Gresham Insurance Company Limited

Solvency and Financial Condition Report

Year ended 31 December 2017

AVIVA

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Gresham Insurance Company Limited

Solvency and Financial Condition Report

2017

Summary

The purpose of the Solvency and Financial Condition Report (SFCR) is to provide information about the capital position of Gresham Insurance Company Limited (the Company), at 31 December 2017, based on the Solvency II (SII) requirements.

The report sets out different aspects of the Company's business and performance, system of governance, risk profile, valuation methods used for solvency purposes and its capital management practices.

Business and Performance

The Company is a limited company registered in England and Wales and member of the Aviva plc group of companies. The Company transacts general insurance business in the United Kingdom through a business arrangement with Barclays Bank plc. The major class of business underwritten is personal lines home insurance. Whilst the Company only conducts non-life insurance activities, it also has life insurance obligations in relation to annuities stemming from non-life insurance contracts (PPO).

The Company made a profit before tax of £4m in the year ended 31 December 2017 *(2016: profit of £6m)*. This comprises an underwriting profit of £1m *(2016: profit of £3m)*, net investment income of £nil *(2016: £1m)* and a profit from other activities of £3m *(2016 profit of £2m)*.

Gross written premium fell by 9% in the year *(2016: fell by 8%)* because strong new business growth has not been large enough to offset a declining back book of policies as a result of a competitive home insurance market. The majority of written premium is ceded to the Company's immediate parent Aviva Insurance Limited (AIL), through a quota share reinsurance arrangement, with levies being excluded from this arrangement. Gross claims incurred of £55m *(2016: £55m)* were unchanged. Net claims incurred are £nil *(2016: £nil)* due to the reinsurance arrangement with AIL.

The Company's net investment income of £nil *(2016: £1m)* comprised interest receivable and unrealised losses *(2016: unrealised gains)* on the Company's holding of Government Bonds and Collective Investment Undertakings. The Company received non-insurance income of £3m during the year *(2016: £4m)*.

There have been no significant business or other events during the year which have had a material effect on the Company.

Section A of this report sets out further details about the Company's key operations and financial performance over the reporting period.

System of Governance

The Board's responsibilities include ensuring that an appropriate System of Governance is in place throughout the Company. To discharge this responsibility, the Board has established frameworks for risk management and internal control using a 'three lines of defence' model. However, the Board sets the Company's risk appetite itself. A strong system of governance throughout the Company aids effective decision-making and supports the achievement of the Company's objectives for the benefit of customers, shareholders and regulators. Key features of the Company's System of Governance are as follows:

- The roles and responsibilities of the Board are well defined;
- The Company's Board has delegated responsibilities to management within the Aviva Group to assist in its oversight of risk management and the approach to internal controls;
- The Company has implemented four key control functions – Risk Management, Actuarial, Compliance and Internal Audit;

- The Company has in place a remuneration policy, skills requirements and procedures for assessing the fitness and propriety of senior management and key function holders;
- The Company's risk strategy, appetite and framework, its approach to its Own Risk and Solvency Assessment (ORSA), and its governance over the use of the standard formula are set out in its Risk Management Framework policy and its risk policies and business standards; and
- The Company's outsourcing strategy is supported by its Procurement and Outsourcing Business Standard.

There have been no material changes in the system of governance during the year.

Section B of this report provides further details of the Company's System of Governance.

Risk Profile

The Company's business is about protecting its customers from risk. As an insurer, the Company accepts the risks inherent to its core business line of non-life insurance.

The Company receives premiums which are invested in order to maximise risk-adjusted returns, so that the Company can fulfil its promises to customers while providing a return to its shareholders. In doing so, the Company has a preference for retaining those risks which it believes it is capable of managing to generate a return.

The types of risk to which the Company is exposed have not changed significantly over the year and remain credit, market, underwriting, liquidity and operational risks.

For those risk types managed through the holding of capital, the Company measures and monitors its risk profile on the basis of the Solvency Capital Requirement (SCR). Some categories of risk are not measured and managed solely by holding capital, principally liquidity risk, which is measured through both absolute level targets and bespoke liquidity coverage ratios.

Section C of this report further describes the risks to which the Company is exposed and how it measures, monitors, manages and mitigates these risks, including any changes in the year to risk exposures and specific risk mitigation actions taken.

Valuation for Solvency Purposes

Assets, technical provisions and other liabilities are valued in the Company's SII Balance Sheet according to the SII regulations. The basis of the SII valuation principle is the amount for which they could be exchanged, transferred or settled by knowledgeable and willing third parties in an arm's length transaction. The value of Technical Provisions under SII is equal to the sum of a Best Estimate Liability and a Risk Margin.

At 31 December 2017, the Company's excess of assets over liabilities was £67m *(2016: £80m)* on a SII basis which is £1m *(2016: £2m)* higher than the value under IFRS.

Section D of this report provides further description of the bases, methods and main assumptions used in the valuation of assets, Technical Provisions and other liabilities for each material asset/liability class. In addition, it also provides an explanation of the material differences between the IFRS and SII bases of valuation.

Capital Management

The Company manages Own Funds in conjunction with solvency capital requirements. In the calculation of the SCR, the Company has chosen to implement the standard formula (SF).

In managing capital, the Company seeks, on a consistent basis, to:

- Match the profile of its assets and liabilities, taking into account the risks inherent in the business;
- Maintain sufficient, but not excessive, financial strength in accordance with risk appetite to support new business growth and satisfy the requirements of the Company's regulators and other stakeholders, giving the Company's customers assurance of its financial strength;
- Retain financial flexibility by maintaining strong liquidity; and
- Allocate capital rigorously to support value adding growth and repatriate excess capital where appropriate.

There have been no material changes to the objectives, policies or processes of the Company for managing its Own Funds during the year.

At 31 December 2017, the total eligible Own Funds to meet the SCR was £67m *(2016: £80m)* all of which was represented by unrestricted tier 1 capital. The Company's SCR, at 31 December 2017, was £5m *(2016: £7m)*. The overall surplus position was £62m *(2016: £73m)* which translates to a regulatory cover ratio of 1,338% *(2016: 1,175%)*.

Section E of this report further describes the objectives, policies and procedures employed by the Company for managing its own funds. The section also covers information on structure and quality of Own Funds and calculation of SCR, including information about the Company's use of SF.

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A. Business and Performance

In this Chapter

A.1 Business

A.2 Underwriting Performance

A.3 Investment Performance

A.4 Performance of Other Activities

A.5 Any Other Information

A. Business and Performance

The 'Business and Performance' section of the report sets out the Company's business structure, key operations, and financial performance over the reporting period.

A.1 Business

The Company is a limited company registered in England and Wales and is a member of the Aviva plc group of companies, (the Group).

Qualifying holdings

The Company's shares and the associated voting rights are wholly owned by AIL, being a qualifying holding in the Company.

Supervisor

The Company is authorised by the Prudential Regulatory Authority (PRA). The Company and the Group are regulated by the PRA and the Financial Conduct Authority (FCA) in the UK. The PRA is part of the Bank of England. Contact details for the PRA are as follows:

Address	20 Moorgate, London, EC2R 6DA
Telephone number	+44 (0) 20 7601 4444

External auditor

The Company's external auditor is PricewaterhouseCoopers LLP. Contact details are as follows:

Address	7 More London Riverside, London, SE1 2RT
Telephone number	+44 (0) 20 7583 5000

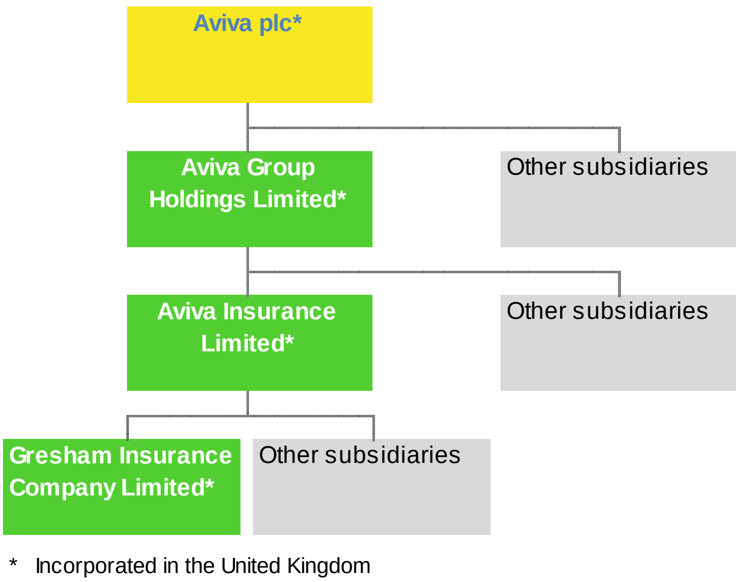
Financial statements

The Company's financial statements are available from the Company Secretary, Aviva Company Secretarial Services Limited, St Helen's, Undershaft, London, EC3P 3DQ.

The SFCR is presented in pound sterling rounded to the nearest million which is consistent with the presentation in the IFRS financial statements. The Quantitative Reporting Templates (QRT) are presented in pound sterling rounded to the nearest thousand. Rounding differences of +/- one unit can occur.

A.1.1 Organisation

The following chart shows, in simplified form, the Company's position within the structure of the Group as at 31 December 2017:



Gresham Insurance Company Limited is a subsidiary of Aviva Insurance Limited, which is registered in Scotland. Aviva plc is the ultimate controlling parent entity registered in England.

A.1.2 Business operations and events occurring in the year

Business operations

The only material SII line of business underwritten by the Company is Fire and Other Damage to Property. The Company underwrites its business in the UK, as presented in QRT S.05.01 (Appendix F.1).

Whilst the Company only conducts non-life insurance activities, it does have life insurance obligations in relation to annuities stemming from non-life insurance contracts (PPO).

A.2 Underwriting Performance

A.2.1 Measurement of underwriting performance

The Company uses the underwriting result to measure its underwriting performance. Underwriting result is a non-GAAP financial performance measure, calculated on an IFRS basis. It excludes certain items to enhance comparability and understanding of underwriting performance by highlighting net income attributable to on-going underwriting operations. Examples of items excluded from underwriting result are investment return, economic assumption changes, and non-insurance income. The items excluded from underwriting result, which comprise the Company's investment performance and its performance of other activities, are detailed in sections A.3 and A.4 respectively.

A.2.2 Underwriting performance during the year

The Company made a profit before tax of £4m for the year ended 31 December 2017 *(2016: £6m)*. This comprises an underwriting profit of £1m *(2016: £3m)*, net investment income of less than £1m *(2016: £1m)* and a profit from other activities of £3m *(2016: £2m)*, as shown in the table below.

Reconciliation of underwriting result to profit before tax Year ended 31 December	£m 2017	£m 2017	*£m* *2016*	*£m* *2016*
Profit for the year before tax		4		*6*
Less: net investment income (see A.3)		-		*(1)*
Add back: Other costs	-		*2*	
Less: non-insurance income	(3)		*(4)*	
Performance of other activities (see A.4)		(3)		*(2)*
Underwriting profit		1		*3*

A.2.3 Solvency II lines of business

A summary of the information provided in the premium, claims and expenses QRT S.05.01 is provided in the table below. The net result of £4m *(2016: £5m)* comprises the underwriting result of £1m *(2016: £3m)* and the profit from other activities of £3m *(2016: £2m)*.

