

Notes to the financial statements

1. Basis of Presentation

Zurich Financial Services presents its financial statements in accordance with Swiss law.

2. Summary of significant accounting policies

a) Exchange rates

Assets and liabilities expressed in currencies other than Swiss francs are translated at year-end exchange rates. Revenues and expenses are translated using the exchange rate at the date of the transaction. Unrealized exchange losses are recorded in the statement of income and unrealized exchange gains are deferred until realized.

b) Investments in subsidiaries

Investments in subsidiaries are equity interests, which are held on a long-term basis for the purpose of the holding company's business activities. They are carried at a value no higher than their cost price less adjustments for impairment.

3. Administrative expense

Administrative expense consists mainly of directors' fees of CHF 2,936,941 (prior year CHF 2,634,268), and management fees of CHF 8,000,000 (prior year CHF 8,000,000).

4. Taxes

The tax expense consists of income, capital and other taxes.

5. Investments in subsidiaries

Investments in subsidiaries include a 57% interest in Zurich Group Holding with a carrying value of CHF 6,064,302,120 (prior year CHF 6,064,302,120) and a 100% interest in Allied Zurich p.l.c., with a carrying value of CHF 4,595,865,096 (prior year CHF 4,595,865,096). Allied Zurich p.l.c. holds the remaining 43% interest in Zurich Group Holding. Additionally, Zurich Financial Services holds 49,000 shares of Zurich Insurance Company with a book carrying value of CHF 2,750,190 (prior year CHF 2,750,190).

6. Commitments and contingencies

Zurich Financial Services has provided unlimited guarantees in support of various entities belonging to the Zurich Capital Markets group of companies and to the Farmers Group Inc. In addition, Zurich Financial Services has agreed with the Superintendent of Financial Institutions, Canada, to provide additional capital in case the applicable capital adequacy tests for the Canadian business are not met and to provide assistance in case of liquidity issues.

Furthermore, Zurich Financial Services has entered into various support agreements and a guarantee for the benefit of its subsidiaries. These contingencies amounted to CHF 4,061 million as of December 31, 2006 (CHF 4,118 million as of December 31, 2005).

Zurich Financial Services knows of no event that would require it to satisfy the guarantees or to take action under a support agreement.

7. Shareholders' equity

a) Issued share capital

As of December 31, 2006 Zurich Financial Services had 144,749,399 issued and fully paid registered shares of CHF 0.10 par value, amounting to a share capital of CHF 14,474,939.90. As of December 31, 2005, the share capital amounted to CHF 360,017,387.50, divided into 144,006,955 fully paid registered shares of CHF 2.50 par value.

On February 15, 2006, the Board of Zurich Financial Services approved the issuance of a maximum of 1,000,000 dividend-paying shares from the contingent share capital to employees. At the Annual General Meeting on April 20, 2006, shareholders approved a share capital reduction in the form of a nominal value reduction of each registered share from CHF 2.50 to CHF 0.10. At the effective date of the nominal value reduction on July 3, 2006 Zurich Financial Services had 144,565,255 issued and fully paid shares, including 558,300 shares issued out of the contingent capital. As a result of this reduction, the share capital was reduced by CHF 346,956,612 from CHF 361,413,137.50 to a new total of CHF 14,456,525.50. Until December 31, 2006, a total of 742,444 shares were issued to employees from contingent share capital. As a consequence, 144,749,399 fully paid shares with a nominal value of CHF 0.10 were issued as of December 31, 2006, amounting to a share capital of CHF 14,474,939.90.

In the previous year, shareholders approved, at the Annual General Meeting on April 19, 2005, a share capital reduction in the form of a nominal value reduction of each registered share from CHF 6.50 to CHF 2.50. As a result of that reduction, the share capital was reduced by CHF 576,027,820 from CHF 936,045,207.50 to CHF 360,017,387.50.

b) Authorized share capital

Until June 1, 2008, the Board of Zurich Financial Services is authorized to increase the share capital by an amount not exceeding CHF 600,000 by issuing up to 6,000,000 fully paid registered shares with a nominal value of CHF 0.10 each. An increase in partial amounts is permitted. The Board determines the date of issue of such new shares, the issue price, type of payment, conditions for exercising pre-emptive rights, and the beginning of the dividend entitlement. The Board may issue such new shares by means of a firm underwriting by a banking institution or syndicate with subsequent offer of those shares to the current shareholders. The Board may allow the expiry of pre-emptive rights which have not been exercised, or it may place these rights as well as shares, the pre-emptive rights of which have not been exercised, at market conditions.

The Board is further authorized to restrict or withdraw the pre-emptive rights of shareholders and to allocate them to third-parties if the shares are to be used for the take-over of an enterprise, or parts of an enterprise or of participations or if issuing shares for the financing including re-financing of such transactions; or for the purpose of expanding the scope of shareholders in connection with the quotation of shares on foreign stock exchanges.

c) Contingent share capital

Capital market instruments and option rights to shareholders:

The share capital of Zurich Financial Services may be increased by an amount not exceeding CHF 548,182.80 by the issuance of up to 5,481,828 fully paid registered shares with a nominal value of CHF 0.10 each (1) through the exercise of conversion and/or option rights which are granted in connection with the issuance of bonds or similar debt instruments by Zurich Financial Services or one of its Group companies in national or international capital markets; and/or (2) by the exercise of option rights which are granted to the shareholders. When issuing bonds or similar debt instruments connected with conversion and/or option rights, the pre-emptive rights of the shareholders will be excluded. The current owners of conversion and/or option rights shall be entitled to subscribe for the new shares. The conversion and/or option conditions are to be determined by the Board.

