 24,370 | 1,140 | **25,510** |
| Cash outflow relating to restructuring costs | (9,157) | – | **(9,157)** |
| **Adjustments for non-cash items** | 32,858 | – | **32,858** |
| **Changes in working capital and provisions** | (33,763) | 19,133 | **(14,630)** |
| **Cash generated from operating activities** | 14,308 | 20,273 | **34,581** |
| Income tax paid | (6,608) | – | **(6,608)** |
| **Net cash inflow from operating activities** | 7,700 | 20,273 | **27,973** |
| **Cash flows from investing activities** | | | |
| Acquisition of property, plant and equipment | (4,066) | – | **(4,066)** |
| Payment to increase investment in associate | (5,101) | – | **(5,101)** |
| Rebate of consideration on RSAI acquisition | 3,893 | – | **3,893** |
| Expenses of F&CGH Group acquisition | (11,998) | – | **(11,998)** |
| Net cash acquired with subsidiary undertakings | 132,791 | – | **132,791** |
| Investment income from investing activities | 2,206 | (528) | **1,678** |
| **Net cash inflow/(outflow) from investing activities** | 117,725 | (528) | **117,197** |
| **Cash flows from financing activities** | | | |
| Proceeds from issue of share capital | 822 | – | **822** |
| Drawdown of revolving credit facility from FP Group | 5,000 | – | **5,000** |
| Repayment of revolving credit facility from FP Group | (15,000) | – | **(15,000)** |
| Proceeds from long-term borrowings | 25,000 | – | **25,000** |
| Interest paid on loans | (11,299) | – | **(11,299)** |
| Other interest paid | (879) | – | **(879)** |
| Equity dividends paid | (16,480) | – | **(16,480)** |
| Preference dividends paid | (23) | – | **(23)** |
| Purchase of own shares | (1,165) | – | **(1,165)** |
| **Net cash outflow from financing activities** | (14,024) | – | **(14,024)** |
| **Net increase in cash and cash equivalents** | 111,401 | 19,745 | **131,146** |
| Cash and cash equivalents at 1 January | 25,770 | 24,168 | **49,938** |
| **Cash and cash equivalents at 31 December** | 137,171 | 43,913 | **181,084** |
| **Cash and cash equivalents** | | | |
| Shareholders | 137,171 | (3,232) | **133,939** |
| Policyholders | – | 47,145 | **47,145** |
| | 137,171 | 43,913 | **181,084** |

# Five Year Record

### Historical summaries

*IFRS has been adopted for the years ending 31 December 2004 and 2005. For the years ending 31 December 2001, 2002 and 2003 the Group Financial Statements have been prepared under UK GAAP. The five year historical summaries are not directly comparable. The main changes which would be required for the years ended 31 December 2001, 2002 and 2003 to comply with IFRS relate to both presentational and measurement items. Details of changes for year-ended 31 December 2004 are disclosed in Note 42.*

| Group profit and loss accounts | UK GAAP 2001 £000 | UK GAAP 2002 £000 | UK GAAP 2003# £000 |
|---|---|---|---|
| **Turnover** | | | |
| Group and share of joint venture | 87,151 | 90,041 | 110,629 |
| Share of joint venture | (941) | (721) | – |
| Group turnover | 86,210 | 89,320 | 110,629 |
| Selling expenses | (2,695) | (1,744) | (2,735) |
| **Net revenue** | 83,515 | 87,576 | 107,894 |
| Administrative expenses | | | |
| Expenses, excluding amortisation of goodwill and Reinvestment Plan costs | (61,236) | (64,101) | (73,513) |
| Amortisation of goodwill | (7,145) | (15,280) | (22,153) |
| Total administrative expenses | (68,381) | (79,381) | (95,666) |
| Other operating income | 1,665 | 1,241 | 1,081 |
| **Group operating profit** | 16,799 | 9,436 | 13,309 |
| Share of operating loss in joint venture | (212) | (33) | (15) |
| Total operating profits of the group and share of joint venture | 16,587 | 9,403 | 13,294 |
| Exceptional costs | (2,268) | (19,169) | (12,334) |
| (Loss)/gain on disposal of subsidiary undertaking | (170) | – | 1,000 |
| Other finance income/(expenditure) | 510 | 351 | (174) |
| Interest and investment income receivable | 3,179 | 2,473 | 1,006 |
| Interest payable | (260) | (5,924) | (11,359) |
| **Profit/(loss) on ordinary activities before taxation** | 17,578 | (12,866) | (8,567) |
| Tax on profit/(loss) on ordinary activities | (7,015) | (286) | (3,154) |
| **Profit/(loss) on ordinary activities after taxation** | 10,563 | (13,152) | (11,721) |
| Dividend on Cumulative Preference Shares | (30) | (26) | (19) |
| **Profit/(loss) attributable to ordinary shareholders** | 10,533 | (13,178) | (11,740) |
| Interim dividend | (5,980) | (5,996) | (5,994) |
| Final dividend | (10,470) | (10,494) | (10,485) |
| Transferred from reserves | (5,917) | (29,668) | (28,219) |
| Earnings per Ordinary Share before amortisation of goodwill, gain on disposal of subsidiary undertaking and exceptional costs | 13.57p | 10.36p | 12.04p |
| Earnings/(loss) per Ordinary Share | 7.30p | (8.80)p | (7.83)p |
| Diluted earnings/(loss) per Ordinary Share | 7.30p | (8.80)p | (7.83)p |
| **Dividends** | | | |
| Interim dividend per Ordinary Share | 4.00p | 4.00p | 4.00p |
| Final dividend per Ordinary Share | 7.00p | 7.00p | 7.00p |
| | 11.00p | 11.00p | 11.00p |
| **Dividend cover** | 0.64 | (0.80) | (0.71) |
| Dividend cover before amortisation of goodwill, gain on disposal of subsidiary undertakings and exceptional costs | 1.19 | 0.94 | 1.10 |

# The accounts for the year ended 31 December 2003 have been restated in order to comply with UITF 38 'Accounting for ESOP Trusts'.

## Historical summaries (cont'd)

| Consolidated Income Statements | IFRS* 2004 £000 | IFRS 2005 £000 |
|---|---|---|
| **Revenues** | | |
| Investment management fees | 154,507 | **277,356** |
| Investment income attributable to policyholders | 28,047 | **28,918** |
| Other income | 3,249 | **691** |
| **Total revenues** | 185,803 | **306,965** |
| Fee and commission expenses | (5,837) | **(10,895)** |
| **Net revenues** | 179,966 | **296,070** |
| **Operating expenses** | | |
| Losses on financial instruments carried at fair value through profit or loss | (24,373) | **(26,408)** |
| Dealing costs on investment contract assets | (2,526) | **(1,226)** |
| **Net operating costs: investment and insurance contracts** | (26,899) | **(27,634)** |
| Operating expenses | (101,367) | **(150,695)** |
| Re-Investment Plan costs | (5,428) | **(22,162)** |
| Impairment of intangible assets – management contracts | – | **(111,500)** |
| Amortisation of intangible assets – management contracts | (20,762) | **(55,801)** |
| **Total operating expenses before restructuring costs** | (154,456) | **(367,792)** |
| **Operating profit/(loss) before restructuring costs** | 25,510 | **(71,722)** |
| Restructuring costs: | | |
| – Reorganisation costs post acquisition of F&CGH Group | (18,332) | **(22,405)** |
| – Operations outsourcing | (932) | **(2,235)** |
| **Operating profit/(loss) after restructuring costs** | 6,246 | **(96,362)** |
| Finance revenue | 4,641 | **15,570** |
| Finance costs | (14,983) | **(19,495)** |
| Impairment in associate and other financial investment | – | **(5,026)** |
| Loss on disposal of subsidiaries | – | **(672)** |
| Share of loss of associates | (318) | **(339)** |
| **Loss before tax** | (4,414) | **(106,324)** |
| Tax – Policyholders | (445) | **(118)** |
| Tax – Shareholders | 1,318 | **29,169** |
| Tax income | 873 | **29,051** |
| **Loss for the year** | (3,541) | **(77,273)** |
| **Attributable to:** | | |
| Equity holders of the parent | (3,541) | **(77,273)** |
| Minority interests | – | **–** |
| **Loss for the year** | (3,541) | **(77,273)** |
| Earnings per Ordinary Share before amortisation and impairment of intangibles, restructuring costs, and the cost of the Re-Investment Plan | 12.76p | **15.90p** |
| Loss per Ordinary Share | (1.60)p | **(16.36)p** |
| Diluted loss per Ordinary Share | (1.56)p | **(15.77)p** |
| **Dividends** | | |
| Memo | | |
| Final dividend for 2003 and 2004 | 10,487 | **32,952** |
| Interim dividend for 2004 and 2005 | 5,993 | **18,865** |
| | 16,480 | **51,817** |
| Final dividend per Ordinary Share for 2003 and 2004 | 7.0p | **7.0p** |
| Interim dividend per Ordinary Share for 2004 and 2005 | 4.0p | **4.0p** |
| **Dividend cover†** | (0.21) | **(1.58)** |
| Dividend cover before amortisation and impairment of intangibles, restructuring costs and the cost of the Re-Investment Plan† | 1.72 | **1.45** |

* as restated for IFRS
† based on the dividends paid during 2004 and 2005

# F&C Asset Management plc
# Company Financial Statements
**for the year ended 31 December 2005**

**These Financial Statements have been prepared in accordance with UK GAAP.**
**The Consolidated Financial Statements of the F&C Asset Management Group, given on pages 61 to 159, have been prepared in accordance with IFRS.**

# Statement of Directors' Responsibilities for the Company

The following statement, which should be read in conjunction with the Independent Auditors' Report set out on pages 164 to 165, is made with a view to distinguishing for members the respective responsibilities of the Directors and of the auditors in relation to the financial statements.

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company as at the end of the financial year and of the profit or loss of the Company for the financial year.

The Directors consider that in preparing the Company's financial statements on pages 166 to 189, the Company has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all accounting standards which they consider to be applicable have been followed (subject to any material departures disclosed and explained in the notes to the financial statements).

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

# Independent Auditors' Report to the Shareholders of F&C Asset Management plc

We have audited the parent company financial statements of F&C Asset Management plc for the year ended 31 December 2005 which comprise a Balance Sheet and the related notes 1 to 22. These parent Company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Group financial statements of F&C Asset Management plc for the year ended 31 December 2005.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an 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 Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the parent Company financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the parent company financial statements and the part of the Directors' Remuneration Report to be audited 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 parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the parent company financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the Financial and Business Highlights, Key Highlights of 2005, Chairman's Statement, Chief Executive's Report, Corporate Responsibility Report, Non-executive Directors, Executive Directors, Report of the Directors, Directors' Report on Corporate Governance, the unaudited part of the Directors' Remuneration Report, Notice of the Annual General Meeting and Corporate Information. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent Company financial statements. Our responsibilities do not extend to any other information.

