

Chairman's introduction



Mike Biggs, Chairman

“Direct Line Group believes that the combination of a good governance structure, a strong values-based culture and the highest standards of corporate behaviour stimulates value creation.”

Dear shareholders and other stakeholders

At Direct Line Group, we are committed to meeting the high standards of corporate governance rightly expected of a Group such as ours. Having complied with the UK Corporate Governance Code in relation to the key Board structure and processes by the time of the IPO in 2012, we undertook a governance review in 2013. This was designed to further test whether we have the most appropriate governance framework fit for a stand-alone listed company, with clarity as to accountabilities and responsibilities.

Our objective of good corporate governance influences everything that we do at Direct Line Group and is the responsibility not only of the Board and the executive management but of every member of staff.

Our Code of Business Conduct governs our interactions with our various stakeholders and ultimately helps with our goal of becoming Britain's best retail general insurer. This is set out alongside.

Our Code of Business Conduct

The Board requires that all employees adhere to the highest possible standards of professional and ethical conduct – and this applies equally to the Board itself. Each function within the Group operates with policies and minimum standards and the following principles:

- **Business practices**
We shall engage in honest, professional and ethical conduct and maintain effective procedures to prevent confidential information being misused
- **Dealing with customers**
We shall treat customers fairly, openly and honestly and operate an effective complaints process to address any perceived departure from these standards
- **Dealing with shareholders and other stakeholders**
We shall seek to maximise shareholder value over time, recognising that wealth generated also benefits customers and employees as well as the communities where we operate
- **Dealing with employees**
We shall maintain a working environment that attracts, motivates and retains employees and shall be intolerant of any type of discrimination, harassment or victimisation
- **Dealing with suppliers of goods and services and business partnerships**
We shall maintain the highest possible standards of integrity in business relationships with suppliers and partners by treating them honestly and with respect and avoiding compromising offers of gifts and hospitality¹
- **Dealing with communities and the environment**
We shall contribute to the social and economic well-being of those communities where we are an employer and encourage employees to participate in projects and initiatives to strengthen those communities
- **Dealing with competitors**
We shall compete with competitors honestly and in accordance with competition law
- **Dealing with regulators**
We shall maintain a constructive and open relationship with our regulators to foster mutual trust, respect and understanding and shall not offer anything to officials in return for favourable treatment

Note:

1. You may view our ethical code for suppliers on our website (www.directlinegroup.com).

Our values



Do the right thing

For our people, our customers, our shareholders and our wider stakeholders; make decisions based on what is right, not what is easy; demonstrate personal and professional integrity; do what's right for the long-term sustainability of our business.



Aim higher

Strive to be the best in every area of the business; be ambitious, courageous and innovative; relentlessly challenge and improve; seek and embrace change; learn from our mistakes; persevere, always deliver our promises and don't settle for second best.



Work together

Collaborate across all levels and across all functions; leverage the skills, knowledge and experience, irrespective of hierarchy, to deliver the best possible results; develop relationships based upon trusting each other, partnerships and win-wins; recognise and celebrate success.

We also place great emphasis on the values set out below that underpin these business principles. As we reported to you last year, the executive management engaged with employees to shape these, with the intention that they become central to our approach and behaviours. In line with those values, we seek to maintain an environment where everybody feels responsible for the future success of the business and is empowered to do the right thing.

Board composition

The Board comprises myself as Chairman (independent upon appointment to the Board), five independent Non-Executive Directors, one Non-Executive Director nominated by RBS Group and therefore not independent, and two Executive Directors.

The changes in directorate during 2013 were in respect of the Directors nominated by RBS Group. Mark Catton stepped down from the Board when RBS Group ceded control of the Company in March 2013 (whereupon RBS Group became entitled to nominate only one and not two Directors to the Board). In October 2013 he was reappointed when Bruce Van Saun resigned in order to take up an appointment as RBS Group's Chief Executive Officer, Citizens and Head of Americas in the United States. Mark Catton will step down as a Director when RBS Group's holding in the Company falls below 20%.

Governance review

To help meet our goals of efficiency and strong governance, the Board undertook a planned post-IPO review of the Group's governance arrangements.

Its aims were to clarify and simplify the governance framework, so as to help improve our day-to-day business operations while maintaining appropriate controls.

As a result of the review, we have re-engineered the High Level Controls and System of Governance Document, Enterprise-wide Risk Management Framework, Group Policies and Minimum Standards to remove unnecessary content, close gaps, reduce duplication and give greater focus and accountability to each element. Further details are provided in this report on page 60.

Consequently, individual components of the governance framework are now more clearly articulated and aligned to the expectations of the Board. The framework as a whole is considered fit for purpose to support our strategic priorities as a dynamic retail general insurance business, rather than as a division within a large bank.

I believe that this exercise will increase ownership and oversight and that our governance arrangements have become more transparent and effective.

Diversity

We are strongly committed to the merits of diversity at Board level and throughout the Group. 33% of the Board are women and we are keen to maintain this representation at around the current level. During the year, the proportion of women on the Executive Committee increased from 10% to 20% – that is, two women on a Committee of 10, namely Sara Gomez, Group Human Resources Director, and Angela Morrison, Chief Information Officer.

Board effectiveness review

Our intended practice is to conduct a thorough review of the effectiveness of the performance of the Directors, the Board as a whole and its committees on an annual basis, with the input of an external facilitator at least once every three years.

Given that the Board was largely new to the Company last year in the run up to the IPO, I felt it was appropriate to assess its performance at the same time as reviewing the main elements of the Company's governance architecture. Accordingly, the Company appointed Edis-Bates Associates to assist us as independent external facilitators. A description of the process and the findings of the evaluation are set out on page 63.



Michael N Biggs, Chairman
25 February 2014



Take ownership

Treat it like it's OUR business; take the initiative, if you can see a better way, go make a difference; take decisions, be accountable for your actions in whatever role you carry out; take responsibility for your own personal development and performance.



Say it like it is

Be real, authentic and true to self; have adult to adult conversations with all audiences; listen, seek to understand and respect diversity of views; be open, call out issues we see; share information and keep things as simple as possible.



Bring all of yourself to work

Be the best you can be, the real and whole you; celebrate our diversity of skills, experiences and personalities; be a role model to others, demonstrate 'can do' spirit, have fun and make this a great place to be; be excited about our Company and our future; believe in yourself, feel confident and empowered.