£m	Fire and other damage to property insurance	Other	Total
Year ended 31 December 2017			
Gross written premium	144	5	149
Net earned premium	7	-	7
Gross claims incurred	(54)	(1)	(55)
Net claims incurred	(1)	1	-
Net expenses incurred	(6)	-	(6)
Total expenses			(3)
Year ended 31 December 2016			
Gross written premium	*159*	*5*	*164*
Net earned premium	*8*	*-*	*8*
Gross claims incurred	*(51)*	*(4)*	*(55)*
Net claims incurred	*1*	*(1)*	*-*
Net expenses incurred	*(7)*	*-*	*(7)*
Total expenses			*(3)*

The Company's gross written premium, which is underwritten in the UK, decreased by 9% *(2016: 8%)*. There were stronger new business sales compared to 2016 however, this new business growth has not been large enough to offset a declining back book of policies as a result of a competitive home insurance market. The majority of written premium is ceded to the Company's parent AIL, through a quota share reinsurance arrangement, with levies being excluded from this arrangement.

Gross claims incurred of £55m *(2016: £55m)* were unchanged. The effect on gross claims incurred of lower premium in 2017 were offset by the impact of £6m prior year claims reserve releases in 2016 not replicated in 2017. Net claims incurred were £nil reflecting the reinsurance arrangement with AIL.

Net expenses incurred decreased during the year due to reduced levies of £6m *(2016: £7m)*. Total expenses included non-insurance income of £3m *(2016: £4m)*, (see A.4).

A.3 Investment Performance

The Company's net investment income for the year of £nil *(2016: £1m)* comprised interest receivable of £1m and unrealised losses on the Company's holding of financial investments in Government Bonds and Collective Investment Undertakings of £1m. Net investment income is stated after the deduction of immaterial investment expenses.

A.4 Performance of Other Activities

A.4.1 Other income and expense

As described in section A.2.1, performance of other activities comprises those items of other income and expense, other than net investment return, excluded from underwriting result. The Company delivered a profit before tax of £4m *(2016: £6m)*, of which £3m *(2016: £2m)* arose from its performance of other activities during the year. The material component of the Company's other activities is its non-insurance income of £3m *(2016: £4m)*. Non-insurance income arises from items, such as legal expenses, sold as add-ons to existing policies; this income has fallen during the year in line with premium.

A.5 Any Other Information

There is no other material information to report regarding the Company's Business and Performance.

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B. System of Governance

In this Chapter

B.1 General Information on the System of Governance

B.2 Fit and Proper Policy

B.3 Risk Management System including the Own Risk and Solvency Assessment

B.4 Internal Control System

B.5 Internal Audit Function

B.6 Actuarial Function

B.7 Outsourcing

B.8 Any Other Information

B. System of Governance

This section of the report sets out information regarding the 'System of Governance' in place within the Company. Details of the structure of the undertaking's 'administrative, management or supervisory body' (defined as the Board) are provided. The roles, responsibilities and governance of key functions (defined as the Risk, Compliance, Internal Audit and Actuarial Functions) are also provided. Other components of the System of Governance are also outlined, including the risk management system and internal control system implemented across the business.

B.1 General Information on the System of Governance

B.1.1 Board structure

The Company's Board is responsible for promoting the long-term success of the Company and for setting its strategy. It sets the Company's risk appetite and satisfies itself that financial controls and risk management systems are robust. A strong system of governance throughout the Company aids effective decision making and supports the achievement of the Company's objectives for the benefit of policyholders and the shareholder.

The duties of the Company's Board are set out in its terms of reference. The terms of reference lists both those items that are specifically reserved for decision by the Board and those matters that must be reported to the Board. The Company's Board is composed of senior management from within the Group and a Director nominated by Barclays Bank plc.

The Company's Board has delegated responsibilities to management within the Group to assist in its oversight of risk management and the approach to internal controls.

The 'three lines of defence model', and roles and responsibilities of key functions

Roles and responsibilities for risk management in the Company are based around the three lines of defence model.

The first line

Management are responsible for the application of the Risk Management Framework and for implementing and monitoring the operation of the system of internal control, and for providing assurance to the Board.

The second line

- The Risk Function is accountable for the quantitative and qualitative oversight and challenge of the identification, measurement, management, monitoring and reporting of principal risks and for developing the Risk Management Framework;
- The Actuarial Function is accountable for actuarial methodology, and reporting to the relevant governing body on the adequacy of reserves and capital requirements, as well as on underwriting and reinsurance arrangements; and
- The Compliance Function supports and advises the business on the identification, measurement and management of its regulatory, financial crime and conduct risks and is accountable for monitoring and reporting on the Company's compliance risk profile.

The third line

The Internal Audit Function provides independent and objective assessment on the robustness of the Risk Management Framework and the appropriateness and effectiveness of internal control to the Board.

Sections B.3.2, B.4.2, B.5 and B.6 detail the roles, responsibilities, authority, resources, independence and reporting lines of the Risk, Compliance, Internal Audit and Actuarial Functions respectively, and how their independence is ensured.

B.1.2 Material changes in the system of governance

There have been no material changes in the system of governance during the year.

B.1.3 Adequacy of the Company's system of governance

An assessment of the effectiveness of the governance, internal control and risk management systems of the parent company and several of its subsidiaries, including the Company, was conducted at the end of 2017, leading to the parent company's Chief Executive Officer (CEO) certifying that:

- There are sound risk management and internal control systems that are effective and fit for purpose in place across the business; and
- The business operates in a manner which conforms to the minimum requirements outlined in the Company's risk policies and business standards.

The Company's Chief Risk Officer (CRO) provided his own certificate which states that:

- The Risk Function has reviewed and challenged the process supporting the CEO's certification and is satisfied that it can provide reasonable assurance of the material accuracy and completeness of the CEO's assessment; and
- No material gaps exist in the Risk Management Framework.

Any material risks not previously identified, control weaknesses or non-compliance with the Company's risk policies and business standards or local delegations of authority are highlighted as part of this process. The results of the certification process and details of key failings or weaknesses are reported to the Board to enable them to carry out an effectiveness assessment. The Board last carried out a full review of the effectiveness of the Company's systems of internal control and risk management in March 2018.

B.1.4 Remuneration policy and practices

All staff are employed by a fellow subsidiary of Aviva plc, Aviva Employment Services Limited, and a recharge is made to the Company. All Aviva staff acting on behalf of the Company are subject to the Group's remuneration policy, which is designed to incentivise and reward employees for achieving business goals in a manner that is consistent with the Group's strategy, business plans, values and behaviours, sound and effective risk management and good governance.

The directors of the Company receive no remuneration from the Company.

The director appointed by Barclays Bank plc is remunerated in line with practices within Barclays Bank plc.

Executive directors

The Group's remuneration policy provides market competitive remuneration. Remuneration of executive directors includes a basic salary, variable components, pension contributions and benefits including relocation and mobility. This incentivises executive directors to achieve both the annual business plan and through significant levels of deferral the longer-term strategic objectives of the businesses for which they are responsible. As well as rewarding the achievement of objectives, variable remuneration can be zero if performance thresholds are not met.

Remuneration of EDs is split between the following components:

- Basic salary informed by individual and business performance, levels of increase for the broader UK employee population and relevant pay data;
- Variable components (refer to section 'Variable components' below for further details);
- Pensions;
- Benefits;
- Relocation and mobility; and
- Shareholding requirement.

Variable components

The main forms of variable remuneration for the EDs are:

- Annual Bonus: Awards are based on performance in the year. Performance is assessed against a range of relevant financial, employee, customer and risk targets designed to incentivise the achievement of strategy as well as individual strategic objectives. Targets are set annually and pay-out levels are determined based on performance against those targets. A significant proportion of any bonus award is deferred into shares which vest in three equal tranches; and
- Long Term Incentive Plan (LTIP): Shares are awarded which vest over a three year period, in some cases dependent on the achievement of performance conditions over that period.

Employees

Remuneration arrangements for Aviva employees that are not executive directors take account of the seniority and nature of the role, and individual performance. The aim is to provide employees with remuneration packages that are clear and simple to understand, transparent, consistent and fair. Remuneration includes a basic salary, variable components and pension contributions.

The variable components are discretionary and fully flexible as opposed to a contractual entitlement, and there is a possibility of zero awards being made should the performance of the relevant businesses or individuals require this. Individual awards are based on a calibrated assessment of performance of individuals relative to peers.

The remuneration of employees in Risk, Compliance, Internal Audit and Actuarial Functions is determined independently of the financial results of the business areas they oversee. This reinforces the independence of these Functions.

Performance criteria for share awards

Shares in Aviva plc can be awarded to both executive directors and employees. These vest after three years, in some cases dependent on performance conditions. Current performance targets are based on two measures. The first measures return on equity and is set as a percentage. The second compares total shareholder return to other similar companies.

Pension and early retirement schemes

There were no enhanced pension arrangements or early retirement schemes for members of the Board or key function holders in place during 2017.

B.1.5 Material transactions with the shareholder, persons with significant influence on the Company and members of the Board

The Company has a quota share reinsurance arrangement with AIL, with effect from 1 January 2006. The key terms of the agreement remain: a 100% cession rate on premiums, claims costs and underwriting expense costs is applied in respect of the underwriting year; and a requirement for the Company to retain a percentage in relation to levies.

The key management of the Company are considered to be the statutory directors. Note 4 to the financial statements gives details of their remuneration.

B.2 Fit and Proper Policy

B.2.1 Requirements for the persons who run the Company or who are other key function holders

The membership of the Board is designed to provide skills necessary to manage the Company's underlying business activities and key risks. Specific skills considered within Board appointments include knowledge and experience in respect of:

- Insurance and financial markets;
- Business strategy and business models;
- System of governance;
- Financial and actuarial analysis; and
- Regulatory framework and requirements.

The Company's requirements in respect of skills, knowledge and expertise for key function holders are set following engagement with both internal and external subject matter experts in each specialism. These requirements and qualifications are captured within individual role descriptions for each key function role.

B.2.2 Process assessing fitness and propriety

The Company has implemented processes to ensure that individuals acting on its behalf are both fit and proper in line with the PRA Fit and Proper requirements for individuals subject to the Senior Insurance Managers Regime and the FCA requirements for Approved Persons. This means that as part of recruitment and employee screening an individual's career history will be assessed and validated to establish whether an individual's skills and knowledge are appropriately matched to the role. It also means that checks are in place to ensure that an individual is honest, of good reputation, has integrity and is financially sound.

The governance over the fitness and propriety of individuals includes recruitment, performance management and training. To ensure that the Company protects itself against employing individuals who potentially could threaten its customers, properties, facilities or reputation, the majority of its fitness and propriety processes take place at recruitment and more specifically at pre-employment screening. A minimum set of basic screening requirements has been agreed and implemented. Additional enhanced screening requirements are applied for individuals who will run the Company or become notified or approved senior managers.

Compliance with the initial and ongoing fitness and propriety minimum requirements is reported on a half-yearly basis by the CEO of the parent company to the Group People function.

B.3 Risk Management System including the Own Risk and Solvency Assessment

B.3.1 Risk Management Framework

The Risk Management Framework forms an integral part of management and Board processes and the decision-making framework across the Company. The key elements are:

- Risk appetite;
- Risk governance, including risk policies and business standards and roles and responsibilities; and
- The processes used to identify, measure, manage, monitor and report risks (IMMMR), including the use of risk models and stress and scenario testing.