### Basis of audit opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the parent company financial statements and the part of the Directors' Remuneration Report to be audited 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 parent company financial statements and the part of the Directors' Remuneration Report to be audited.

### Opinion

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 December 2005; and
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP

ERNST & YOUNG LLP
Registered Auditor
Edinburgh

10 April 2006

# Company Balance Sheet

| | Notes | As at 31 December 2005 £000 | As at 31 December 2004 (as restated) £000 |
|---|---|---|---|
| **Fixed assets** | | | |
| Intangible fixed assets | 5 | **1,208** | – |
| Tangible fixed assets | 6 | **4,189** | 3,565 |
| Investments in subsidiaries | 7 | **1,048,329** | 1,061,599 |
| Other investments | 8 | **2,086** | 7,415 |
| | | **1,055,812** | 1,072,579 |
| **Current assets** | | | |
| Debtors – amounts falling due: | | | |
| Within one year | 9 | **67,047** | 45,239 |
| Outwith one year | 9 | **2,926** | 801 |
| Cash and short-term deposits | | **100** | 1,485 |
| | | **70,073** | 47,525 |
| **Creditors (amounts falling due within one year)** | 10 | **(31,045)** | (28,182) |
| **Net current assets** | | **39,028** | 19,343 |
| **Total assets less current liabilities** | | **1,094,840** | 1,091,922 |
| **Creditors (amounts falling due outwith one year)** | 10 | **(65,800)** | (50,800) |
| **Provisions for liabilities** | 11 | **(2,813)** | (2,003) |
| **Net assets excluding pension deficit** | | **1,026,227** | 1,039,119 |
| **Pension deficit** | 14 | **(15,655)** | (6,498) |
| **Net assets including pension deficit** | | **1,010,572** | 1,032,621 |
| **Capital and reserves** | | | |
| Called up ordinary share capital | 15, 16 | **484** | 482 |
| Share premium account | 16 | **30,730** | 28,956 |
| Merger reserve | 16 | **912,674** | 912,674 |
| Other reserves | 16 | **51,675** | 103,651 |
| Profit and loss account | 16 | **15,009** | (13,142) |
| **Total shareholders' funds** | 16 | **1,010,572** | 1,032,621 |

The financial statements were approved by the Board of Directors and authorised for issue on 10 April 2006. They were signed on its behalf by:

Robert Jenkins
*Chairman*

10 April 2006

Alain Grisay
*Chief Executive*

10 April 2006

# Accounting Policies

### Basis of preparation

The separate financial statements of the Company are presented as required by the Companies Act and are prepared under the historical cost convention and in accordance with applicable accounting standards in the United Kingdom

In accordance with Section 230 of the Companies Act 1985 a separate Profit and Loss Account for the Company is not presented.

Comparatives have been restated after the adoption of the following UK GAAP standards which became effective during the year:

FRS 20 – Share-based Payment
FRS 21 – Events after the Balance Sheet Date
FRS 22 – Earnings per Share
FRS 23 – The Effects of Changes in Foreign Exchange Rates
FRS 25 – Financial Instruments: Disclosure and Presentation
FRS 26 – Financial Instruments: Measurement

The financial impacts of their related adjustments are shown in note 1.

The Company has taken advantage of the exemption in FRS 25 and has not disclosed the information required by paragraphs 51 to 95 of that standard because the Company is included in the Group's Consolidated Financial Statements which are publicly available and include disclosures given under IAS 32.

### Turnover

Turnover comprises income from investment management services.

Asset management fees, investment advisory fees and other revenue generated by the Company's investment management activities are recognised in the Profit and Loss Account over the period for which these investment management services are provided.

Performance fees are recognised when the quantum of the fee can be estimated reliably, which is when the performance period ends, when this occurs on or before the reporting date, or where there is a period of less than six months remaining to the end of the performance period and there is evidence at the reporting date which suggests that the current performance will be sustainable.

### Dividend recognition

Dividend receivables and liabilities are only recognised when the dividends have been declared and approved or the date of payment for interim dividends.

### Intangible fixed assets

Intangible fixed assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible fixed assets are carried at cost less accumulated amortisation and any accumulated impairment losses.

The useful lives of management contracts are finite and are amortised on a straight line basis over their estimated average contract term, depending on the nature of the contract, with amortisation being charged to the Profit and Loss Account. The amortisation period is reviewed at each financial year-end. The estimated useful lives have been assessed as being 20 years from date of acquisition.

### Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses.

Expenditure on tangible fixed assets is capitalised on initial recognition. Subsequent expenditure is only capitalised when it is probable that there will be future economic benefits associated with the expenditure which can be measured reliably. All other expenditure is recognised in the Profit and Loss Account as an expense as incurred.

Tangible fixed assets are depreciated so as to write off the cost of assets, using the straight line method, over their estimated useful lives, as follows:

| | | |
|---|---|---|
| Leasehold improvements | – | 10 years |
| Office furniture & equipment | – | 3-5 years |
| Computer equipment | – | 3 years |

The carrying value of assets and their useful lives are reviewed at each reporting date. If an indication of impairment exists, the assets are written down to their recoverable amount and the impairment is charged to the Profit and Loss Account in the year in which it arises.

# Accounting Policies

**Financial instruments**

When financial instruments are recognised initially they are measured at fair value plus directly attributable transaction costs.

Financial instruments are classified into the categories described below:

(i) *Available for sale financial assets* are carried at fair value in the Balance Sheet. In respect of unquoted instruments, or where the market for a financial instrument is not active, fair value is established by using recognised valuation methodologies, in accordance with International Private Equity and Venture Capital Valuation Guidelines.

For unquoted investments in early stage enterprises and enterprises with revenues but without significant profits or significant positive cash flows, fair value is determined using the Price of a Recent Investment Method. After an appropriate period, an assessment is made as to whether either the circumstances of the investment have changed such that another valuation methodology is appropriate, and whether there is any evidence of deterioration or strong defensible evidence of an increase in value. In the absence of these indicators fair value is determined to be that reported at the previous balance sheet date.

Unquoted investments with revenues, maintainable profits and/or maintainable cash flows are valued by deriving an Enterprise Value of the underlying business.

Movements in fair value, other than impairment losses and foreign exchange movements on monetary assets, are taken to the fair value reserve in equity until derecognition of the asset, at which time the cumulative amount in this reserve is recognised in the Profit and Loss Account. The following assets are classified as *Available for sale*:

- Fixed assets
  - Other investments

  The fair value of instruments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date.

(ii) *Loans and receivables* are measured on initial recognition at fair value plus any incremental costs incurred. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest rate method. Gains and losses are recognised in the Profit and Loss Account when loans and receivables are derecognised or impaired, as well as through the amortisation process. The following assets and liabilities are classified as *Loans and receivables*:

- Current assets:
  - Debtors due within one year
  - Loan to investee company due outwith one year
- Creditors (amounts falling due within one year)
- Creditors (amounts falling due outwith one year)

  The Company has adopted "trade date" accounting. Accordingly, financial investments are recognised on the date the Company commits to the purchase of the investments, and are derecognised on the date it commits to their sale.

  Investments in subsidiaries are carried at cost less any impairment.

**Derecognition of financial assets and liabilities**

*Financial assets*

A financial asset or, where applicable, a part of a financial asset, is derecognised when the rights to receive cash flows from the asset have expired.

*Financial liabilities*

A financial liability is derecognised when the obligation under the liability is either discharged, cancelled or expires.

### Impairment of financial assets

The Company assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

*Assets carried at amortised cost*

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective yield. The carrying amount of the asset shall be reduced and the amount of the loss shall be recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the Profit and Loss Account to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

*Assets carried at cost*

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

*Available for sale financial assets*

If an available for sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from equity to the Profit and Loss Account. Reversals in respect of equity instruments classified as available for sale are not recognised in the Profit and Loss Account. Reversals of impairment losses on debt instruments are reversed through the Profit and Loss Account, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the Profit and Loss Account.

### Deferred taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay less or receive more tax, with the following exceptions:

- Provision is made for tax on gains arising from the revaluation (and similar fair value adjustments) of fixed assets, or gains on disposal of fixed assets that have been rolled over into replacement assets, only to the extent that, at the balance sheet date, there is a commitment to dispose of the assets concerned. However, no provision is made where, on the basis of all available evidence at the balance sheet date, it is more likely than not that the taxable gain will be rolled over into replacement assets and charged to tax only when the replacement assets are sold.
- Provision is made for deferred tax that would arise on remittance of the retained earnings of overseas subsidiaries only to the extent that, at the balance sheet date, dividends have been accrued as receivable.
- Deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the underlying timing differences can be deducted.

Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

### Operating leases

Rentals paid under operating leases are charged to the Profit and Loss Account on a straight line basis over the lease term.

Lease incentives are recognised by the Company as a reduction of the rental expense, allocated on a straight line basis, over the shorter of the lease term and a period ending on a date from which it is expected the prevailing market rental will be payable.

### Accounting for Employee Share Option Plan (ESOP) Trusts

UITF38 requires that own shares arising through an ESOP trust be deducted in arriving at shareholders' funds until they vest unconditionally to the employees. Consideration paid and received for the purchase or sale of these shares are included in shareholders' funds and no gain or loss is recognised. Other assets and liabilities of the ESOP trusts are recognised as assets and liabilities of the sponsoring company.

# Accounting Policies

Equity of the Company is held by ESOP trusts in order to satisfy a number of F&C Group share-based payment plans and future exercises of options and awards by employees of subsidiary companies. The cost relating to the share-based payment plans are recognised in the subsidiary companies which employ the staff in receipt of awards, and the Company recognises any fresh issue of shares or re-issue of treasury shares when it occurs. These shares are included in the financial statements of the Company as a deduction from shareholders' funds. The Trustees of the ESOP trusts have waived their right to the dividend entitlement on these shares.

### Provisions

A provision is recognised in the Balance Sheet when the Company has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. No provision is established where a reliable estimate of the obligation cannot be made.

Where the Company expects some or all of a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

Where the Company has obligations under property leases and where the space has ceased to be used for the purposes of the business, full provision is made for future net outstanding liabilities under such leases after taking into account the effect of any expected sub-letting arrangements.