The Board of Directors is authorized, when issuing bonds or similar debt instruments connected with conversion and/or option rights, to restrict or withdraw the right of shareholders for advance subscription in cases where such bonds are issued for the financing or re-financing of a takeover of an enterprise, of parts of an enterprise, or of participations. If the right for advance subscription is withdrawn by the Board, the convertible bond or warrant issues are to be offered at market conditions (including standard dilution protection provisions in accordance with market practice) and the new shares are issued at then current convertible bond or warrant issue conditions. The conversion rights may be exercisable during a maximum of 10 years and option rights for a maximum of seven years from the time of the respective issue. The conversion or option price or its calculation methodology shall be determined in accordance with market conditions, whereby for shares of Zurich Financial Services the quoted share price is to be used as a basis.

Employee participation:

Following the decision of the Board of Directors of Zurich Financial Services of February 15, 2006 to issue up to a maximum of 1,000,000 dividend-paying shares with a nominal value of CHF 0.10 each out of the 1,500,000 shares available for employees, until December 31, 2006, 742,444 shares of this contingent share capital have been issued. Consequently, as of the same date, the share capital may be increased by an amount not exceeding CHF 75,755.60 by issuing the remaining 757,556 fully paid registered shares with a nominal value of CHF 0.10 each to employees of Zurich Financial Services and Group companies. The pre-emptive rights of the shareholders, as well as the right for advance subscription, are excluded. The issuance of shares or respective option rights to employees shall be subject to one or more regulations to be issued by the Board of Directors and shall take into account performance, functions, levels of responsibility and criteria of profitability. Shares or option rights may be issued to the employees at a price lower than that quoted on the stock exchange.

8. Reserve for treasury shares

This reserve fund corresponds to the purchase value of all Zurich Financial Services shares held by Group companies of Zurich Financial Services as shown in the table below.

Reserve for treasury shares	Number of shares 2006	Purchase value 2006 ¹	Number of shares 2005	Purchase value 2005 ¹
As of January 1	192,027	49,623	298,113	77,235
Additions during the year	110,000	35,008	532,682	112,077
Sales during the year	(140,576)	(41,448)	(638,768)	(138,636)
Decrease due to nominal value reduction of common stock		(384)		(1,053)
As of December 31	161,451	42,799	192,027	49,623
Average purchase price of additions, in CHF		318		210
Average selling price, in CHF		281		204

¹ in CHF thousands

9. Shareholders

The shares registered in the share ledger as of December 31, 2006, were owned by 112,662 shareholders of which 106,839 were private individuals holding 20.1% of the shares (or 11.8% of all outstanding shares), 2,226 were foundations and pension funds holding 8% of the shares (or 4.7% of all outstanding shares), and 3,597 were other legal entities holding 71.9% of the shares (or 42% of all outstanding shares).

According to the information available to us on December 31, 2006, no shareholder of Zurich Financial Services held more than 5% of the voting rights of the issued share capital.

Proposed appropriation of available earnings

	2006	2005
Registered shares eligible for dividends		
Shares eligible as of December 31, 2006 and 2005, respectively	144,749,399	144,006,955

in CHF thousands	2006	2005
Appropriation of available earnings as proposed by the Board of Directors		
Net income	1,187,996	781,121
Balance brought forward	778,217	662,096
Retained earnings	1,966,213	1,443,217
Dividend	(1,592,243) ²	(665,000) ¹
Transfer to general legal reserve	–	–
Balance carried forward	373,970 ²	778,217 ¹

The Board of Directors proposes a dividend of CHF 11.00 per share to the Annual General Meeting on April 3, 2007.

If this proposal is approved, a payment of CHF 7.15 per share, after deductions of 35% Swiss withholding tax, is expected to be paid starting from April 10, 2007, free of charge and in accordance with dividend payment instructions.

Zurich, February 14, 2007

On behalf of the Board of Directors of Zurich Financial Services

Manfred Gentz

¹ These figures are based on the issued and outstanding share capital on July 3, 2006. The proposed dividend published in the Annual Report 2005 was CHF 662,432 thousand resulting in a balance carried forward of CHF 780,785 thousand. The change was due to a resolution by the Board of Directors on February 15, 2006, according to which, out of contingent share capital, up to 1,000,000 shares could have been allocated for issuance to share based incentive plans. As of July 3, 2006, 558,300 shares have been issued out of the contingent capital.

² These figures are based on the issued and outstanding share capital as of December 31, 2006. They may change following a resolution of the Board of Directors dated February 14, 2007, according to which the remaining contingent capital shares for employees (up to 757,556 shares) may be issued up until the proposed record date for the dividend payment, i.e. April 9, 2007. Treasury shares and shares held for cancellation by Zurich Financial Services on April 9, 2007 are not entitled to dividends.