For the purposes of risk identification and measurement risks are usually grouped by risk type: credit, market, liquidity, general insurance and operational risk. Risks falling within these types may affect a number of metrics, including those relating to balance sheet strength, liquidity and profit. They may also affect the performance of products delivered to customers and service provided to customers and distributors, which can be categorised as risks to brand and reputation or as conduct risk.

To promote a consistent and rigorous approach to risk management the Company has adopted a number of risk policies and business standards which set out the risk strategy, appetite, framework and minimum requirements for its operations. Compliance with these policies and standards is confirmed annually.

A regular top-down key risk identification and assessment process is carried out by the Risk Function. This includes the consideration of emerging risks and is supported by deeper thematic reviews. The risk assessment processes are used to generate risk reports which are shared with the Board.

Risk models are an important tool in the measurement of risks and are used to support the monitoring and reporting of the risk profile and in the consideration of the risk management actions available. A range of stress (where one risk factor, such as equity returns, is assumed to vary) and scenario (where combinations of risk factors are assumed to vary) tests are undertaken to evaluate their impact on the business and the management actions available to respond to the conditions envisaged.

The Risk Function is accountable for quantitative and qualitative oversight and challenge of the IMMMR process and for developing the Risk Management Framework. Internal Audit provides an independent assessment of the risk framework and internal control processes.

Board oversight of risk and risk management across the Company is maintained on a regular basis. The Board has overall responsibility for determining risk appetite, which is an expression of the risk the business is willing to take. Risk appetites are set relative to capital and liquidity.

The Company's position against risk appetite is monitored and reported to the Board on a regular basis. Long-term sustainability depends upon the protection of franchise value and good customer relationships. As such, the Company has a risk preference that it will not accept risks that materially impair the reputation of the Company and requires that customers are always treated with integrity.

B.3.2 Risk Function

The Risk Function is responsible for the design and implementation of the Risk Management Framework. The Risk Function reports to the Company's Board on material risks, together with any other specific areas of risk requested by the Board, and assists the Board and management in the effective operation of the Risk Management Framework including, amongst other things, the provision of specialist analysis and quality reviews, an aggregated view of the risk profile, and an assessment of the key risks associated with the business's strategy, major projects, strategic investments and other key decisions.

The Risk Function has authority to review all areas of the Company and has full, free and unrestricted access to all activities, records, property and personnel necessary to complete its work. The CRO has direct management accountability for the Risk Function.

B.3.3 ORSA

The Company considers that its ORSA comprises all the processes and tools that underpin the consideration of risk and capital implications in key decisions, including business planning. It provides a continuous and forward-looking assessment of the short-term and long-term risks that the Company faces, or may face, and ensures that its capital requirements are met at all times. In this context, the Board has confirmed the use of the regulatory capital requirement plus a risk appetite buffer as the Company's own measure of capital for the purposes of the ORSA.

The ORSA therefore comprises a number of elements of the Risk Management Framework, which are embedded in the business through the requirements of the business standards around capital allocation, strategy, business planning and stress testing. These elements create an overview of the impact of risk on the business, which are taken into account by management in day-to-day decision making. In particular, using economic capital in decision making ensures risk and capital management are connected. The outcomes of the ORSA processes provide the Company's Board and management with insights on the key risks and current and future capital requirements.

The CEO and his direct reports are responsible for the majority of the underlying ORSA processes set out above. The Risk Function is responsible for the design of the Risk Management Framework, including the ORSA, the ORSA Policy and annual ORSA reporting.

Review and approval

The outputs from the ORSA processes are reported to and reviewed by the Board regularly during the year. The Board sets the approach to the ORSA and oversees the ORSA processes. The results of the Company's ORSA processes are considered by the Board when reviewing the Company's strategy and plans.

The annual ORSA Report brings together and summarises a high level description of the key components of ORSA, together with key developments and outcomes during the year. This is submitted to the Board, and subject to its approval, shared with the PRA.

Economic capital (as a risk based capital measure) is embedded in the Company's Risk Management Framework and is used as an input to a range of business and strategic decisions. The framework, supported by risk policies and business standards, sets out the areas where economic capital management information must be used as part of decision making and risk management processes. This ensures that requirements to use economic capital are embedded within the relevant processes including, but not limited to, strategy and planning. Economic capital is calculated using the SF calculation, the appropriateness of which is reviewed annually and reported to the Board.

B.4 Internal Control System

B.4.1 System of Internal Control

The Company's principles for ensuring effective internal control are set out in the Risk Management Framework and, in particular, the Internal Control Business Standard. These include:

- An appropriate "tone from the top". This supports the effective management of exposures, adequate resourcing, effective communication, malpractice reporting, a business ethics code that is annually signed up to by employees, and a commitment to integrity, ethical behaviour and compliance;
- A clear organisational structure that supports the system of internal control and includes the effective operation of an adequately resourced three lines of defence model, appropriate and proportionate segregation of duties, a clear system of delegated authorities, clearly defined roles and responsibilities for staff, and the consideration of risk management and control responsibilities when setting objectives for and reviewing the performance of all staff;
- Implementation of risk policies and business standards, and consistent IMMMR of all risks;
- Effective controls for each of its core business processes which are regularly monitored and reported on; and
- A risk oversight process that provides adequate challenge to the completeness and openness of internal control and risk assessment.

B.4.2 Compliance Function

The primary purpose of the Compliance Function is to assess and manage exposure to regulatory risk. The Compliance Function is an integral part of the Risk Management Framework and constitutes a key part of the Company's corporate governance, including relationships with the FCA and the PRA, and other regulatory bodies. The Compliance Function is a critical contributor to the safe and sound operation of the Company and underpins the achievement of its strategy and business goals. The key processes that comprise the Company's compliance activity are:

- Conduct regulatory risk management (including monitoring regulatory developments), performed by the Compliance Function and including activities such as:
  - Setting conduct and financial crime policy framework;
  - Providing advice, support, guidance and challenge on conduct and financial crime risk; and
  - Managing conduct and financial crime regulatory engagement.

- Prudential regulatory risk management (including monitoring regulatory developments), performed by the Risk Function and including activities such as:
  - Setting prudential regulatory risk policy framework;
  - Providing advice, support, guidance and challenge on prudential regulatory risk; and
  - Managing prudential regulatory engagement.
- Legal developments monitoring, performed by the Legal and Company Secretarial Function.

Through these processes the Compliance, Risk and Legal Functions also take responsibility for reporting information to the Board. The Board receives a report from the CRO annually which covers any material concerns regarding conduct risk and the treatment of customers generally, along with details and an assessment of the adequacy of management's response.

The CRO has responsibility for prudential and conduct regulatory risk management, whilst the General Counsel is responsible for monitoring legal developments. Those carrying out compliance activities have authority to review all areas of the Company and have full, free and unrestricted access to all activities, records, property and personnel necessary to complete their work, where appropriate.

B.5 Internal Audit Function

The Company's Internal Audit Function is led by the Internal Audit Director who reports directly to the Group Chief Audit Officer and to the Chairman of the parent company's Audit Committee.

The Internal Audit Function provides reports to the Company's Board on the robustness of the Company's Risk Management Framework and the appropriateness and effectiveness of the system of internal control. In doing this it considers the adequacy of the Company's system of internal control to manage its business risk and to safeguard its assets and resources. It also considers the effectiveness of any actions put in place by management to address any deficiencies that might exist in the system of internal control.

The Internal Audit Function investigates and reports on cases of suspected financial crime and employee fraud and malpractice, and undertakes designated advisory projects for management.

Independence and objectivity

The Internal Audit Function maintains its independence and objectivity by reporting directly to the Group Chief Audit Officer and the Chairman of the parent company's Audit Committee. The parent company's Audit Committee has a duty to recommend the appointment or dismissal of the Internal Audit Director to the parent company Board and to participate, jointly with the Group Chief Audit Officer or designee, in the determination of the objectives of the Internal Audit Director and the evaluation of his levels of achievement, including consultation with the CEO.

The Internal Audit Director proposes a budget which ensures that Internal Audit has sufficient skills and resources to discharge its responsibilities. The Internal Audit Function is authorised to review all areas of the Company and has full, free, and unrestricted access to all activities, records, property, and personnel necessary to complete its work.

Internal Audit Function staff have no direct responsibility for any operational activities. There is a formal policy of rotating staff to ensure that independence is maintained. There is also a restriction on the audits that staff who have previously worked elsewhere in the Company can perform. The Internal Audit Function cannot perform any projects for management that will threaten its actual or perceived independence and objectivity.

An annual declaration of independence is signed by all members of the Internal Audit Function's staff.

B.6 Actuarial Function

The Actuarial Function is accountable for actuarial methodologies and calibrations, plus the resultant Best Estimate Liabilities and capital requirements. The Actuarial Function produces an annual report to the Board providing all of the information necessary for the Company's Board to form their own opinion on the adequacy of Technical Provisions and on the Company's underwriting and reinsurance arrangements.

The independence of the Actuarial Function is derived through its membership of the wider Risk Function. The Actuarial Function is led by the Chief Risk Actuary, who reports to the Company's CRO. All persons employed by the Actuarial Function in a defined actuarial role are subject to the Fit and Proper policy requirements to ensure they have the requisite skills and knowledge to complete their responsibilities. (Fit and Proper requirements are considered in section B.2.)

The Actuarial Function has the authority to review all areas of the Company and has full, free and unrestricted access to all activities, records, property and personnel necessary to complete its work.

B.7 Outsourcing

Policy

The Procurement and Outsourcing Business Standard contains information on the Company's outsourcing policy, setting out the relevant responsibilities, objectives, process, and monitoring arrangements to be applied in cases of outsourcing, all of which shall be consistent with the overall strategy. The standard applies equally to any externally or internally (intra-group) outsourced activity. The objective of this standard is to ensure that minimum control objectives and controls for supplier related activities are followed by all elements of the business, to ensure that supply risk is managed effectively, customers are being treated fairly and continue to receive good outcomes, as well as mitigating potential financial, operational, contractual, and brand damage caused by inadequate management.

The Business Standard aligns with UK regulatory expectations, the FCA, the PRA, and the SII framework and where appropriate, regulatory guidance will be applied as a requirement. The standard applies to all staff involved in supplier related activities and provides direction to staff on their roles and responsibilities in effectively managing supplier activity. It provides clarity on the definition of outsourcing, including where activity is delegated to an intermediary, and whether a function or activity outsourced is assessed as critical or important. All staff have a responsibility to comply with this standard if they are involved with supplier related activity.

The objectives and controls in the Business Standard cover the following areas:

- Supply governance: business oversight of operational performance for sourcing and supply management activities;
- Sourcing: how a service provider of suitable quality is selected;
- Supplier contracting and approvals: financial, commercial and legal approval of contracts; and
- Supplier management and business continuity: risk based approach to management of supply contracts.

Critical or important outsourcing will attract the highest level of rigour, including regulatory notification, performance and relationship reviews, regulatory compliance review, risk and control assessments.

Critical and important outsourced functions and activities

The Company receives a wide range of services from within the Group. Various claims handling and fulfilment activities, including travel claims handling, loss adjusting and property repairs are outsourced to companies outside the Group.

Jurisdiction of service providers

Services provided from within the Group and claims handling and fulfilment activities are carried out in the UK. Certain support functions are carried out in Sri Lanka.

B.8 Any Other Information

The Company has no other material information to disclose.

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C. Risk Profile

In this Chapter

C.1 Underwriting Risk

C.2 Market Risk

C.3 Credit Risk

C.4 Liquidity Risk

C.5 Operational Risk

C.6 Other Material Risks

C.7 Any Other Information

C. Risk Profile

This chapter provides information on the Company's Risk Profile.