### Pension costs

The Company operates a pension scheme providing benefits on final pensionable salary. The pension scheme assets are measured using market value. Pension scheme liabilities are measured using a Projected Unit Method and discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability. Past service costs arise when the Company makes a commitment to provide a higher level of benefit than previously promised. Past service costs are recognised in the Profit and Loss Account on a straight line basis over the period in which the increases in benefit vest.

The surplus/(deficit) in a defined benefit scheme is the excess/(shortfall) of the value of the assets in the scheme compared against the present value of the scheme liabilities and is recognised as an asset/(liability) of the Company.

Any scheme asset reflects the amount that can be recovered through reduced contributions in the future, being the present value of the liability expected to arise from future service by current scheme members less the present value of future employee contributions. The present value of the reduction in future contributions is determined using the discount rate applied to measure the defined benefit liability. The deferred tax relating to the defined benefit asset or liability is offset against the defined benefit asset or liability and not included with other deferred tax assets or liabilities.

The increase in the present value of the liabilities of the Company's defined benefit pension scheme expected to arise from employee service in the period is charged to operating profit. The expected returns on the scheme assets and the increase during the period in the present value of the scheme liabilities arising from the passage of time are included in other finance income or expenditure. Actuarial gains and losses are recognised directly in reserves.

### Related party disclosures

FRS 8, 'Related Party Disclosures' requires disclosure of the details of material transactions between the reporting entity and related parties. The Company has taken advantage of the exemption in FRS 8 not to disclose transactions between F&C Group companies which eliminate on consolidation.

### Foreign currencies

The Company's financial statements are presented in pounds Sterling, the Company's functional and presentation currency.

Transactions in foreign currencies are translated to the functional currency at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the exchange rate ruling at the balance sheet date, and any exchange differences arising are taken to the Profit and Loss Account.

Non-monetary assets and liabilities measured at historical cost in a foreign currency are translated using the exchange rate at the date of transaction and are not subsequently restated. Non-monetary assets and liabilities stated at fair value in a foreign currency are translated at the exchange rate at the date the fair value was determined. When fair value movements in assets and liabilities are reflected in the Profit and Loss Account, the corresponding exchange movements are also recognised in the Profit and Loss Account. Conversely, when fair value movements in assets and liabilities are reflected directly in reserves, the corresponding exchange movements are also recognised directly in reserves.

### Share capital

When shares are issued, any component that creates a financial liability of the Company is presented as a liability in the Balance Sheet, measured initially at fair value, net of transaction costs and thereafter at amortised cost until extinguished on conversion or redemption.

The remainder of the proceeds on issue is allocated to the equity component and included in shareholders' funds, net of transaction costs.

*Preference share capital*

The Company's issued preference share capital is classified as a liability. It is carried at amortised cost in the Balance Sheet. Preference dividends are recognised in the Profit and Loss Account as an interest expense as they accrue.

### Cash Flow Statement

The Company has taken advantage of the exemptions in FRS 1 (revised) 'Cash Flow Statements' and has elected not to prepare its own Cash Flow Statement as it is included within the Consolidated Cash Flow Statement in the Group financial statements of F&C Asset Management plc.

# Notes to the **Financial Statements**

## 1. Restatement of prior year

### (a) Summary reconciliation of changes in profit/(loss) after tax for the year ended 31 December 2004

| | | Year ended 31 December 2004 £000 |
|---|---|---|
| **UK GAAP loss on ordinary activities after tax (as previously reported)** | | (375) |
| Dividends receivable from subsidiaries | (i) | 12,150 |
| Share-based payments | (ii) | 3,792 |
| Foreign exchange movements | (iii) | (297) |
| Interest on Preference Shares | (iv) | (32) |
| Increase in profit | | 15,613 |
| **UK GAAP profit on ordinary activities after tax (as restated)** | | 15,238 |

**Notes to the reconciliation of profit/(loss) and Balance Sheet as presented in tables above and below.**

Details of the UK GAAP adjustments are set out below.

(i) *Dividends (FRS 21)*

Dividends receivable from subsidiary undertakings which declared a dividend after the period and in respect of the period to the balance sheet date were previously recognised in the accounts for that period. Under FRS 21 dividends are recognised as a liability in the period in which they are declared. As a result, profit for the year ended 31 December 2004 is increased by the excess of the subsidiary companies' 2003 proposed final dividends over those proposed for 2004.

Dividends declared by the Company after the period end in respect of the period to the balance sheet date were previously recognised in the financial statements for that period. Under FRS 21 dividends are recognised as a liability in the period in which they are declared. As a result, the Company's retained earnings at each balance sheet date were increased to the extent that the current year final dividend exceeds the previous year's final dividend and current liabilities are decreased by the amount of the final dividend. The effect of this adjustment was to decrease current liabilities by £10,485,000 and £32,914,000 at 1 January 2004 and 31 December 2004 respectively, as shown in notes 1(b) and 1(c).

(ii) *Share-based payments (FRS 20)*

Previously, because the Company was regarded as the controlling party of the ESOP trusts for accounting purposes, the share-based payment related charge was reflected in the Company's accounts.

Under FRS 20, the cost relating to the share-based payment plans are reflected in the subsidiary companies which employ the staff and the Company recognises any fresh issue of shares or re-issue of treasury shares when it occurs. Accordingly, on restatement, following adoption of FRS 20, a net charge of £3,792,000 has been reversed in 2004.

The deferred tax asset previously recognised in connection with share-based payment expenses of £13,000 at 1 January 2004 and £8,275,000 at 31 December 2004, has also been reversed, reducing net assets and reserves by these amounts. In addition, a related provision for National Insurance contributions of £330,000 has been reversed at 31 December 2004.

(iii) *Foreign Exchange Movements (FRS 23)*

Previously, an exchange gain was recognised on translation of a financial asset. Under FRS 23, the gain recognised was reversed, resulting in a reduction in profit and shareholders' funds of £297,000 in the year ended 31 December 2004 as shown in note 1(c).

(iv) *Financial instruments: Disclosure and Presentation (FRS 25)*

Previously, Preference Shares were classified as share capital. FRS 25 requires this class of share capital, which attracts a pre-determined rate of dividends, to be classified as a liability. The impact of this reclassification is to reduce net assets by £390,000 as at 1 January 2004 and by £800,000 as at 31 December 2004 as shown in notes 1(b) and 1(c). As a result, the dividends are accounted for as an interest charge in the Profit and Loss Account reducing profit in 2004 by £32,000.

(v) *Financial instruments: Measurement (FRS 26)*

In accordance with FRS 26, other financial investments (available for sale) are recognised and measured at their fair value with adjustments to fair value taken directly to reserves.

The effect of measuring the Company's available for sale investments at fair value is to increase other financial investments by £1,650,000 and £2,312,000 at 1 January 2004 and 31 December 2004 respectively as shown in notes 1(b) and 1(c). The increase in reserves from these adjustments, after recognising deferred tax, amounts to £1,155,000 as at 1 January 2004 and £1,618,000 as at 31 December 2004.

## 1. Restatement of prior year (cont'd)

### (b) Balance Sheet as at 1 January 2004 – effect of prior year adjustments

| | As previously reported £000 | Dividends £000 | Reclassification of preference shares £000 | Revaluation of available for sale investments £000 | Share-based payments £000 | As restated £000 |
|---|---|---|---|---|---|---|
| **Fixed assets** | | | | | | |
| Tangible fixed assets | 4,293 | – | – | – | – | 4,293 |
| Investments in subsidiaries | 295,325 | – | – | – | – | 295,325 |
| Other investments | 2 | – | – | 1,650 | – | 1,652 |
| **Total fixed assets** | 299,620 | – | – | 1,650 | – | 301,270 |
| **Current assets** | | | | | | |
| Debtors (amounts falling due within one year) | 33,662 | (17,950) | – | – | – | 15,712 |
| Debtors (amounts falling due outwith one year) | 900 | – | – | – | (13) | 887 |
| Cash and short-term deposits | 8,523 | – | – | – | – | 8,523 |
| **Total current assets** | 43,085 | (17,950) | – | – | (13) | 25,122 |
| **Creditors (amounts falling due within one year)** | | | | | | |
| Proposed ordinary dividend | (10,485) | 10,485 | – | – | – | – |
| Other creditors | (17,442) | – | – | – | – | (17,442) |
| **Net current assets** | 15,158 | (7,465) | – | – | (13) | 7,680 |
| **Total assets less current liabilities** | 314,778 | (7,465) | – | 1,650 | (13) | 308,950 |
| **Creditors (amounts falling due outwith one year)** | (2,234) | – | (390) | – | – | (2,624) |
| **Provisions for liabilities** | (2,319) | – | – | (495) | – | (2,814) |
| **Net assets excluding pension deficit** | 310,225 | (7,465) | (390) | 1,155 | (13) | 303,512 |
| **Pension deficit** | (5,459) | – | – | – | – | (5,459) |
| **Net assets including pension deficit** | 304,766 | (7,465) | (390) | 1,155 | (13) | 298,053 |
| **Capital & reserves** | | | | | | |
| Called up preference share capital | 390 | – | (390) | – | – | – |
| Called up ordinary share capital | 150 | – | – | – | – | 150 |
| Share premium account | 2,795 | – | – | – | – | 2,795 |
| Merger reserve | 276,132 | – | – | – | – | 276,132 |
| Other reserves | 8,028 | 10,485 | – | 1,155 | – | 19,668 |
| Profit and loss account | 17,271 | (17,950) | – | – | (13) | (692) |
| **Total shareholders' funds** | 304,766 | (7,465) | (390) | 1,155 | (13) | 298,053 |

# Notes to the Financial Statements

## 1. Restatement of prior year (cont'd)

### (c) Balance Sheet as at 31 December 2004 – effect of prior year adjustments

| | As previously reported £000 | Dividends £000 | Foreign exchange £000 | Reclassification of Preference Shares £000 | Revaluation of available for sale investments £000 | Share-based payments £000 | As restated £000 |
|---|---|---|---|---|---|---|---|
| **Fixed assets** | | | | | | | |
| Tangible fixed assets | 3,565 | – | – | – | – | – | 3,565 |
| Investments in subsidiaries | 1,061,599 | – | – | – | – | – | 1,061,599 |
| Other investments | 5,400 | – | (297) | – | 2,312 | – | 7,415 |
| **Total fixed assets** | 1,070,564 | – | (297) | – | 2,312 | – | 1,072,579 |
| **Current assets** | | | | | | | |
| Debtors (amounts falling due within one year) | 51,039 | (5,800) | – | – | – | – | 45,239 |
| Debtors (amounts falling due outwith one year) | 9,076 | – | – | – | – | (8,275) | 801 |
| Cash and short-term deposits | 1,485 | – | – | – | – | – | 1,485 |
| **Total Current Assets** | 61,600 | (5,800) | – | – | – | (8,275) | 47,525 |
| **Creditors (amounts falling due within one year)** | | | | | | | |
| Proposed ordinary dividend | (32,914) | 32,914 | – | – | – | – | – |
| Other creditors | (28,182) | – | – | – | – | – | (28,182) |
| **Net current assets** | 504 | 27,114 | – | – | – | (8,275) | 19,343 |
| **Total assets less current liabilities** | 1,071,068 | 27,114 | (297) | – | 2,312 | (8,275) | 1,091,922 |
| **Creditors (amounts falling due outwith one year)** | (50,000) | – | – | (800) | – | – | (50,800) |
| **Provisions for liabilities** | (1,639) | – | – | – | (694) | 330 | (2,003) |
| **Net assets excluding pension deficit** | 1,019,429 | 27,114 | (297) | (800) | 1,618 | (7,945) | 1,039,119 |
| **Pension deficit** | (6,498) | – | – | – | – | – | (6,498) |
| **Net assets including pension deficit** | 1,012,931 | 27,114 | (297) | (800) | 1,618 | (7,945) | 1,032,621 |
| **Capital & reserves** | | | | | | | |
| Called up preference share capital | 800 | – | – | (800) | – | – | – |
| Called up ordinary share capital | 482 | – | – | – | – | – | 482 |
| Share premium account | 28,956 | – | – | – | – | – | 28,956 |
| Merger reserve | 912,674 | – | – | – | – | – | 912,674 |
| Other reserves | 69,119 | 32,914 | – | – | 1,618 | – | 103,651 |
| Profit and loss account | 900 | (5,800) | (297) | – | – | (7,945) | (13,142) |
| **Total shareholders' funds** | 1,012,931 | 27,114 | (297) | (800) | 1,618 | (7,945) | 1,032,621 |

## 2. Auditors' remuneration

| | **2005 £000** | **2004 £000** |
|---|---|---|
| Auditors' remuneration – audit services | **40** | 30 |
| Auditors' remuneration – non-audit services: | | |
| Further assurance services | **193** | 734 |
| Tax advisory services | **278** | 83 |
| Other non-audit services | **2,801** | 104 |
| Total non-audit services | **3,272** | 921 |
| **Total auditors' remuneration** | **3,312** | 951 |

## 3. Directors' remuneration

Details of Directors' remuneration are as follows:

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Aggregate emoluments | **3,238** | 3,072 |
| Aggregate compensation paid to Directors for loss of office | **1,995** | 1,679 |
| Company contributions paid to defined contribution pension scheme | **293** | 84 |
| Aggregate value of gains made by Directors on exercise of share options | **–** | 436 |

A total of 161,870 options have been exercised by a Director since the year-end, realising a gain of £123,000.

| | 2005 Number | 2004 Number |
|---|---|---|
| Members of defined contribution pension scheme | **1** | 5 |
| Members of defined benefits pension scheme | **2** | 2 |

Full disclosure of Directors' remuneration is shown on page 54.

The Company has no employees (including Directors) under contract of employment, all F&C Group employees being employed by several subsidiary companies.

## 4. Dividends

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| **Declared and paid during the year** | | |
| Equity dividends on Ordinary Shares: | | |
| Final dividend for 2004: 7.0p (2003: 7.0p) | **32,952** | 10,487 |
| Interim dividend for 2005: 4.0p (2004: 4.0p) | **18,865** | 5,993 |
| | **51,817** | 16,480 |
| **Proposed for approval at the Annual General Meeting (not recognised as a liability as at 31 December)** | | |
| Equity dividends on Ordinary Shares: | | |
| Final dividend for 2005: 7.0p (2004: 7.0p) | **33,381** | 32,914 |

The entitlement to receive dividends (on its holding of F&C shares) held by the ESOPs has been waived by the Trustees. This has resulted in the following dividends being waived:

| | F&C Group ESOP | | Abacus Trust | |
|---|---|---|---|---|
| | Shares | £000 | Shares | £000 |
| **2004 Dividends** | | | | |
| 2003 Final | 469,700 | 33 | – | – |
| 2004 Interim | 469,700 | 19 | – | – |
| **2005 Dividends** | | | | |
| 2004 Final | 969,700 | 68 | 10,665,706 | 747 |
| 2005 Interim | 890,200 | 36 | 5,791,630 | 232 |

## 5. Intangible fixed assets

| | Management contracts £000 |
|---|---|
| **Cost:** | |
| At 1 January 2005 | – |
| Additions | 1,249 |
| **At 31 December 2005** | **1,249** |
| **Amortisation:** | |
| At 1 January 2005 | – |
| Amortisation for the year | 41 |
| **At 31 December 2005** | **41** |
| **Net book value:** | |
| **At 31 December 2005** | **1,208** |
| At 31 December 2004 | – |

## 6. Tangible fixed assets

| | Leasehold Improvements £000 | Office furniture and equipment £000 | Computer equipment £000 | Total £000 |
|---|---|---|---|---|
| **Cost:** | | | | |
| At 1 January 2005 | 2,972 | 468 | 4,171 | 7,611 |
| Additions | – | 1 | 1,731 | 1,732 |
| Disposals | – | – | (231) | (231) |
| **At 31 December 2005** | **2,972** | **469** | **5,671** | **9,112** |
| **Depreciation:** | | | | |
| At 1 January 2005 | 583 | 261 | 3,202 | 4,046 |
| Depreciation charge for the year | 291 | 66 | 751 | 1,108 |
| Disposals | – | – | (231) | (231) |
| **At 31 December 2005** | **874** | **327** | **3,722** | **4,923** |
| **Net book amounts:** | | | | |
| **At 31 December 2005** | **2,098** | **142** | **1,949** | **4,189** |
| At 31 December 2004 | 2,389 | 207 | 969 | 3,565 |

## 7. Investments in subsidiaries

| | £000 |
|---|---|
| **Cost:** | |
| At 1 January 2005 | 1,063,961 |
| Adjustment to cost of acquisition of F&CGH Group | (13,270) |
| **At 31 December 2005** | **1,050,691** |
| **Amounts written off:** | |
| **At 1 January 2005 and 31 December 2005** | **(2,362)** |
| **Net book amounts:** | |
| **At 31 December 2005** | **1,048,329** |
| At 31 December 2004 | 1,061,599 |

Details of subsidiary undertakings are set out in note 19.

## 8. Other investments

| | Other Investments – quoted £000 | Other Investments – unquoted £000 | Total £000 |
|---|---|---|---|
| At 1 January 2005 (as restated) | 2 | 7,413 | 7,415 |
| Additions in the year | – | 509 | 509 |
| Adjustment to fair value of investments | – | (228) | (228) |
| Impairment provided for during the year | – | (5,610) | (5,610) |
| **At 31 December 2005** | **2** | **2,084** | **2,086** |

The cost of quoted investments as at 31 December 2005 was £2,000 (31 December 2004 – £2,000).

The valuation of quoted investments as at 31 December 2005 was £2,000 (31 December 2004 – £2,000).

Included in the impairment charge in the year, is £5,101,000 relating to the Company's investment in Cardinal Capital Partners Limited (Cardinal), a private Limited Liability Partnership hedge fund manager based in Ireland. During 2005, the Company's Directors made a decision to channel all relevant business through the F&C Group's own in-house capability and as such, no assets were placed with Cardinal for management. As a result of this decision the Directors considered it appropriate to fully provide against the investment and therefore the investment in Cardinal has been written down to nil as at 31 December 2005, giving rise to the impairment charge recognised.

An impairment charge of £509,000 was made in respect of the Company's investment in ISIS EP LLP, a private Limited Liability Partnership based in London. This investment has been written down to reflect the doubt the Directors have as to the level of future returns on the investment.

### Securities

The fair value of quoted investments is based on quoted market prices at the balance sheet date without any deduction for transaction costs.

The fair value of unquoted investments have been valued in accordance with International Private Equity and Venture Capital Valuation Guidelines and in accordance with the Limited Partnership Agreements where possible.

# Notes to the Financial Statements

## 9. Debtors

| | Note | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|---|
| **Amounts due within one year** | | | |
| Trade debtors | | **1,285** | 275 |
| Accrued income | | **4,233** | 2,479 |
| Amounts owed by fellow subsidiary undertakings | | **34,994** | 20,518 |
| Loans to subsidiary undertakings | | **20,886** | 16,555 |
| Prepayments | | **1,057** | 598 |
| VAT recoverable | | **200** | 663 |
| Group relief receivable | | **2,810** | 3,104 |
| Other debtors | | **1,582** | 1,047 |
| | | **67,047** | 45,239 |
| **Amounts due outwith one year** | | | |
| Loan to investee company | | **2,500** | – |
| Deferred tax | 13 | **426** | 801 |
| | | **2,926** | 801 |

The Company subscribed £2,500,000 for non-voting, non-participating B class capital in ISIS EP LLP (LLP), an investee company, in order to ensure that LLP has sufficient regulatory capital. These proceeds are held in a designated bank account by LLP and all bank interest earned on that account accrues to the Company as a dividend on B capital. The loan is redeemable on the withdrawal by the Company from LLP and therefore, there is no fixed redemption date for this loan. The Company retains the right to withdraw from the LLP and to require other members of the LLP to immediately purchase all of the Company interest in the LLP. The consideration receivable will be deferred and only receivable by the Company on the third anniversary of the date of withdrawal.

## 10. Creditors

| | Note | 31 December 2005 £000 | 31 December 2004 (as restated) £000 |
|---|---|---|---|
| **Amounts due within one year:** | | | |
| Trade creditors | | **1,666** | 1,179 |
| Accruals | | **5,667** | 5,055 |
| Amounts owed to parent undertaking | | **–** | 336 |
| Amounts owed to subsidiary undertakings | | **5,834** | 1,782 |
| Other creditors | | **5,029** | 17,247 |
| Loans from subsidiary undertakings | 12 | **12,849** | 2,583 |
| | | **31,045** | 28,182 |
| **Amounts due outwith one year:** | | | |
| Preference share capital | | **800** | 800 |
| Loans from subsidiary undertakings and Friends Provident Group | 12 | **65,000** | 50,000 |
| | | **65,800** | 50,800 |

Other creditors at 31 December 2005 includes £2,942,000 (31 December 2004: £16,212,000) of estimated further consideration payable in respect of the acquisition of F&C Group (Holdings) Limited on 11 October 2004.