C.1 Underwriting Risk

C.1.1 Exposure

The Company's exposure to non-life insurance underwriting risk arises from:

- Inadequate claims reserving assumptions;
- Unforeseen fluctuations in the timing, frequency and severity of claims and claim settlements relative to expectations;
- Unexpected claims arising from a single source;
- Inaccurate pricing of risks or inappropriate underwriting of risks when underwritten; and
- Inadequate reinsurance protection or other risk transfer techniques.

The Company underwrites household insurance, transacted though a business arrangement with Barclays Bank plc. There are also some outstanding reserves in respect of motor business that was underwritten historically.

The Company has a quota share arrangement with its parent company, AIL, with effect from 1 January 2006. The majority of written premium is ceded to AIL, although an amount of premium is excluded from this arrangement to meet the cost of levies. The Company is also a named party to Group wide external catastrophe reinsurance arrangements.

There were no material changes to the Company's underwriting risk profile over the year to 31 December 2017.

The Company's overall exposure to underwriting risk is measured using the SCR. QRT S.25.01 (Appendix F.1.7) shows that the Company's undiversified SCR for underwriting risk is immaterial *(2016: immaterial)*. Underwriting risk is also measured and monitored in terms of best estimate liabilities, total sum insured and estimated maximum loss. Estimated maximum loss is an estimation of the maximum loss that could be reasonably sustained as a result of a single incident considered to be within the realms of probability.

There has been no material change to the measures used to assess underwriting risk during the reporting period.

C.1.2. Risk concentration

The Company's general insurance business is UK domiciled, and managed and priced in the UK. Its most concentrated non-life underwriting peril is North European Windstorm. The business written is sold exclusively via Barclays Insurance Services Company Limited.

C.1.3 Risk mitigation

The Company manages its exposure to general insurance risk through the application of controls frameworks that include:

- Claims reserving that is undertaken by local actuaries and is also subject to periodic external review;
- Extensive use of data, financial models and analysis to improve pricing and risk selection;
- Underwriting limits linked to delegations of authority that govern underwriting decisions;
- Product development in a management framework that ensures products and propositions meet customer needs;
- Product limits and exclusions; and
- Governance of outsourced functions writing products on behalf of the Company.

The primary technique used to mitigate underwriting risk is reinsurance as described in section C1.1.

The management of insurance risk is overseen by the Board.

C.1.4 Stress and scenario testing and sensitivity analysis

Descriptions of the methods used, assumptions made and outcomes of stress and scenario testing and sensitivity analysis is provided in section C.7.1.

C.1.5 Special purpose vehicles

The Company has not transferred underwriting risk to special purpose vehicles, as defined by the SII Directive.

C.2 Market Risk

C.2.1 Exposure

The Company's exposure to market risk arises from the risk of adverse financial impact resulting directly or indirectly from fluctuations in interest rates and inflation. Market risk arises due to fluctuations in both the value of liabilities and the value of assets held.

Given the reinsurance the Company has in place as outlined in section C1.1, the Company is primarily exposed to fluctuations in interest rates affecting the value of its Government Bonds. There is no exposure to foreign currency exchange rates.

There has been no material change in the Company's overall market risk exposure during the period.

The Company's overall exposure to market risk is measured using the SCR. QRT S.25.01 (Appendix F.1.7) shows that the Company's undiversified SCR for market risk is immaterial *(2016: £1m)*. This includes credit risk in respect of the Company's bond holdings whose risk profile and management is described in section C.3.

There has been no material change to the measures used to assess market risk during the reporting period.

C.2.2 Risk concentration

The Company holds UK Government Bonds and Collective Investment Undertakings. It is thus exposed to a concentration of UK Government Bonds. The Collective Investment Undertakings are invested in liquidity funds.

C.2.3 Risk mitigation

The Company manages market risk locally as part of the wider market risk framework, within local regulatory constraints and in line with established Group policy.

The Company did not have any derivatives during the year or at year-end.

C.2.4 Stress and scenario testing and sensitivity analysis

Descriptions of the methods used, assumptions made and outcomes of stress and scenario testing and sensitivity analysis is provided in section C.7.1.

C.3 Credit Risk

C.3.1 Exposure

The Company's exposure to credit risk arises from the risk that it will incur a financial loss from the default or failure of third parties to meet their payment obligations to the Company, or variations in market values as a result of changes in expectations related to these risks.

The Company's approach to managing credit risk recognises that there is a risk of adverse financial impact resulting from fluctuations in credit quality of third parties including default, rating transition and credit spread movements. The Company's credit risks arise principally from exposures to Government Bonds, insurance debtors, reinsurance counterparties and bank deposits.

The Company's management of credit risk includes implementation of credit risk management processes as part of the wider risk framework (including limits frameworks), the operation of specific risk management committees, and detailed reporting and monitoring of exposures against pre-established risk criteria.

The principal basis used to measure the Company's exposure to credit risk is the SCR. QRT S.25.01 (Appendix F.1.7) shows that the Company's undiversified SCR for credit risk is £4m *(2016: £5m)*. Counterparty risk relates to the risk associated with reinsurers and insurance debtors. The Company is additionally exposed to the credit risk associated with Government Bonds included in the market risk SCR reported in the QRT as described in section C2.1. There has been no material change in the Company's counterparty risk exposure over the reporting period.

The following metrics are also used when measuring and assessing its credit risk exposure and to support risk management actions and investment decisions as part of the monitoring undertaken within the wider UK&I GI framework:

- Maximum exposure: credit exposure of the Company's financial assets to counterparties; and
- External credit rating: available Moody, Standard & Poor and Fitch ratings.

There has been no material change to the measures used to assess credit risk during the reporting period.

The overall credit quality of the Company's financial investments is strong. At 31 December 2017, all Government Bonds were held with the UK Government, rated AA and valued at £64m *(2016: £65m)*. Similarly, reinsurance assets all have external credit ratings of A or above. Collective Investment Undertakings are held with highly rated banking institutions or liquidity funds.

C.3.2 Risk concentration

The Company has exposure to its immediate parent AIL via the reinsurance quota share arrangement discussed in section C.1.1. At 31 December 2017, the reinsurance asset recoverable from AIL is £103m *(2016: £115m)*. This asset is neither impaired nor overdue. As at 31 December 2017, and after allowing for Deferred Acquisition Costs (DAC), this counterparty risk exposure is legally offset against a creditor balance with AIL associated with future premium payments. The Company's exposure to AIL as at 31 December 2017, net of DAC and creditor balances, is negative £20m *(2016: negative £3m)*. The Company is also a named party to Group wide external catastrophe reinsurance arrangements, and hence could independently access external catastrophe reinsurance recoveries due.

The Company's exposure to receivables of £82m at 31 December 2017 *(2016: £91m)* primarily comprises amounts due from insurance contract holders which are neither impaired nor overdue.

C.3.3 Risk mitigation

As described in section C3.1, the Company has in place a credit control framework to manage credit risk.

In accordance with the requirements of the Financial Risk Mitigation Business Standard the effectiveness of arrangements to mitigate credit risk are assessed and documented as part of the wider assessment. On-going monitoring is carried out by reporting management information to the Board, against pre-defined trigger points, to enable appropriate oversight and to prompt action if effectiveness deteriorates.

C.3.4 Stress and scenario testing and sensitivity analysis

Descriptions of the methods used, assumptions made and outcomes of stress and scenario testing and sensitivity analysis is provided in section C.7.1.

C.4 Liquidity Risk

C.4.1 Exposure

The Company's exposure to liquidity risk arises from the risk that its liabilities cannot be settled, in a timely and cost-effective manner, as they fall due because of insufficient liquid assets. Liquidity risk may arise from uncertainty of the value and timing of liabilities or the ability to realise assets to produce cash to meet obligations. The Company assesses liquidity risk under a range of scenarios and various levels of liquidity stress. Sources of liquidity risk include:

- Insurance underwriting e.g. unexpected catastrophe claims arising from adverse weather events;
- Variances of actual operational cash flow from shorter-term forecasts; and
- Timing mismatches between claims payments, premium income and reinsurance recoveries.

The principal bases used to measure and assess the Company's exposure to liquidity risk are absolute liquidity coverage relative to pre-defined appetites and the quantum of certain liquid assets. These are calibrated to ensure sufficient liquidity to meet expected liquidity requirements following an extreme liquidity-specific stress events covering both short-term and long-term stress scenarios.

There has been no material change to the measures used to assess liquidity risk during the reporting period.

There were no material changes in the Company's exposure to liquidity risk throughout the year and the Company's liquidity profile was maintained within appetite.

C.4.2 Risk concentration

The credit limit framework described in section C.3.1 above also avoids concentrations of liquidity risk by preventing investment in a restricted number of issuers, asset classes and sectors. The Company's investment strategy ensures it has sufficient liquid funds to meet its expected obligations as they fall due.

C.4.3 Risk mitigation

The Company manages its liquidity risk by considering the liquidity impact before accepting new risks and managing its existing liquidity profile by:

- Monitoring of projected short-term cash flow needs;
- Setting liquidity risk appetites which require that sufficient liquid resources be maintained to cover net outflows in a stress scenario over a range of timeframes;
- Defining trigger levels that enable action to be taken before those levels are breached; and
- Its parent, AIL, maintaining a liquidity risk management plan which details management actions to address liquidity funding requirements in a significant stress scenario that includes consideration of the Company.

The Company monitors the effectiveness of liquidity risk mitigation techniques as follows:

- The internal controls that enable effective liquidity risk management are subject to assurance testing as part of wider testing undertaken within AIL to ensure they operate effectively; and
- Liquidity positions are regularly reported to and monitored by the Board against pre-defined trigger points to enable appropriate oversight and actions to take place if effectiveness deteriorates.

C.4.4 Expected Profit Included Future Premiums (EPIFP)

The amount of EPIFP, calculated in accordance with Article 1 of the SII regulations and included within the valuation of the Company's Technical Provisions as at 31 December 2017 is £nil *(2016: £nil)*. (See the Own Funds QRT S.23.01.01, Appendix F.1.6.)

C.4.5 Stress and scenario testing and sensitivity analysis

Descriptions of the methods used, assumptions made and outcomes of stress and scenario testing and sensitivity analysis are provided in section C.7.1.

C.5. Operational Risk

C.5.1 Exposure

The Company's exposure to operational risk arises from the risk of direct or indirect loss, caused by inadequate or failed internal processes, people and systems, or external events including changes in the regulatory environment. The Company has a limited appetite for operational risk and aims to reduce these risks as far as commercially sensible.

Conduct risk, an element of operational risk, is where the Company does not achieve positive or fair customer outcomes. Management of conduct risk was a key priority for the Company across the whole lifecycle of its products and throughout the end to end journey of its customers in 2017 with robust governance and metrics embedded across the organisation.

The Company also seeks to manage its exposure to reputational risk, which is the risk of loss to the Company's franchise value from damage caused to the Company's brands or reputation. Examples of factors, regardless of whether authenticated or not, which could damage the Company's brands or reputation include litigation, employee misconduct, operational failures, the outcome of regulatory investigations, media speculation and negative publicity, disclosure of confidential client information or inadequate services.