£13,270,000 of the accrual at 31 December 2004 has been released during 2005 following a reassessment of the net assets of F&C Group (Holdings) Limited and its subsidiaries acquired and a resulting adjustment to consideration payable.

## 11. Provisions for liabilities

| | Property – onerous contracts £000 | Deferred tax £000 | Total £000 |
|---|---|---|---|
| At 1 January 2004 (as restated) | 2,263 | 495 | 2,758 |
| Provided during the year | 454 | 199 | 653 |
| Provision utilised during the year | (1,408) | – | (1,408) |
| At 31 December 2004 (as restated) | 1,309 | 694 | 2,003 |
| Provided during the year | 1,512 | – | 1,512 |
| Provision utilised during the year | (634) | (68) | (702) |
| **At 31 December 2005** | **2,187** | **626** | **2,813** |

*Onerous contracts*

The Company holds all properties under operating leases. This includes a number of vacant and sub-let properties which were either previously occupied by the Company or are partially occupied by the Company. Provision has been made for the residual lease commitments where significant, after taking into account existing and expected sub-tenant arrangements. The remaining terms are for up to 17 years. Assumptions as to whether each leasehold property may be sub-let or assigned in the future have been made. All leases, and the majority of subleases, are for fixed guaranteed rentals. One sub-lease involves the possible receipt of contingent rent. Any contingent rent received is recognised as income during the period. The provision is subject to uncertainties over time including market rent reviews and break-options within the lease arrangements.

*Deferred tax*

The deferred tax provision relates to short-term timing differences, which have originated but not reversed at the balance sheet date. The provision is subject to uncertainties in respect of the timing of the reversal of the timing differences.

The deferred tax provision relates to the revaluation of available for sale assets and is recognised as a separate component of equity.

For further details see note 13.

## 12. Loans from subsidiary undertakings and Friends Provident Group

| | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|
| **Wholly repayable within five years:** | | |
| US $4,000,000 loan; wholly repayable on demand (i) | **2,349** | 2,083 |
| £10,000,000 subordinated loan, at 6 month Sterling LIBOR +1%, wholly repayable on 4 June 2006 (ii) | **10,000** | 10,000 |
| £25,000,000 subordinated loan, at 6 month Sterling LIBOR +1.05%, wholly repayable on 11 October 2009 (iii) | **25,000** | 25,000 |
| £15,000,000 subordinated loan, at 6 month Sterling LIBOR +1.05%, wholly repayable on 31 December 2009 (ii) | **15,000** | 15,000 |
| £25,000,000 subordinated loan at 6 month Sterling LIBOR + 1%, wholly repayable on 14 March 2007 (ii) | **25,000** | – |
| £500,000 loans from subsidiary undertakings, wholly repayable on demand (iv) | **500** | 500 |
| | **77,849** | 52,583 |

(i) The US $4,000,000 subordinated loan is due to Friends Ivory & Sime North America, Inc, an overseas subsidiary. The loan may be repaid by the Company by giving ten banking days' notice in writing to Friends Ivory & Sime North America Inc.

(ii) The £25,000,000, £15,000,000 and £10,000,000 subordinated loans are all with F&C Treasury Limited, a subsidiary undertaking.

(iii) The £25,000,000 subordinated loan is with Friends Provident Life and Pensions Limited, a subsidiary of Friends Provident plc.

(iv) The £500,000 loans relate to two loans of £250,000 from subsidiary undertakings.

# Notes to the Financial Statements

### 12. Loans from subsidiary undertakings and Friends Provident Group (cont'd)

| | Note | 31 December 2005 £000 | 31 December 2004 £000 |
|---|---|---|---|
| **Amounts repayable:** | | | |
| In one year or less, or on demand | 10 | **12,849** | 2,583 |
| In more than one year but not more than two years | 10 | **25,000** | 10,000 |
| In more than two years but not more than five years | 10 | **40,000** | 40,000 |
| In more than five years | | **–** | – |
| | | **77,849** | 52,583 |

### 13. Deferred taxation

| | 2005 £000 | 2004 (as restated) £000 |
|---|---|---|
| 1 January | **106** | 405 |
| Adjustments in respect of previous periods | **(351)** | (103) |
| Provided during the year | **45** | (195) |
| **At 31 December** | **(200)** | 107 |

| | Note | 31 December 2005 £000 | 31 December (as restated) 2004 £000 |
|---|---|---|---|
| Deferred taxation provided in the accounts is as follows: | | | |
| Short-term timing differences | | **313** | 634 |
| Revaluation of available for sale assets | | **(626)** | (694) |
| Depreciation in advance of capital allowances | | **113** | 167 |
| | | **(200)** | 107 |
| Disclosed in the accounts as follows: | | | |
| Debtors | 9 | **426** | 801 |
| Provision for liabilities | 11 | **(626)** | (694) |
| **Net deferred tax (liability)/asset** | | **(200)** | 107 |

## 14. Pension commitments

**The ISIS Asset Management plc Pension Fund**

The Company continues to operate a defined benefit scheme ("The ISIS Asset Management plc Pension Fund") in the UK which provides benefits based on final pensionable salary. This scheme was closed to new entrants from 31 December 1995. The assets of the scheme are held separately from those of the Company but are managed by the Company. The contributions are determined by an independent qualified actuary on the basis of triennial valuations using the attained age method since the scheme is now closed to new members. The most recent triennial valuation was at 31 March 2005.

The results of the full actuarial valuation carried out at 31 March 2005 were updated to 31 December 2005 by a qualified independent actuary for the purposes of FRS17: Retirement Benefits.

| | |
|---|---|
| Date of last actuarial valuation | 31 March 2005 |
| Scheme actuary | Mercer Human Resource Consulting Limited |
| Method of valuation | Projected Unit |
| Market value of assets at last valuation date | £33,550,000 |
| Level of funding | 80% |

A contribution schedule was agreed by the Company and trustees in May 2003. The Company has paid contributions of £100,000 per month during 2005. The Company has agreed to pay monthly contributions of at least one-twelfth of the annual amount of 25% of basic salaries until April 2008. These contributions are subject to review at future actuarial valuations, the next one of which is due no later than 31 March 2008. The results of the 31 March 2005 valuation are currently being considered by the Fund's trustees and the Company. The minimum estimated amount of contributions expected to be paid into the scheme during the current financial year is £1,200,000.

As the ISIS Asset Management plc Pension Fund is a closed scheme, under the projected unit method the current service cost will tend to increase as a percentage of pensionable salaries as the average age of members increases.

While the Company itself has no employees, there are a significant number of deferred pensioners who are members of the scheme, therefore, the Company is considered to be the sponsor of the scheme.

The major assumptions used on all the schemes by the actuaries for the purposes of FRS 17 were:

| | **31 December 2005** | **31 December 2004** | **31 December 2003** |
|---|---|---|---|
| Rate of increase in salaries | **4.00%** | 4.00% | 4.00% |
| Rate of increase of pensions in payment (range) | **2.75% – 3.50%** | 2.75% – 3.50% | 3.50% |
| Discount rate | **4.70%** | 5.30% | 5.40% |
| Inflation assumption | **2.75%** | 2.75% | 2.50% |

**14. Pension commitments (cont'd)**

The assets in the scheme and the expected rates of return used on the scheme were:

**(i) Expected long-term rates of return**

| | 31 December 2005 | 31 December 2004 | 31 December 2003 |
|---|---|---|---|
| Equities | **7.00%** | 7.00% | 7.00% |
| Gilts | **5.00%** | 5.00% | 5.00% |
| Corporate bonds | **4.70%** | 5.30% | 5.40% |
| Cash | **4.00%** | 4.00% | 4.00% |

**(ii) Value of assets in the scheme**

| | 31 December 2005 £000 | 31 December 2004 £000 | 31 December 2003 £000 |
|---|---|---|---|
| Equities | **30,758** | 25,776 | 23,201 |
| Gilts | **6,026** | 4,477 | 3,172 |
| Corporate bonds | **2,304** | 2,337 | 3,053 |
| Cash | **724** | 370 | 229 |
| Total market value of scheme assets | **39,812** | 32,960 | 29,655 |
| Actuarial value of scheme liabilities | **(62,176)** | (42,243) | (37,453) |
| Deficit in the scheme | **(22,364)** | (9,283) | (7,798) |
| Deferred tax asset on deficit | **6,709** | 2,785 | 2,339 |
| **Net pension deficit** | **(15,655)** | (6,498) | (5,459) |

**(iii) Analysis of amount recognised in reserves**

| | | 2005 £000 | % | 2004 £000 | % |
|---|---|---|---|---|---|
| Actual return less expected return on assets | (a) | **3,610** | **9** | 260 | 1 |
| Experience gains and losses on liabilities | (b) | **(1,805)** | **(3)** | 231 | (1) |
| Changes in assumptions | | **(14,760)** | | (2,166) | |
| **Actuarial loss recognised in reserves** | (b) | **(12,955)** | **(21)** | (1,675) | (4) |

Included within the changes in assumptions above is £6,662,000 (2004: £nil) relating to the strengthening of the mortality assumptions.

The percentages shown for each year are calculated as follows:

(a) Percentage of the scheme assets at the balance sheet date.

(b) Percentage of the present value of the scheme liabilities at the balance sheet date.

## 14. Pension commitments (cont'd)

### (iv) Movement in deficit during the year

| | 2005 £000 | 2004 £000 |
|---|---|---|
| Deficit in scheme at 1 January | **(9,283)** | (7,798) |
| Movements in year: | | |
| Current service costs | **(766)** | (958) |
| Past service costs | **(514)** | – |
| Contributions | **1,200** | 1,200 |
| Expected return on pension scheme assets | **2,209** | 1,992 |
| Interest on pension liabilities | **(2,255)** | (2,044) |
| Actuarial loss recognised in reserves | **(12,955)** | (1,675) |
| **Deficit in scheme at 31 December** | **(22,364)** | (9,283) |

### (v) History of experience gains and losses

| | 2005 | 2004 | 2003 | 2002 | 2001 |
|---|---|---|---|---|---|
| **Difference between the expected and actual return on scheme assets:** | | | | | |
| amount (£000) | **3,610** | 260 | 2,168 | (9,116) | (5,879) |
| percentage of scheme assets | **9%** | 1% | 7% | (37%) | (18%) |
| **Experience gains and losses on scheme liabilities:** | | | | | |
| amount (£000) | **(1,805)** | 231 | 22 | 1,265 | (600) |
| percentage of the present value of the scheme liabilities | **(3%)** | 1% | –% | 4% | (2%) |
| **Total amount recognised in reserves:** | | | | | |
| amount (£000) | **(12,955)** | (1,675) | 753 | (8,012) | (4,904) |
| percentage of the present value of the scheme liabilities | **(21%)** | (4%) | 2% | (24%) | (16%) |

## 15. Ordinary share capital

| | 31 December 2005 | | 31 December 2004 | |
|---|---|---|---|---|
| | Number of shares | £000 | Number of shares | £000 |
| **Authorised:** | | | | |
| **Equity interests** | | | | |
| Ordinary Shares of 0.1p | **800,000,000** | **800** | 800,000,000 | 800 |
| Deferred Shares of 0.1p | **100,000,000** | **100** | 100,000,000 | 100 |
| **Allotted, issued and fully paid:** | | | | |
| **Equity interests** | | | | |
| Ordinary Shares of 0.1p | **483,434,237** | **484** | 482,200,131 | 482 |

### (a) Ordinary share capital of 0.1p

| | No. of Ordinary Shares 2005 | 2004 |
|---|---|---|
| Issued at 1 January | **482,200,131** | 150,256,675 |
| Share options exercised during the year | **1,234,106** | 546,732 |
| Shares issued in respect of the acquisition of F&CGH Group: | | |
| – shares issued by way of consideration | **–** | 320,374,763 |
| – shares issued to Abacus Trust | **–** | 11,021,961 |
| **Issued at 31 December** | **483,434,237** | 482,200,131 |

The holders of Ordinary Shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

### 15. Ordinary share capital (cont'd)

During the year the following share options were exercised, in line with the rules of the appropriate scheme, and ordinary shares allotted:

| Exercise date | Executive Share Option Scheme | No. of Ordinary Shares | Exercise price (p) |
|---|---|---|---|
| 5 January 2005 | 1995 | 5,000 | 203.83 |
| 5 January 2005 | 2002 | 40,000 | 139.00 |
| 6 January 2005 | 2002 | 109,711 | 139.00 |
| 6 January 2005 | 1995 | 34,112 | 214.00 |
| 12 January 2005 | 2002 | 86,474 | 139.00 |
| 19 January 2005 | 2002 | 20,000 | 139.00 |
| 28 January 2005 | 2002 | 48,000 | 139.00 |
| 28 January 2005 | 1995 | 4,845 | 203.83 |
| 9 February 2005 | 2002 | 135,518 | 139.00 |
| 18 February 2005 | 2002 | 5,582 | 139.00 |
| 18 February 2005 | 1995 | 3,706 | 232.50 |
| 18 February 2005 | 1995 | 3,706 | 214.00 |
| 29 March 2005 | 2002 | 40,796 | 139.00 |
| 6 April 2005 | 2002 | 30,215 | 139.00 |
| 14 April 2005 | 2002 | 70,000 | 139.00 |
| 19 April 2005 | 2002 | 30,000 | 139.00 |
| 11 May 2005 | 2002 | 8,206 | 139.00 |
| 11 May 2005 | 1995 | 30,000 | 214.00 |
| 5 July 2005 | 2002 | 17,986 | 139.00 |
| 4 August 2005 | 2002 | 44,691 | 139.00 |
| 16 August 2005 | 2002 | 39,208 | 139.00 |
| 24 August 2005 | 2002 | 20,000 | 139.00 |
| 9 September 2005 | 2002 | 36,870 | 139.00 |
| 12 October 2005 | 2002 | 316,545 | 139.00 |
| 25 October 2005 | 2002 | 9,353 | 139.00 |
| 2 December 2005 | 2002 | 43,582 | 139.00 |
| | | **1,234,106** | |

The consideration received in respect of the Ordinary Share capital issued during the year ended 31 December 2005 was £1,776,000 (year ended 31 December 2004: £822,000).

The F&C Asset Management plc Group operates several share-based payment schemes which have a contingent right to the allotment of shares in the Company.

## 15. Ordinary share capital (cont'd)

At 31 December 2005 the contingent right to the allotment of shares was as follows:

| Scheme | No. of awards outstanding | Exercise price (p) | Exercisable/vested |
|---|---|---|---|
| 2002 Executive Share Option Scheme | 2,729,971 | 139.00 | 19 March 2006-19 March 2013 |
| 2002 Executive Share Option Scheme | 1,270,331 | 240.83 | 9 March 2007-9 March 2014 |
| 2002 Share Save Scheme | 581,111 | 114.00 | 9 May 2006-9 November 2008 |
| 2002 Share Save Scheme | 343,564 | 181.00 | 19 April 2007-19 October 2009 |
| 2002 Share Save Scheme | 473,750 | 186.60 | 29 April 2008-29 October 2010 |
| Re-Investment Plan | 4,625,626 | 0.00 | From 11 October 2006 |
| Re-Investment Plan | 9,533,741 | 0.00 | From 11 October 2006-11 October 2007 |
| Long-Term Remuneration Plan | 5,952,988 | 0.00 | From 15 November 2007 |
| Purchased Equity Plan | 684,425 | 0.00 | From 24 March 2008 |
| 1995 Executive Share Option Scheme | 730,028 | 203.83 | 24 March 2006-9 June 2008 |
| 1995 Executive Share Option Scheme | 781,834 | 232.50 | 24 March 2006-16 July 2009 |
| 1995 Executive Share Option Scheme | 642,029 | 214.00 | 24 March 2006-28 April 2010 |
| 1995 Executive Share Option Scheme | 18,740 | 320.17 | 24 March 2006-20 October 2010 |
| 1995 Executive Share Option Scheme | 520,500 | 455.83 | 24 March 2006-1 March 2011 |

The following shares are held in Employee Share Option Plan (ESOP) trusts. These are categorised as own shares, and deducted from shareholders' funds:

| | 31 December 2005 Number | 31 December 2004 Number |
|---|---|---|
| F&C Group ESOP Trustee Limited | **890,200** | 969,700 |
| Abacus Trust | **5,673,904** | 11,021,961 |
| | **6,564,104** | 11,991,661 |

The aggregate nominal value of own shares held by ESOPs at 31 December 2005 was £7,000 (31 December 2004: £12,000). The market value of these shares at 31 December 2005 was £11,635,000 (31 December 2004: £29,499,000).

During the year, the Company purchased 104,780 of its own Ordinary Shares (2004: 500,000) of 0.1p to satisfy the exercises of awards granted under the share save scheme in respect of 'good leavers'. The cost of this to the Company, after exercise price monies paid by the former employees was £87,000 (2004: £1,156,000). The consideration paid for the shares was £223,000 (2004: £1,156,000).

### (b) Cumulative Preference Shares of £1 each

| | 31 December 2005 Number of shares | 31 December 2005 £000 | 31 December 2004 Number of shares | 31 December 2004 £000 |
|---|---|---|---|---|
| **Authorised, allotted, issued and fully paid** | | | | |
| At 1 January | **800,000** | **800** | 390,000 | 390 |
| Preference Shares issued during the year | – | – | 410,000 | 410 |
| **At 31 December** | **800,000** | **800** | 800,000 | 800 |

The issued Cumulative Preference Shares are classified as financial liabilities. The key terms and conditions relating to these Preference Shares are as follows:

– Dividends on the Cumulative Preference Shares are paid in priority to any payment of dividend on any other class of shares.

– On a return of assets on liquidation, the assets of the Company available for distribution shall be applied first in repaying the holders of the Cumulative Preference Shares the amounts paid up or credited as paid up on such shares, together with any arrears of the fixed dividend.

– Holders of Cumulative Preference Shares are entitled to one vote in instances where the fixed dividend is six months in arrears or in the event that a resolution put to the meeting varies or impacts the rights and privileges attached to these shares.

The terms of the Cumulative Preference Shares confer the right to receive a variable rate dividend on the amount paid up or credited as paid up on the Cumulative Preference Shares at the rate of 2% per annum above the London Inter-Bank Offer Rate (LIBOR) expressed as a rate per annum at the commencement of each half-yearly dividend payment period.

# Notes to the **Financial Statements**

## 16. Reserves

**Reconciliation of movement in reserves**

| | Ordinary share capital £000 | Preference share capital £000 | Deferred share capital £000 | Share premium account £000 | Merger reserve £000 | Fair value reserve[1] £000 | Special distri-butable reserve[1] £000 | Profit and loss account £000 | Total share-holders' funds £000 |
|---|---|---|---|---|---|---|---|---|---|
| Balance at 1 January 2004 previously reported | 150 | 390 | – | 2,795 | 276,132 | – | 8,028 | 17,271 | 304,766 |
| Prior year adjustment | – | (390) | – | – | – | 1,155 | 10,485 | (17,963) | (6,713) |
| Balance at 1 January 2004 (as restated) | 150 | – | – | 2,795 | 276,132 | 1,155 | 18,513 | (692) | 298,053 |
| Share capital allotted on exercise of options | 1 | – | – | 821 | – | – | – | – | 822 |
| Share capital issued to Abacus Trust | 11 | – | – | 25,340 | – | – | – | (25,351) | – |
| Share capital issued as consideration | 320 | – | – | – | 736,542 | – | – | – | 736,862 |
| Purchase of own shares | – | – | – | – | – | – | – | (1,164) | (1,164) |
| Capitalisation of merger reserve | – | – | 100 | 99,900 | (100,000) | – | – | – | – |
| Cancellation of Deferred Shares | – | – | (100) | – | – | – | 100 | – | – |
| Conversion of share premium account | – | – | – | (99,900) | – | – | 99,900 | – | – |
| Actuarial loss, net of deferred tax | – | – | – | – | – | – | – | (1,173) | (1,173) |
| Retained loss for the year | – | – | – | – | – | 463 | – | (1,242) | (779) |
| Transfer from special distributable reserve in relation to dividends | – | – | – | – | – | – | (16,480) | 16,480 | – |
| Balance at 31 December 2004 (as restated) | 482 | – | – | 28,956 | 912,674 | 1,618 | 102,033 | (13,142) | 1,032,621 |
| Share capital allotted on exercise of options | 2 | – | – | 1,774 | – | – | – | – | 1,776 |
| Purchase of own shares | – | – | – | – | – | – | – | (87) | (87) |
| Actuarial loss, net of deferred tax | – | – | – | – | – | – | – | (9,069) | (9,069) |
| Retained loss for the year | – | – | – | – | – | (159) | – | (14,510) | (14,669) |
| Transfer from special distributable reserve in relation to dividends | – | – | – | – | – | – | (51,817) | 51,817 | – |
| **Balance at 31 December 2005** | **484** | **–** | **–** | **30,730** | **912,674** | **1,459** | **50,216** | **15,009** | **1,010,572** |

(1) Fair value reserve and Special distributable reserve constitute 'Other reserves' as disclosed in the Balance Sheet and amount to £51,675,000 (2004: £103,651,000).