As part of the wider Group strategy of digital customer interaction, its use of advanced data analytics and the increasing cyber security threat, together with regulators' attention to conduct issues, the Company has increased its inherent exposure to risks such as data theft, conduct breaches and customer service interruption arising from IT systems failure. The Company and its parent has sought to contain and reduce exposure to these risks through on-going investment in programmes to improve IT security and resilience, disaster recovery, data governance and outsourcing risk. The Company has also implemented the new Group Operational Risk and Control Management Framework, which better integrates the results of the risk identification and assurance activities carried out across the Company's three lines of defence.

Operational risks are initially identified and assessed against implemented controls. Residual risk, outside tolerance, is given prioritised management action to reduce it within tolerance. Operational risk is quantitatively assessed on the basis of financial loss and misstatement. Potential reputational and conduct impacts are qualitatively assessed. There has been no material change to the measures used to assess operational risk during the reporting period.

The Company holds economic capital, based on the SII SCR, against residual operational risk, to the extent that it cannot be eliminated by management action. QRT S.25.01 (Appendix F.1.7) shows that the Company's undiversified SCR for operational risk is £1m *(2016: £2m)*. The Company also produces specific conduct risk management information used to measure and analyse its exposure to conduct risk.

The have been no material changes, during the year, to the Company's exposure to operational risk.

C.5.2 Risk Concentration

The Company's products are sold under the 'Barclays' brand, enabling leverage on the strength of that brand and supporting delivery of the Company's business strategy. Whilst reputational risk is mostly borne by the Barclays brand, the Company is vulnerable to any operational failures that adversely impact public perception of the 'Barclays' brand.

C.5.3 Risk mitigation

Operational risks are considered by the Company to be preventable and are managed through business controls. The Company's operational risk strategy is to improve its business processes to:

- Reduce operational risk and associated losses, thereby improving cost to income ratio and variability in financial performance;
- Improve customer outcomes and employee satisfaction; and
- Sustain customer confidence and a positive regulatory reputation.

The Company's business standards set out the minimum control objectives and controls that each business area is required to operate. Operational risk tolerances are quantitative boundaries that constrain specific risk-taking activities at an operational level.

The Company records and analyses operational risk events to ensure remedial action is taken, lessons are learnt and, if the event impacts customers, they are treated fairly. This includes risk events that do not give rise to a financial loss, such as near misses or fortuitous gains. This assessment enables the Company to highlight areas for improvement, implement corrective actions to avoid recurrence, and improve its understanding of operational risk.

The Company has identified business critical functions and has exit and termination plans and business continuity and disaster recovery plans in the event of supplier failure. These plans are reviewed at least annually.

The Company's three lines of defence all monitor the effectiveness of the controls that are in place against operational risk. Further details of the three lines of defence are included in section B.1.1, including the specific roles and responsibilities of each line. Operational risk is overseen by the Board.

C.5.4 Stress and scenario testing and sensitivity analysis

Descriptions of the methods used, assumptions made and outcomes of stress and scenario testing and sensitivity analysis is provided in section C.7.1

C.6 Other Material Risks

The Company has no material information to disclose regarding other material risks.

C.7 Any Other Information

C.7.1 Stress and scenario testing and sensitivity analysis

Stress and Scenario Testing (SST) in relation to the Company is an element of the wider Risk Management Framework, providing insight into key risk exposures and dependencies of the Company; considering resilience of potential changes to these exposures and dependencies; and anticipating a range of possible outcomes. The evaluation of the potential impacts on the Company's SII capital and liquidity positions enables the Company to identify and prepare for appropriate ways to mitigate and manage the realisation of such impacts.

The Company carries out a range of sensitivity tests (where one risk factor, such as interest rates, is assumed to vary) and scenario tests (where combinations of risk factors are assumed to vary) to evaluate their impact on the business and to enable identification of plausible management actions to mitigate such impacts.

C.7.1.1 Stress and scenario testing

A range of SST are considered as part of the Company's Plan, with the results of these demonstrating that, after consideration of any management actions that may be required to restore surplus in extreme scenarios, the Company retains a SII surplus post a stress. The stress and scenario tests performed by the Company, have considered potential impacts including the most significant risks to the Company of counterparty credit risk (arising from both the quota share arrangement in place with its parent company and the participation in the Group catastrophe reinsurance programme) and operational risks (arising from outsourcing operations and internal failings).

A range of assumptions are made in the development of SST and the measurement of resilience to such events. These assumptions are defined by suitable experts and, where applicable, by the PRA.

C.7.1.2 Sensitivity analysis

Management use the sensitivity analyses to assess a range of potential single factor standalone impacts of differing levels of severity on the capital and liquidity positions of the Company and to ensure that the Company has a sufficient range of plausible management actions that could be executed in a timely manner to mitigate the potential impacts.

The SCR is the primary basis used by the Company to measure and assess its risks. The sensitivity analysis performed by the Company includes consideration of the sensitivity of its SCR cover ratio to a range of economic assumptions. For the Company, this includes consideration of impacts from changes in interest rates and changes in reinsurer ratings. The results of these analyses demonstrate that, after consideration of any management actions that may be required to restore surplus in extreme scenarios, the Company retains a SII surplus. This limited impact is primarily driven by the asset holdings, which are predominately Government Bonds and Collective Investment Undertakings with holdings in liquid funds and the extensive reinsurance arrangements in place.

C.7.2 Prudent Person Principle

The Company ensures that its assets are invested in accordance with the prudent person principle as set out in Article 132 of the SII Directive (Directive 2009/138/EC) through the collective application of its risk policies and business standards. These ensure that the Company invests in assets whose risks it can properly identify, measure, monitor, manage, control and report, and appropriately take into account in the assessment of its overall solvency needs having regard to the term and nature of its liabilities. The Company's Asset Liability Management Business Standard and certain provisions of the Investment Management Business Standard contain mandatory requirements to ensure that the Company develops its own set of key risk indicators and takes into account the risks associated with its investments without relying only on the risk being adequately captured by the capital requirements. Given the relatively small value of the Company's retained liabilities, it achieves this by investing in low-risk, short term Government Bonds and Collective Investment Undertakings with holdings in liquid funds.

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D. Valuation for Solvency Purposes

In this chapter

D.1 Assets

D.2 Technical Provisions

D.3 Other Liabilities

D.4 Alternative Methods of Valuation

D.5 Any Other Information

D. Valuation for Solvency Purposes

The 'Valuation for Solvency Purposes' section of the report provides a description of the bases, methods and main assumptions used in the valuation of assets, Technical Provisions and other liabilities for each material asset and liability class.

The Company's IFRS balance sheet is presented in column (b) of the following table, in accordance with the classification of assets and liabilities used in its financial statements. The references given in column (a) are to relevant accounting policies and notes provided in the financial statements.

A number of reclassifications, required to align the Company's IFRS balance sheet as shown in its financial statements, to the classifications required for the prescribed format of the SII balance sheet QRT, are given in column (c). The most significant reclassifications are:

- Under the SII requirements, cash flows relating to reinsurance premium are included within Reinsurance Recoverables, and cash flows relating to premium and policyholder tax are included within Technical Provisions. In the IFRS balance sheet these amounts are included within reinsurance payables, insurance and intermediaries receivables and other liabilities respectively;
- Amounts payable to Group companies under IFRS, are reclassified within the SII balance sheet to the relevant underlying nature of the balance; and
- Investments including cash equivalents are reclassified under SII.

The Company's assets and liabilities, as valued under IFRS and in line with SII requirements are shown in column (d). The Company's SII balance sheet is summarised in column (e) and detailed in the balance sheet QRT S.02.01 included in Appendix F.1.1. Differences between the valuation of the Company's assets and liabilities under SII and IFRS are presented in column (f).

Where the valuation of assets and liabilities is the same under IFRS and SII, a description of the bases, methods and main assumptions can be found in the accounting policies and notes of the Company's financial statements. If the valuation is materially different, a description of the bases methods and main assumptions used under SII is given in Sections D.1, D2.1 and D.3.

Assets and other liabilities have been valued, according to the requirements of the SII regulations, at the amount for which they could be exchanged between knowledgeable willing parties in an arm's length transaction. The value of other liabilities is not adjusted to take account of the impact of changes in own credit standing of the Company. The valuation of Technical Provisions is detailed in Section D.2.1.

The Company applied the following hierarchy of valuation approaches:

1. Quoted market prices in active markets for the same assets or liabilities;
2. Quoted market prices in active markets for similar assets and liabilities (with adjustments to reflect differences where necessary); and
3. Alternative methods of valuation.

The criteria to determine whether a market is active are consistent with IFRS 13: Fair Value Measurement. An "Active market" under IFRS is defined as a market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. The assets, classified as Level 1 and Level 2 under IFRS 13: Fair Value Measurement, are deemed as market consistent under SII. The assets classified as Level 3, for which there is no active market, are considered to use alternative valuation methods under SII. The Company has not used any alternative methods of valuation.

Balance Sheet – IFRS and SII

As at 31 December 2017 £m	Note in financial statements (a)	IFRS balance sheet classified according to financial statements (b)	Reclassification of IFRS balances to SII balance sheet categories (c)	Reclassified IFRS balance sheet (d) =(b)+(c))	SII balance sheet (e)	Valuation differences between SII and IFRS (f) =(e)-(d)
Deferred acquisition costs (DAC)	N & 12	22	-	22	-	(22)
Financial investments						
Government Bonds	K & 9	64	-	64	64	-
Collective investment undertakings		-	61	61	61	-
Reinsurance recoverables	I & 10	110	(80)	30	(1)	(31)
Receivables						
Insurance and intermediaries	L & 11	79	(79)	-	-	-
Reinsurance	L & 11	3	-	3	3	-
Cash and cash equivalents	O & 20	61	(61)	-	-	-
Prepayments and accrued income		3	-	3	3	-
Assets		342	(159)	183	130	(53)
Technical Provisions	H & 13	(110)	74	(36)	(5)	31
Payables and other financial liabilities						
Debts owed to credit institutions		(1)	1	-	-	-
Insurance and intermediaries payable	M & 15	(1)	(2)	(3)	(3)	-
Reinsurance payables	M & 15	(80)	80	-	-	-
Payables trade not insurance	M & 15	(11)	(12)	(23)	(23)	-
Amounts due to Group Companies	M & 15	(21)	21	-	-	-
Other liabilities						
Current tax liabilities	Q & 14	(1)	1	-	-	-
Accruals	16	(29)	29	-	-	-
Reinsurers share of DAC	N & 16	(22)	-	(22)	-	22
Other liabilities		-	(33)	(33)	(32)	1
Liabilities		(276)	159	(117)	(63)	54
Excess of assets over liabilities		66	-	66	67	1

D.1 Assets

Assets have been valued according to the requirements of the SII Directive and related guidance. The basis of the SII valuation principle is the amount for which they could be exchanged between knowledgeable willing parties in an arm's length transaction. A description of the basis of valuation under SII along with valuation differences between the SII bases and the IFRS financial statements, by asset class, is provided below; if the valuation method has been described in the financial statements it has not been included in this section.

D.1.1 Deferred acquisition costs

Deferred acquisition costs are recognised under IFRS reporting and deferred to the extent they are expected to be recoverable out of future margins in revenues on related contracts. Under SII these are not recognised and are therefore valued at £nil in the SII balance sheet. The associated cash flows are included in the valuation of SII Technical Provisions.

D.1.2 Collective investment undertakings

The Company's collective investment undertakings are all invested in highly liquid investments that are readily convertible into cash and valued on the basis of the liquid investments they hold. The Company's collective investment undertakings are subject to an insignificant risk of change in value.

D.1.3 Reinsurance recoverables

Reinsurance recoverables are calculated as the probability-weighted average of discounted future cash flows relating to reinsurance contracts, adjusted for the expected losses due to counterparty default. Although established separately, reinsurance recoverables are valued on the same basis and using the same methodology and assumptions used to derive Technical Provisions - Best Estimate Liabilities, as described in Section D.2.1, subject to the following:

- Internal expenses are only allowed if they are recoverable under the reinsurance agreement;
- Where the timing of recoveries diverges from that for payments a separate projection is used;
- Allowance for risk of default depends on the credit rating and exposure to the reinsurance counterparty; and
- Reinsurance assets take into account reinsurance commissions.

Reinsurance recoverables, consistent with the calculation of Technical Provisions - Best Estimate Liabilities, includes expected recoveries from pre-inception contracts where they occur within the premium or claims provisions.

Cash flows relating to future reinsurance arrangements comprise both expected recoveries and expected reinsurance premium payments. This means reinsurance contracts which are expected to be written are taken into account and thus assumptions in relation to the likely future reinsurance purchasing decisions are required.

The Company has a significant exposure to its parent company, AIL, arising from the quota share reinsurance agreement. Further details are set out in Section C.3.1.

The material differences between the SII and IFRS valuation bases for reinsurance recoveries are as follows:

- Only reinsurance cash flows relating to long tailed (predominantly PPO) claims reserves are discounted under IFRS whereas all reinsurance cash flows are discounted under SII;
- The rate used to discount PPO cash flows is lower under SII than the equivalent rate used under IFRS;
- The unearned reinsurance premium reserve established under IFRS is replaced with a lower Best Estimate reinsurance premium provision, but the impact of this is offset by the release of deferred reinsurance commissions from other liabilities (see section D.3.2); and
- The SII valuation takes into account the additional reinsurance premium that is expected to be paid for reinsurance to cover business incepted at the valuation date. This is not accounted for under IFRS.

The Company does not have any Special Purpose Vehicles.

D.1.4 Prepayments

Prepayments are classified as Other Assets on the SII Balance Sheet. Prepayments are valued at their fair value, which is considered to be the same as their cost.

D.1.5 Changes made to recognition and valuation bases and estimations during the reporting period

There were no changes made to the recognition and valuation bases used or to estimations during the reporting period.

D.2 Technical Provisions

This section provides a definition of SII Technical Provisions, the methodology and main assumptions used in the valuation of the SII Technical Provisions, the total value of SII Technical Provisions split by material lines of business, a comparison of the valuation of SII Technical Provisions with IFRS Technical Provisions and a description of the level of uncertainty in Technical Provisions.

D.2.1 Valuation of Technical Provisions

SII Technical Provisions are summarised in the following table. They are also detailed in the QRT S.17.01 (Non-life Technical Provisions) and S.12.01 (Life Technical Provisions), see Appendix F.1.3.

As at 31 December 2017	Best Estimate Liabilities	Risk Margin	Technical provisions
Line of Business			
Motor vehicle liability	1	-	1
Fire and property damage	(6)	-	(6)
General liability insurance	3	-	3
Non-life insurance obligations	(2)	-	(2)
PPOs other than health insurance	7	-	7
Life insurance obligations	7	-	7
Total	5	-	5

Whilst the Company only conducts non-life insurance activities, it also has life insurance obligations in the UK in relation to annuities stemming from non-life insurance contracts (PPO). PPO are classified as Technical Provisions - Life (excluding health and index-linked and unit-linked), within the prescribed format of the SII Balance Sheet.

An explanation of the differences between the SII valuation of Technical Provisions and there valuation in the Company's financial statements under IFRS is given in section D.2.3.

D.2.1.1 Non-life Best Estimate Liabilities

The following general principles apply to the valuation of Best Estimate Liabilities for all the Company's non-life business.

- A Best Estimate is one that represents the expected outcome from the range of possible outcomes for the future and is reasonable and realistic taking account of all the uncertainties involved.
- A consistent approach has been applied across all non-life business.
- The calculation of Technical Provisions is performed on a going concern basis. This means that it can be assumed that contracts run to their conclusion and as a result a proportion of expected future costs will be covered by future business.

The Company's Best Estimate Liabilities are valued based on the present value of future cash flows discounted using relevant risk-free interest rates adjusted for the EIOPA prescribed credit risk adjustment and Volatility Adjustment at the valuation date. The cash flows that are considered when calculating the Best Estimate Liabilities derive from:

- In-force and expired contracts;
- Contracts that have not yet incepted but that the Company has an obligation to enter into at the valuation date (pre-inception contracts); and
- Future cancellations or endorsements by the policyholder.

Best Estimate Liabilities comprise a claims provision and a premium provision. The claims provision includes cash flows relating to events that occurred before the valuation date, whether reported or not. The cash flows include premiums, net claims costs and expenses. The premium provision includes cash flows relating to future claim events that have not yet occurred, but that are covered by existing contracts and legally binding pre-inception contracts. The cash flows include premiums, net claims and expenses, in respect of future claim events. Where future premium cash flows are expected to exceed projected future claim and expense cash flows, the premium provision is negative, as is the case for Fire and Other Damage to Property.

When modelling these cash flows the inflows are considered separately from the outflows. Claims costs take into account recoveries from salvage and subrogation. Expenses include administrative, investment management, loss adjustment and acquisition expenses including commissions and premium taxes.

Claims costs

The ultimate cost of outstanding claims is estimated using a range of standard actuarial claims projection techniques. The main assumption underlying these techniques is that the Company's past claims experience can be used as a basis to project future claims. Therefore these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years. The estimation of ultimate claims costs is done at the level of homogenous risk groups. These groups are mapped to SII lines of business.

Qualitative judgement is used to reflect changes in external factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy conditions and claims handling procedures.

Premium provisions

Premium provisions are estimated by selecting an exposure measure and using that to establish the unearned and pre-inception exposure. Claims cost projections are set for each future period using trends in historic claims data adjusted for known anomalies in the data that are not expected to be repeated in the future, changes in mix and volume of business and to allow for the impact of projected claims inflation. These cost projections are then applied to the predicted exposure to determine the cash flows.

Expenses

Expenses are adjusted for expense and claims inflation and allocated between the claims and premium provisions. They are analysed by homogenous risk group or at a minimum by SII line of business. Future administrative costs and commission payments are projected using Best Estimate expense forecasts. Investment expenses are modelled as a percentage of Technical Provisions. Future unallocated loss adjustment expense provisions are set in relation to expected claims levels.

Events not In Data (ENID)

ENID are events not deemed to be captured by the data which need to be separately allowed for within the Best Estimate calculations to take appropriate account of uncertainty. Two types of ENID are considered: "known unknowns", which are possible future scenarios that can be anticipated and "unknown unknowns", which are future scenarios that are completely unexpected. No allowance is made for "unknown unknowns" as by definition, they cannot be known or quantified.

Allowances for "known unknowns" are made using scenario analysis to cover any foreseeable event with a potentially material impact. A core list of events is specified which is considered as the starting point for the analysis. ENID are considered both at SII lines of business level, and at portfolio level with allocations to SII lines of business, depending on the scenario being considered.

Discounting

All cash flows are discounted using the appropriate SII yield curve in the relevant currency. The yield curve is based on the risk free rate at the valuation date and is adjusted for the EIOPA prescribed credit risk adjustment and Volatility Adjustment. Payments are assumed to occur either mid-month or mid-year. Cash flows are modelled in monthly time intervals for the first 10 years and annually thereafter.

Future management actions

There are no future management actions assumed in the calculation of the Company's gross of reinsurance Best Estimate Liabilities as at 31 December 2017.

D.2.1.2 PPO Best Estimate Liabilities

The Company's Best Estimate Liabilities for PPO, in common with non-Life business, are valued based on the present value of future cash flows discounted using relevant risk-free interest rate adjusted for the EIOPA prescribed credit risk adjustment and Volatility Adjustment at the valuation date. The cash flows that are considered when calculating the Best Estimate Liabilities for PPO derive from:

- Payment of claims benefits: relating to the future care needs of the claimant; and
- Expenses: there are relatively small (compared to the size of claims benefits) administrative costs in relation to each PPO.

PPO Best Estimate liabilities use life insurance actuarial methods and techniques to estimate appropriate assumptions for each individual claimant.

Discounting

PPO cash flows are discounted using the appropriate SII yield curve adjusted for the EIOPA prescribed credit risk adjustment and Volatility Adjustment. The methods are consistent with those applied to non-life cash flows.

Longevity assumptions

Assumptions are made in relation to the future longevity of each PPO. These assumptions are based on the latest, general mortality assumptions for the population as a whole (including future expected changes in mortality), as well as any impairment to life expectancy on individual PPO based on independent medical opinions.

Inflation assumptions

PPO payments escalate based on indices specified at the time of settlement of the PPO. The majority of PPO claims escalate based on an Annual Survey of Hours and Earnings index (ASHE) with a smaller number escalating in line with the Retail Prices Index (RPI). The small number of PPO claims the Company has escalate at the ASHE index. Assumptions are therefore required for the future escalation of this index. The Company assumes that, over the longer term, the future escalation of the ASHE indices will be linked to RPI within the UK economy and uses market consistent views of future RPI inflation as the basis to project future ASHE inflation. Adjustments are then made to allow for expected differences between future ASHE inflation and future RPI inflation.

D.2.1.3 Risk Margin

The Risk Margin is an estimate of the amount, in addition to the Best Estimate Liability, that a third party would expect to receive in order to assume ownership of the Company's insurance obligations. The Risk Margin calculation takes material underwriting, non hedgeable market (except interest rate), credit and operational risk into account. Once calculated it is allocated to each SII line of business, although on materiality grounds some SII lines of business are allocated no Risk Margin.

The Company's Risk Margin is less than £1m as at 31 December 2017.

D.2.1.4 Simplifications

In some areas of the calculation of the SII Best Estimate Liabilities, simplified methods have been used. The simplifications used have been assessed and have no material impact on the value of SII Best Estimate Liabilities. Where simplified methods are used, these are documented and justified in the Company's reserving reports and documentation. The main simplifications within the calculation of SII Best Estimate Liabilities are:

- The Company's Best Estimate Liabilities include a provision in relation to ENIDs. For the purposes of discounting cashflows, it is assumed that ENIDs have the same cashflow profile as other claims.
- Cashflows are modelled in monthly time intervals for the first 10 years and annually thereafter. For the purposes of discounting, all payments are assumed to occur mid-month or mid-year as dictated by the time intervals used.
- When calculating provisions for potential reinsurer default, reinsurance assets are grouped by reinsurer counterparty credit rating and within each credit rating the same probabilities of default are assumed.
- Gross premium debtors are split by class of business and payment date based on the split of written premium.
- The volume of Legally Obliged Unincepted business has been estimated based on a proportion of January's planned written premium.

D.2.1.5 Material changes in the relevant assumptions compared to the previous reporting period

There were no material changes in the relevant assumptions made in the calculation of technical provisions compared to the previous reporting period.

D.2.2 Level of uncertainty

The actual cost of settling insurance obligations may differ from the Best Estimate Liabilities because experience may be better or worse than assumed or future claims inflation may differ from that expected. There are a number of potential developments that would have a material adverse impact on the Best Estimate Liabilities value including:

- Catastrophic weather events;
- Unanticipated legislative changes; and
- Unanticipated inflation.