The profit of the Company for the year, before dividends, was £37,307,000 (2004: £15,238,000).

## 17. Financial commitments

The Company had the following annual commitments in respect of non-cancellable operating leases and other contracts:

| | Premises | | Other | |
|---|---|---|---|---|
| | **31 December 2005 £000** | 31 December 2004 £000 | **31 December 2005 £000** | 31 December 2004 £000 |
| Commitments expiring within one year | **–** | – | **–** | – |
| Commitments expiring within two to five years | **–** | – | **37** | 27 |
| Commitments expiring outwith five years | **2,644** | 1,296 | **–** | – |
| | **2,644** | 1,296 | **37** | 27 |

The premises financial commitments disclosed above do not include any sub-leasing arrangements which the Company may have in place. The amounts shown reflect gross commitments at the balance sheet dates.

## 18. Capital commitments

The amounts contracted for in terms of capital expenditure, but not provided for in the financial statements at 31 December 2005, amount to £90,000 (31 December 2004 – £nil).

## 19. Subsidiary Undertakings

The principal entities that the Company controls are listed below:

| | Percentage interest and voting rights | Country of registration or incorporation | Nature of business |
|---|---|---|---|
| **(i) United Kingdom** | | | |
| FP Asset Management Holdings Limited[(1)] | 100 | England | Holding company |
| F&C Property Asset Management plc (formerly F&C Property Services Limited)[(1)] | 100 | England | Property investment management |
| Friends Provident Unit Trust Managers Limited[(1)] | 100 | England | OEIC investment management |
| F&C Asset Management Services Limited[(1)] | 100 | England | Employee service company |
| ISIS Equity Partners Holdings Limited[(1)] | 100 | England | Holding company |
| ISIS Investment Manager plc[(1)] | 100 | England | Investment management |
| F&C Managed Pension Funds Limited[(1)] | 100 | England | Insurance management |
| F&C Treasury Limited[(1)] | 100 | England | Treasury management company |
| F&C Group (Holdings) Limited[(1)] | 100 | England | Holding company |
| F&C Group ESOP Trustee Limited[(1)] | 100 | Scotland | ESOP Trustee |
| ISIS Investment Trusts Business Limited[(1)] | 100 | Scotland | Investment Trust management |
| FP Fund Managers Limited[(2)] | 100 | England | Investment management |
| F&C Asset Managers Limited[(2)] | 100 | England | Investment management |
| F&C Property Limited (formerly F&C Property Asset Management plc)[(2)] | 100 | England | Property investment management |
| ISIS Equity Partners plc[(3)] | 100 | England | Private Equity investment management |
| F&C Property Investments Limited[(4)] | 100 | England | Property investment management |
| F&C Fund Management Limited[(4)] | 100 | England | OEIC investment management |
| ISIS Investment Management Limited[(4)] | 100 | England | Investment management |
| WAM Holdings Limited[(5)] | 100 | England | Holding company |
| Cerebys Limited[(6)] | 100 | England | Derivative investment management |
| F&C Unit Management Limited[(6)] | 100 | England | OEIC investment management |
| FCEM Holdings (UK) Limited[(6)] | 100 | England | Holding company |
| F&C (CI) Limited[(7)] | 100 | England | Private Equity investment |
| F&C Investment Services Limited[(7)] | 100 | England | Investment management |
| F&C Management Limited[(7)] | 100 | England | Investment management |
| F&C Property Investment Management Limited[(7)] | 100 | England | Property investment management |
| F&C Alternative Investments (Holdings) Limited[(8)] | 100 | England | Investment holding company |
| F&C Group Management Limited[(8)] | 100 | England | Holding company |
| F&C Emerging Markets Limited[(9)] | 100 | England | Investment management |
| F&C Holdings Limited[(10)] | 100 | England | Holding company |
| F&C Partners LLP[(11)] | 60 | England | Hedge investment management |
| F&C Private Equity Nominees Limited[(12)] | 100 | England | Private Equity investment company |

# Notes to the **Financial Statements**

**19. Subsidiary undertakings (cont'd)**

| | Percentage interest and voting rights | Country of registration or incorporation | Nature of business |
|---|---|---|---|
| **(ii) Overseas** | | | |
| Ivory & Sime (Japan) KK[1] | 100 | Japan | Investment management |
| Ivory & Sime (Bermuda) Limited[1] | 100 | Bermuda | Investment management |
| F&C Channel Islands Limited[6] | 100 | Jersey | Employee services company |
| F&C Management (Jersey) Limited[6] | 100 | Jersey | Investment management |
| F&C Netherlands B.V.[8] | 100 | The Netherlands | Investment management |
| F& C Ireland Limited[8] | 100 | Republic of Ireland | Investment management |
| F&C Luxembourg (formerly AF-Investimentos Internacional, S.A.)[8] | 100 | Luxembourg | Investment management |
| F&C Portugal Gestao de Patrimonios S.A.[8] | 100 | Portugal | Investment management |

(1) Owned by F&C Asset Management plc

(2) Owned by FP Asset Management Holdings Limited

(3) Owned by ISIS Equity Partners Holdings Limited

(4) Owned by WAM Holdings Limited

(5) Owned by F&C Treasury Limited

(6) Owned by F&C Management Limited

(7) Owned by F&C Holdings Limited

(8) Owned by F&C Group (Holdings) Limited

(9) Owned by FCEM Holdings (UK) Limited

(10) Owned by F&C Group Management Limited

(11) Owned by F&C Alternative Investments (Holdings) Limited

(12) Owned by F&C (CI) Limited

**20. Contingent liabilities**

**(a) Shareholding in F&C Group Management Limited (formerly Primrose Street Holdings Limited)**

In December 2000, when Eureko agreed to acquire 90% of the issued share capital of F&C Group (Holdings) Limited from Hypo Vereins-Bank, approximately 73% of the ordinary issued shares of F&C Group Management Limited, a subsidiary company, were held in the form of two bearer share warrants which could not be located prior to the completion of the sale (the ''old Share Warrants'').

Since a bearer share warrant issued by a company entitles the bearer to the shares specified in the share warrant, there is a risk that a third party holding the old Share Warrants may claim that it is entitled to the specified shares in F&C Group Management Limited. If a third party were successful in establishing a claim in relation to the old Share Warrants, F&C Group (Holdings) Limited could be liable to indemnify F&C Group Management Limited under the original indemnity arrangements, which could, as set out below, have a material adverse effect on the F&C Asset Management Group's business, results of operations and/or financial condition.

Although there is a possibility that a third party may seek to establish that it is entitled to the shares specified in the old Share Warrants, the Directors have been informed that Eureko has been advised that the prospect of a third party succeeding in such a claim is remote.

Under the terms of the Sale and Purchase Agreement (in respect of the Merger), Eureko Holdings has given a specific indemnity (guaranteed by Eureko) to F&C Asset Management plc in respect of losses arising in relation to the old share warrants in F&C Group Management Limited (including in respect of the indemnity granted by F&C Group (Holdings) Limited to F&C Group Management Limited) which is capped at approximately £432 million.

## 20. Contingent liabilities (cont'd)

### (b) European court case – VAT on investment trust management fees

In a current European court case, a UK investment trust is seeking to establish that management services to UK investment trusts should be a VAT exempt supply, rather than a taxable supply in accordance with current UK VAT law. If this case were successful, the Company, in common with other relevant fund managers in the UK, would face claims from those investment trusts to which they have supplied services for repayment of the VAT they have charged to them. The AITC (a party to the above litigation) has indicated that it believes claims dating back as far as 1990 may be lodged with fund managers by investment trusts. The Company can submit repayment claims to HM Revenue and Customs, but only dating back as far as 2001, being the maximum time period permitted. The Company has begun to receive protective claims from a number of its investment trust clients and has lodged protective claims with HM Revenue and Customs. At present, the Directors are not able to judge the likelihood that the VAT court case will be successful, nor are they able to quantify the claims that may be received or the extent to which such claims could be mitigated and therefore, are not able to quantify the potential liability.

## 21. Capital Adequacy Directive

The Company, part of the F&C Asset Management plc group, is not subject to the regulatory consolidated capital requirements of the Financial Services Authority.

## 22. Parent undertaking and controlling party

The smallest group of which the Company is a member and for which Group financial statements are prepared is F&C Asset Management plc.

In the opinion of the Directors, the Company's ultimate parent undertaking and controlling party is Friends Provident plc. Friends Provident plc is incorporated in England and Wales. Copies of the Group Report and Accounts can be obtained from the Company Secretary, Pixham End, Dorking, Surrey RH4 1QA.

# Notice of **Annual General Meeting**

Notice is hereby given that the twenty-sixth Annual General Meeting of F&C Asset Management plc will be held at the Signet Library, Parliament Square, Edinburgh EH1 1RF on Tuesday 16 May 2006 at 12 noon for the following purposes:

**Ordinary Business**

To be proposed as ordinary resolutions:

1. To receive the Financial Statements and the Reports of the Directors and the Independent Auditors for the year ended 31 December 2005.
2. To declare a final dividend of 7.0 pence per share on the ordinary shares of the Company.
3. Re-elect Robert Jenkins, who retires by rotation, as a Director.
4. Re-elect Dick de Beus, who retires by rotation, as a Director.
5. Re-elect Keith Bedell-Pearce, who retires by rotation, as a Director.
6. Re-elect Keith Satchell, who retires by rotation, as a Director.
7. To approve the Directors' Remuneration Report for the year ended 31 December 2005.
8. Re-appoint Ernst & Young LLP as auditors to the Company to hold office until the conclusion of the next General Meeting at which Financial Statements are laid before the Company and to authorise the Directors to determine their remuneration.

**Special Business**

To be proposed as an ordinary resolution:

9. Re-approve and renew the authorisation of the terms of the Relationship Agreement between the Company and Friends Provident plc dated 4 October 2004, such approval and renewal to expire on the conclusion of the Annual General Meeting of the Company to be held in 2007 subject to future renewal.