Specific areas of uncertainty are:

- Given the nature of the Company's business, on a gross of reinsurance basis the uncertainty around future weather claims experience is the largest risk the Company is exposed to. The Company has extensive reinsurance in place against these claims so net of reinsurance the level of uncertainty is reduced.
- PPOs represent one of the most uncertain elements of the Company's Technical Provisions due to their long-tailed nature and the sensitivity to changes in economic-related assumptions. Additional uncertainty arises due to potential differences in the life expectancy of claimants compared to that assumed. Gross of reinsurance the level of uncertainty within the Technical Provisions for PPO is very high. The Company purchases reinsurance to mitigate longevity risk in relation to these claims, which materially reduces the level of uncertainty.

D.2.3 Material differences between the SII and IFRS valuation bases

The following table summarises gross of reinsurance SII Technical Provisions by material line of business and compares these to IFRS reclassified Technical Provisions.

Technical Provisions as at 31 December 2017 (Asset)/Liability £m	Best estimate liability (BEL)	Risk margin (RM)	SII Technical Provisions (BEL+RM)	IFRS reclassified Technical Provisions	Difference between SII and IFRS reclassified Technical Provisions
Non-life (excluding health)	(2)	-	(2)	29	31
- Motor vehicle liability	1	-	1	1	-
- Fire and property damage	(6)	-	(6)	25	31
- General liability insurance	3	-	3	3	-
Life (excluding health and index-linked and unit-linked) (PPO)	7	-	7	7	-
Total	5	-	5	36	31

The material differences between the SII and IFRS valuation bases are:

- The unearned premium reserve established under IFRS is replaced with a Best Estimate premium provision which incorporates the expected cost of claims and expenses on the unearned periods of exposure. This leads to a lower premium provision under SII than the equivalent unearned premium reserves under IFRS and is the most material difference between SII and IFRS Technical Provisions in the table above. This difference has a material impact on the Fire and property damage line of business, but immaterial impacts on the other lines of business;
- Only PPO claims are discounted within IFRS provisions, whereas all cash flows are discounted under SII. This difference reduces SII Technical Provisions compared to IFRS provisions and affects all Non-life (excluding health) lines of business;

- An explicit margin for uncertainty is included within IFRS provisions but removed under SII. This impacts all lines of business and reduces SII Technical Provisions compared to IFRS provisions;
- Under SII, provisions are established for Legally Obliged Unincepted Business, whereas these provisions are not included within the IFRS valuation basis. This difference mainly impacts the Fire and property damage line of business. This decreases SII Technical Provisions compared to IFRS provisions.

D.2.4 Volatility Adjustment

The Volatility Adjustment removes temporary distortions in spreads caused by illiquidity in the market or extreme widening of credit spreads, in particular in relation to government bonds. The PRA has approved the Company's application to apply a Volatility Adjustment (PRA reference number: 2191491). The impact of the Volatility Adjustment on Technical Provisions, Basic Own Funds, Eligible Own Funds to meet the SCR, the SCR, Eligible Own Funds to meet the Minimum Capital Requirement (MCR) and the MCR is detailed in the Long Term Guarantees and Transitional measures QRT S.22.01 (see Appendix F.1.5). The impact of removing the Volatility Adjustment from gross Technical Provisions would be to increase their value by less than £1m.

D.2.5 Other reliefs

No transitional provisions have been applied in the calculation of Technical Provisions.

D.3 Other Liabilities

Other liabilities have been valued according to the requirements of the SII Directive and related guidance; the basis of the SII valuation principle is the amount for which they could be exchanged between knowledgeable willing parties in an arm's length transaction. A description of the basis of valuation under SII along with valuation differences between the SII bases and the IFRS financial statements, by material class, is provided below; if the valuation method has been described in the financial statements it has not been included in this section.

The Company's financial statements provide information about contingent liabilities and other risk factors in note 19. The Company has no additional material contingent liabilities to recognise under SII.

D.3.1. Reinsurers share of deferred acquisition costs

Reinsurers' share of deferred acquisition costs of £22m, included within other liabilities under IFRS, are not recognised and therefore valued at £nil in the SII balance sheet.

D.3.2 Other liabilities

Other Liabilities comprise accruals and cash flows payable under the quota share arrangement. Other liabilities expected to be settled within one year are valued, on the SII balance sheet, at the amount expected to be paid. Non-current accruals and other liabilities are valued at their fair value, and are not adjusted to take account of the impact of changes in the own credit standing of the Company. In valuing such liabilities, the timing and monetary amount of expected outflow of cash or other resources are determined and these projected cash flows discounted.

Deferred income of £1m, included within other liabilities under IFRS, is not recognised and therefore valued at £nil in the SII balance sheet.

D.3.3 Assumptions, judgments and level of uncertainty

No material assumptions or judgements were applied to, nor is any material uncertainty associated with, the recognition and valuation of other liabilities.

D.3.4 Changes made to recognition and valuation bases and estimations during the reporting period

There were no changes made to the recognition and valuation bases used or to estimations during the reporting period.

D.4 Alternative Methods of Valuation

The Company's has not used any alternative methods of valuation.

D.5 Any Other Information

The Company has no other material information to disclose.

Gresham Insurance Company Limited

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E. Capital Management

In this chapter

E.1 Own Funds

E.2 Solvency Capital Requirement and Minimum Capital Requirement

E.3 Use of Duration-Based Equity Risk Sub-Module in the Calculation of the Solvency Capital Requirement

E.4 Difference between the Standard Formula and any Internal Model Used

E.5 Non-Compliance with the Minimum Capital Requirement and Non-Compliance with the Solvency Capital Requirement

E.6 Any Other Information

E. Capital Management

This section of the report describes the internal operational structures and procedures underlying the Company's capital management process covering structure and quality of Own Funds; SCR and MCR; methodology for calculation of the SCR and any other material information.

E.1 Own Funds

E.1.1 Management of Own Funds

The Company's policy on capital and risk management is set out in its Risk Management Framework. The Company's capital and risk management objectives are closely interlinked and support earnings growth and dividend policy, whilst also recognising the critical importance of protecting policyholder and other stakeholder interests. The Company's primary objective of managing capital efficiently is to optimise the balance between return and risk, whilst maintaining economic and regulatory capital surplus in accordance with approved risk appetites.

In managing its Own Funds the Company also seeks to:

- Match the profile of its assets and liabilities, taking account of the risks inherent in the business;
- Maintain sufficient, but not excessive, financial strength to support new business growth and satisfy the requirements of its policyholders and its regulator, the PRA;
- Retain financial flexibility by maintaining sufficient liquidity; and
- Allocate capital efficiently, applying it to support value adding growth and repatriating excess capital to its shareholder through dividends.

Own Funds are monitored via forecasts over a three year planning horizon. A number of tests are used to enable the Company to understand the volatility of its earnings and capital requirement, and therefore manage its capital more efficiently.

There have been no material changes to the objectives, policies or processes of the Company for managing its Own Funds during the year.

E.1.2 Eligible Own Funds

An analysis of the Company's Own Funds by tier is presented in the Own Funds QRT S.23.01, (see Appendix F.1.6), and summarised below.

As at 31 December	Total £m 2017	Tier 1 (unrestricted) £m 2017	*Total £m 2016*	*Tier 1 (unrestricted) £m 2016*
Ordinary share capital	61	61	*61*	*61*
Reconciliation reserve	6	6	*19*	*19*
Total Basic Own Funds	67	67	*80*	*80*

Tiering analysis

The Company's ordinary share capital and reconciliation reserve are available to absorb losses and have the Tier 1 features of permanence and subordination. As the Company's Articles of Association do not contain any restriction on the right of the Company to cancel dividends or other distributions at any time before they are paid, the Company's ordinary share capital is classified as unrestricted Tier 1.

The Company's Tier 1 Own Funds of £67m *(2016: £80m)* decreased by £13m during the year. This reduction is driven by an interim dividend paid during the year of £15m *(2016: £nil)* partly offset by capital generated by the Company's operations during the year.

Reconciliation reserve

The Company's capital comprises ordinary share capital and retained earnings. However, retained earnings are not separately disclosed in Own Funds. They are notionally included in the reconciliation reserve, which reconciles the total excess of assets over liabilities with identifiable capital instruments included in Own Funds.

The table below sets out the constituent parts of the reconciliation reserve:

As at 31 December	£m 2017	*£m 2016*
SII excess of assets over liabilities	67	*80*
Ordinary share capital	(61)	*(61)*
Reconciliation reserve	6	*19*

Eligibility of tiered Capital

The eligibility of tiered Capital, to cover the SCR and MCR depends upon the tiering shown above and a number of quantitative limits. The Company's Own Funds satisfy all limits applicable to the SCR and MCR and therefore the eligibility of the Company's capital to cover the SCR and MCR is unrestricted, as shown in the table below.

As at 31 December	£m 2017	*£m 2016*
Total eligible Own Funds to meet the SCR	67	*80*
Total eligible Own Funds to meet the MCR	67	*80*

The ratio of eligible Own Funds to the SCR and the MCR is detailed below.

As at 31 December	2017	*2016*
Ratio of eligible Own Funds to the SCR	1,338%	*1,175%*
Ratio of eligible Own Funds to the MCR	2,046%	*2,390%*

E.1.3 Material differences between equity on an IFRS basis and Own Funds

At 31 December 2017 the Company's Own Funds are equal to its excess of assets over liabilities on a SII basis. The excess of £67m is £1m more than the Company's total equity on an IFRS basis. The following table details the material differences between the excess of assets over liabilities on a SII basis and total equity on an IFRS basis.

As at 31 December 2017	£m	£m	See Section
Total equity on an IFRS basis		66	
Elimination of deferred acquisition costs	(22)		D.1.1
Valuation adjustments to reinsurance recoverables	(31)		D.1.3
Valuation adjustments to Technical Provisions	31		D.2.3
Reinsurers share of deferred acquisition costs	22		D.3.1
Elimination of deferred income	1		D.3.2
		1	
Excess of assets over liabilities on a SII basis		67	

E.1.4 Transitional arrangements and restrictions

The Company's Own Funds are unrestricted and fully transferable.

E.2 Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR)

E.2.1 The amount of the SCR and MCR

The Company's SCR as at 31 December 2017 was £5m *(2016: £7m)*. This is shown in the SCR QRT, S.25.01, see Appendix F.1.7. The final amount of the SCR is subject to supervisory assessment and does not include any regulator-imposed capital add-ons. The Company's MCR as at 31 December 2017 was £3m *(2016: £3m)*. This is shown on the MCR QRT, S.28.01, see Appendix F.1.8.

E.2.2 The composition of the SCR

The Company determines its SCR using SF. An analysis by risk module is presented in the table below. Further detail is shown in the SCR QRT, see Appendix F.1.7.

Diversified SCR by risk component (per the SCR QRT)	£m	*£m*
As at 31 December	2017	*2016*
Market risk	-	*1*
Counterparty default risk	4	*5*
Diversification between risk categories	-	*(1)*
Basic SCR	4	*5*
Operational risk	1	*2*
Total SCR	5	*7*

Each risk module includes the impact of diversification within that module. The diversification benefit presented in the table above of less than £1m *(2016: £1m)* therefore only includes the benefit of diversification between risk modules.

The SCR reduction was mainly driven by reductions in market risk and counterparty default risk. Market risk reduced as a result of a reduction in interest rate risk, because the Company's investment in Government Bonds is now closer to maturity. This reduces the uncertainty associated with the remaining payments. Counterparty default risk reduced mainly because AIL's credit rating improved in 2017.