To be proposed as an ordinary resolution:

10. To augment the contractual separation terms payable to Mr Paterson Brown, the Company's Chief Financial Officer, who will retire from the Board on conclusion of the Annual General Meeting. Details of the proposed augmentation are set out on page 26 of the Report of the Directors accompanying this notice of Annual General Meeting.

To be proposed as an ordinary resolution:

11. That, in light of the exceptional circumstances surrounding the decision by Resolution Life to terminate the contracts relating to the management of its funds by the Company, the Remuneration Committee of the Company be and is authorised to exercise the discretions conferred on it by the rules of:
    (a) The F&C Asset Management plc Long Term Remuneration Plan;
    (b) The ISIS Asset Management plc Reinvestment Plan;
    (c) The ISIS Asset Management plc 1995 Share Option Scheme; and
    (d) The ISIS Asset Management plc 2002 Executive Share Option Scheme (together, the ''Relevant Plans''),

    so as to make a one-off adjustment to the Company's reported underlying earnings per ordinary share for the financial year ended 31 December 2006 for the purposes of determining the extent to which the performance conditions attaching to awards and / or options granted under the Relevant Plans have been satisfied, such adjustment, which will not exceed 3.0 pence per ordinary share, to be carried out in the manner described on pages 27 and 28 of the Report of the Directors accompanying this notice of Annual General Meeting.

To be proposed as an ordinary resolution:

12. That, the amendments to the F&C Asset Management plc Long Term Remuneration Plan which seek to allow the granting of awards to employees below Executive Director level that are not subject to ongoing performance conditions (the main features of which are summarised on pages 28 and 29 of the Report of the Directors accompanying this notice of Annual General Meeting) be and are approved. To authorise the Directors of the Company (or a duly authorised Committee) to take such steps as are necessary or expedient to carry the same into effect for awards made after the date of the meeting.

To be proposed as an ordinary resolution:

13. THAT, in substitution for any existing authority under section 80 of the Companies Act 1985 (the ''Act''), but without prejudice to the exercise of any such authority prior to the date hereof, the Directors of the Company be and they are hereby generally and unconditionally authorised, pursuant to section 80 of the Act, to allot relevant securities (as defined in section 80(2) of the Act) up to an aggregate nominal amount of £159,249.76, such authority to expire on the conclusion of the Annual General Meeting of the Company to be held in 2007, unless previously revoked, varied or extended by the Company in general meeting, save that the Company may, at any time prior to the expiry of such authority, make an offer or enter into an agreement which would or might require relevant securities to be allotted after the expiry of such authority and the Directors of the Company may allot relevant securities in pursuance of such an offer or agreement as if such authority had not expired.

To be proposed as a special resolution:

14. THAT, in substitution for any existing power under section 95 of the Companies Act 1985 (the ''Act''), but without prejudice to the exercise of any such existing power prior to the date hereof, the Directors of the Company be and are hereby empowered, pursuant to section 95(1) of the Act, (a) to allot equity securities (as defined in section 94(2) of the Act) for cash pursuant to the authority under section 80 of the Act conferred on the Directors of the Company and contained in resolution 13 as set out in the notice convening the Annual General Meeting of the Company at which this resolution is proposed and (b) sell relevant shares (as defined in section 94(5) of the Act) in the Company if immediately before the sale, such shares are held by the Company as treasury shares (as defined in section 162A(3) of the Act) (''treasury shares'') for cash (as defined in section 162D(2) of the Act), in each case as if section 89(1) of the Act did not apply to any such allotment or sale, up to an aggregate nominal amount of £159,246.76, such power to expire on the conclusion of the Annual General Meeting of the Company to be held in 2007, unless previously revoked, varied or extended by the Company in general meeting, provided that such power shall be limited to the allotment of equity securities and the sale of treasury shares:

    (i) in accordance with the terms of the Relationship Agreement between the Company and Friends Provident plc dated 4 October 2004, provided that resolution 9 relating to the re-approval and renewal of such Relationship Agreement as set out in the notice convening the Annual General Meeting of the Company at which this resolution is proposed is passed;

    (ii) in order to satisfy options or awards under any share scheme for employees or share incentive plan approved by the Company in general meeting;

    (iii) in connection with an offer of equity securities open for acceptance for a period fixed by the Directors of the Company to the holders of ordinary shares in the share capital of the Company on a fixed record date in proportion (as nearly as practicable) to their respective holdings of such ordinary shares (but subject to such exclusions or other arrangements as the Directors of the Company may consider necessary or expedient to deal with legal problems under or resulting from the application or apparent application of the laws of any territory or the requirements of any regulatory body or any stock exchange in any territory or in connection with fractional entitlements or otherwise howsoever); and

    (iv) other than pursuant to sub-paragraphs (i), (ii) and (iii) of this resolution, up to an aggregate nominal amount of £24,218.05;

    save that the Company may, at any time prior to the expiry of such power, make an offer or enter into an agreement which would or might require equity securities to be allotted or treasury shares to be sold after the expiry of such power and the Directors of the Company may allot equity securities or sell treasury shares in pursuance of such an offer or agreement as if such power had not expired.

# Notice of **Annual General Meeting**

To be proposed as a special resolution:

15. THAT, in substitution for any existing power under section 166 of the Companies Act 1985 (the "Act"), but without prejudice to the exercise of any such power prior to the date hereof, the Company be and is hereby generally and unconditionally authorised, pursuant to and in accordance with section 166 of the Act, to make market purchases (within the meaning of section 163(3) of the Act) of fully paid ordinary shares of 0.1 pence each in the capital of the Company ("ordinary shares"), provided that:

    (i) the maximum aggregate number of ordinary shares hereby authorised to be purchased is 10 per cent. of the issued ordinary share capital of the Company (excluding treasury shares as defined in section 162A(3) of the Act) as at the date of the passing of this resolution;

    (ii) the minimum price which may be paid for an ordinary share is 0.1 pence (exclusive of expenses); and

    (iii) the maximum price (exclusive of expenses) which may be paid for an ordinary share is an amount equal to 105 per cent. of the average of the middle market quotations (as derived from the Daily Official List of the London Stock Exchange) for the ordinary shares for the five business days immediately preceding the date of purchase;

    such authority to expire on the earlier of the first anniversary of the passing of this resolution and the conclusion of the Annual General Meeting of the Company to be held in 2007, unless previously revoked, varied or renewed by the Company in general meeting, save that the Company may at any time prior to the expiry of such authority enter into a contract or contracts to purchase ordinary shares under such authority which will or might be completed or executed wholly or partly after the expiration of such authority and may make a purchase of ordinary shares in pursuance of any such contract or contracts.

By order of the Board

W Marrack Tonkin, FCCA
*Secretary*

80 George Street
Edinburgh EH2 3BU
10 April 2006

Notes

(i) A member who is entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, vote on his/her behalf. A proxy need not be a member of the Company.

(ii) A Form of Proxy for use by Ordinary Shareholders in connection with the meeting is enclosed with these Accounts. To be valid, the Form of Proxy should be completed and sent, together with any power of attorney or other authority (if any) under which it is signed or an extract from the Books of Council and Session or a notarially certified copy or a copy certified in accordance with the Powers of Attorney Act 1971 of such power or authority, so as to reach the Company's registrars, at the address stated thereon, not later than 12 noon on 14 May 2006.

(iii) The Company has made provision for shareholders who would like to lodge their proxy electronically, details of how to lodge a proxy electronically are set out on page 25.

(iv) Completing and returning a Form of Proxy will not prevent an Ordinary Shareholder from attending in person at the meeting referred to above and voting should he or she wish to do so.

(v) The Register of the Directors' and their families' interests in the Company's shares and a copy of the contract of service of each of the Directors of the Company will be available for inspection at the registered office of the Company during normal business hours on any week day (Bank Holidays excepted) from the date of this Notice until the date of the meeting, and at the place of the meeting from 15 minutes prior to and during the continuance of the meeting.

(vi) Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, the Company specifies that only those Ordinary Shareholders entered on the Register of Members of the Company as at 12 noon on 14 May 2006 or, in the event that the meeting is adjourned, on the Register of Members 48 hours before the time of any adjourned meeting, shall be entitled to attend or vote at the meeting in respect of the number of Ordinary Shares registered in their name at that time. Changes to the entries on the Register of Members after 12 noon on 14 May 2006 or, in the event that the meeting is adjourned, in the Register of Members 48 hours before the time of any adjourned meeting, shall be disregarded in determining the rights of any person to attend or vote at the meeting, notwithstanding any provisions in any enactment, the Articles of Association of the Company or other instrument to the contrary.

# Corporate Information

## Directors

Robert Jenkins, Chairman‡
Christopher Jemmett, Deputy Chairman and Senior Independent Non-Executive†
Alain Grisay, Chief Executive
Dick de Beus, Non-Executive‡
Keith Bedell-Pearce, Non-Executive*†
Howard Carter, Executive
David Gray, Non-Executive†‡
John Heywood, Non-Executive*†
Brian Larcombe, Non-Executive*
Karen McPherson, Non-Executive*‡
Jeff Medlock, Non-Executive
Philip Moore, Non-Executive
Ian Paterson Brown, Executive
Keith Satchell, Non-Executive‡

* Member of Remuneration Committee
† Member of Audit & Compliance Committee
‡ Member of Nomination Committee

## Head Office

Exchange House
Primrose Street
London
EC2A 2NY
Telephone 020 7628 8000
Facsimile 020 7628 8188
Email: enquiries@fandc.com

## Secretary and Registered Office

W Marrack Tonkin, FCCA
80 George Street
Edinburgh
EH2 3BU
Telephone 0131 465 1000
Facsimile 0131 225 2375

## Solicitors

Shepherd+ Wedderburn
Saltire Court
20 Castle Terrace
Edinburgh
EH1 2ET

## Principal Bankers

The Royal Bank of Scotland plc
142-144 Princes Street
Edinburgh
EH2 4EQ

## Stockbrokers

Cazenove & Co
20 Moorgate
London
EC2R 6DA

Merrill Lynch International
Merrill Lynch Financial Centre
2 King Edward Street
London
EC1A 1HQ

## Auditors

Ernst & Young LLP
Ten George Street
Edinburgh
EH2 2DZ

## Registrar and Transfer Offices

Lloyds TSB Registrars
PO Box 28448
Finance House
Orchard Brae
Edinburgh
EH4 1WQ

## Corporate information

F&C Asset Management plc is regulated by the Financial Services Authority

## Website

Shareholders are encouraged to visit our website www.fandc.com