E 2.3 Simplifications, undertaking specific parameters and matching adjustment

The Company has not used any simplified calculations, undertaking specific parameters or a matching adjustment in the calculation of its SCR.

E.2.4 MCR Calculation

The Company's MCR is calculated by applying prescribed factors to its net written premium and its Best Estimate Liabilities. The MCR is subject to two further constraints; it must lie in the range of 25 to 45% of the Company's SCR and it cannot be less than an absolute minimum of €3.7m, converted at the exchange rate applicable at the end of October preceding the year end. The Company's MCR is the absolute minimum which is £3m following translation into GBP *(2016: £3m)*.

E.3 Use of the Duration-based Equity Risk Sub-Module in the Calculation of the Solvency Capital Requirement

The Company does not use this option.

E.4 Difference between the Standard Formula and any Internal Model Used

The Company does not use an Internal Model (IM).

E.5 Non-Compliance with the Minimum Capital Requirement and Non-Compliance with the Solvency Capital Requirement

The Company has complied continuously with both the MCR and the SCR throughout the reporting period.

E.6 Any Other Information

The Company has no other material information to disclose.

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F. Appendices

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F.1.1 S.02.01 Balance Sheet
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F.1.2.2 S.05.01 Premium claims and expenses (by line of business) [non-life]
F.1.2.3 S.05.02 Premium claims and expenses (by country) [life]
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F.1.3.1 S.12.01 Technical Provisions [life]
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F.2 Glossary of Abbreviations and Definitions
F.3 Directors' Statement
F.4 Auditors' Report

Appendix F.1.1

Annex I
S.02.01.02
Balance Sheet
Amounts in 000s

		Solvency II Value
		C0010
Assets		
Intangible assets	R0030	
Deferred tax assets	R0040	
Pension benefit surplus	R0050	
Property, plant & equipment held for own use	R0060	
Investments (other than assets held for index-linked and unit-linked contracts)	R0070	125,429
Property (other than for own use)	R0080	
Holdings in related undertakings, including participations	R0090	
Equities	R0100	
- Equities - Listed	R0110	
- Equities - Unlisted	R0120	
Bonds	R0130	64,729
- Government Bonds	R0140	64,729
- Corporate Bonds	R0150	
- Structured Notes	R0160	
- Collateralised securities	R0170	
Collective Investments Undertakings	R0180	60,700
Derivatives	R0190	
Deposits other than cash equivalents	R0200	
Other investments	R0210	
Assets held for index-linked and unit-linked contracts	R0220	
Loans & mortgages	R0230	
- Loans on policies	R0240	
- Loans & mortgages to individuals	R0250	
- Other loans & mortgages	R0260	
Reinsurance recoverables from:	R0270	-1,457
- Reinsurance recoverables - Non-life and health similiar to non-life	R0280	-7,638
- Reinsurance recoverables - Non-life excluding health	R0290	-7,638
- Reinsurance recoverables - Health similar to non-life	R0300	
- Reinsurance recoverables - Life and health similar to life, excluding health and index-linked and unit-linked	R0310	6,181
- Reinsurance recoverables - Health similar to life	R0320	
- Reinsurance recoverables - Life excluding health and index-linked and unit-linked	R0330	6,181
- Reinsurance recoverables - Life index-linked and unit-linked	R0340	
Deposits to cedants	R0350	
Insurance & intermediaries receivables	R0360	0
Reinsurance receivables	R0370	2,979
Receivables (trade, not insurance)	R0380	
Own Shares (held directly)	R0390	
Amounts due in respect of own fund items or initial fund called up but not yet paid in	R0400	
Cash and cash equivalents	R0410	49
Any other assets, not elsewhere shown	R0420	2,709
Total assets	R0500	129,709
Liabilities		
Technical provisions - Non-life	R0510	-2,052
- Technical provisions - Non-life (excluding health)	R0520	-2,052
- TP calculated as a whole - Non-life (excluding health)	R0530	
- Best Estimate - Non-life (excluding health)	R0540	-2,228
- Risk margin - Non-life (excluding health)	R0550	177
- Technical provisions - Health (similar to non-life)	R0560	
- TP calculated as a whole - Health (similar to non-life)	R0570	
- Best Estimate - Health (similar to non-life)	R0580	
- Risk margin - Health (similar to non-life)	R0590	
Technical provisions - Life (excluding index-linked and unit linked)	R0600	6,945
- Technical provisions - Health (similar to life)	R0610	
- TP calculated as a whole - Health (similar to life)	R0620	
- Best Estimate - Health (similar to life)	R0630	
- Risk margin - Health (similar to life)	R0640	
- Technical provisions - Life (excluding health and index-linked and unit-linked)	R0650	6,945
- TP calculated as a whole - Life (excl health, index-linked and unit-linked)	R0660	
- Best Estimate - Life (excl health, index-linked and unit-linked)	R0670	6,945
- Risk margin - Life (excl health, index-linked and unit-linked)	R0680	
Technical provisions - Index-linked and unit-linked	R0690	
- TP calculated as a whole - Index-linked and unit-linked	R0700	
- Best Estimate - Index-linked and unit-linked	R0710	
- Risk margin - Index-linked and unit-linked	R0720	
Contingent liabilities	R0740	
Provisions other than technical provisions	R0750	
Pension benefit obligations	R0760	
Deposits from reinsurers	R0770	
Deferred tax liabilities	R0780	64
Derivatives	R0790	
Debts owed to credit institutions	R0800	626
Financial liabilities other than debts owed to credit institutions	R0810	
Insurance & intermediaries payables	R0820	2,957
Reinsurance payables	R0830	180
Payables (trade, not insurance)	R0840	22,953
Subordinated liabilities	R0850	
- Subordinated liabilities not in BOF	R0860	
- Subordinated liabilities in BOF	R0870	
Any other liabilities, not elsewhere shown	R0880	31,527
Total liabilities	R0900	63,200
Excess of assets over liabilities	R1000	66,510

Appendix F.1.2.1

Annex I

S.05.01.02

Premiums, claims and expenses by line of business

Amounts in 000s

		Line of Business for: life insurance obligations						Life reinsurance obligations		
		Health [accepted non-proportional reinsurance]	Insurance with profit participation	Unit-linked or index-linked insurance	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance	Health reinsurance	Life reinsurance	Total
		C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0300
Premiums written										
Gross - Direct Business	R1410									
Reinsurers' share	R1420									
Net	R1500									
Premiums earned										
Gross - Direct Business	R1510									
Reinsurers' share	R1520									
Net	R1600									
Claims incurred										
Gross - Direct Business	R1610						-34			-34
Reinsurers' share	R1620						-216			-216
Net	R1700						183			183
Changes in other technical provisions										
Gross - Direct Business	R1710									
Reinsurers' share	R1720									
Net	R1800									
Expenses incurred	R1900									
Other expenses	R2500									
Total expenses	R2600									

Appendix F.1.2.2

Annex I
S.05.01.02
Premiums, claims and expenses by line of business
Amounts in 000s

		Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)											
		Medical expense insurance [direct business]	Income protection insurance [direct business]	Workers' compensation insurance [direct business]	Motor vehicle liability insurance [direct business]	Other motor insurance [direct business]	Marine, aviation and transport insurance [direct business]	Fire and other damage to property insurance [direct business]	General liability insurance [direct business]	Credit and suretyship insurance [direct business]	Legal expenses insurance [direct business]	Assistance [direct business]	Miscellaneous financial loss [direct business]
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120
Premiums written													
Gross - Direct Business	R0110							144,457	4,468				
Gross - Proportional reinsurance accepted	R0120												
Gross - Non-proportional reinsurance accepted	R0130												
Reinsurers' share	R0140							137,447	4,251				
Net	R0200							7,010	217				
Premiums earned													
Gross - Direct Business	R0210							151,605	4,689				
Gross - Proportional reinsurance accepted	R0220												
Gross - Non-proportional reinsurance accepted	R0230												
Reinsurers' share	R0240				16			144,578	4,471				
Net	R0300				-16			7,026	217				
Claims incurred													
Gross - Direct Business	R0310				-115			53,659	1,660				
Gross - Proportional reinsurance accepted	R0320												
Gross - Non-proportional reinsurance accepted	R0330												
Reinsurers' share	R0340				725			52,900	1,636				
Net	R0400				-840			759	23				
Changes in other technical provisions													
Gross - Direct Business	R0410												
Gross - Proportional reinsurance accepted	R0420												
Gross - Non-proportional reinsurance accepted	R0430												
Reinsurers' share	R0440												
Net	R0500												
Expenses incurred	R0550							6,185	191				
Other expenses	R1200												
Total expenses	R1300												

		Line of Business for: accepted non proportional reinsurance				
		Non-proportional health reinsurance	Non-proportional casualty reinsurance	Non-proportional marine, aviation and transport reinsurance	Non-proportional property reinsurance	Total
		C0130	C0140	C0150	C0160	C0200
Premiums written						
Gross - Direct Business	R0110					148,925
Gross - Proportional reinsurance accepted	R0120					
Gross - Non-proportional reinsurance accepted	R0130					
Reinsurers' share	R0140					141,698
Net	R0200					7,227
Premiums earned						
Gross - Direct Business	R0210					156,294
Gross - Proportional reinsurance accepted	R0220					
Gross - Non-proportional reinsurance accepted	R0230					
Reinsurers' share	R0240					149,066
Net	R0300					7,227
Claims incurred						
Gross - Direct Business	R0310					55,203
Gross - Proportional reinsurance accepted	R0320					
Gross - Non-proportional reinsurance accepted	R0330					
Reinsurers' share	R0340					55,261
Net	R0400					-57
Changes in other technical provisions						
Gross - Direct Business	R0410					
Gross - Proportional reinsurance accepted	R0420					
Gross - Non-proportional reinsurance accepted	R0430					
Reinsurers' share	R0440					
Net	R0500					
Expenses incurred	R0550					6,376
Other expenses	R1200					-3,414
Total expenses	R1300					2,962

Appendix F.1.2.3

Annex I

S.05.02.01

Premiums, claims and expenses by Country

Amounts in 000s

		Home Country	Top 5 countries (by amount of gross premius written) - life obligations					Total Top 5 and home country
		C0150	C0160	C0170	C0180	C0190	C0200	C0210
	R1400							
		C0220	C0230	C0240	C0250	C0260	C0270	C0280
Premiums written								
Gross	R1410							0
Reinsurers' share	R1420							0
Net	R1500							0
Premiums earned								
Gross	R1510							0
Reinsurers' share	R1520							0
Net	R1600							0
Claims incurred								
Gross	R1610	-34						-34
Reinsurers' share	R1620	-216						-216
Net	R1700	183						183
Changes in other technical provisions								
Gross	R1710							0
Reinsurers' share	R1720							0
Net	R1800							0
Expenses incurred	R1900							0
Other expenses	R2500							
Total expenses	R2600							0

Appendix F.1.2.4

Annex I

S.05.02.01

Premiums, claims and expenses by Country

Amounts in 000s

		Home Country	Top 5 countries (by amount of gross premium written) - non-life obligations					Total Top 5 and home country
		C0010	C0020	C0030	C0040	C0050	C0060	C0070
	R0010							
		C0080	C0090	C0100	C0110	C0120	C0130	C0080
Premiums written								
Gross - Direct Business	R0110	148,925						148,925
Gross - Proportional reinsurance accepted	R0120							0
Gross - Non-proportional reinsurance accepted	R0130							0
Reinsurers' share	R0140	141,698						141,698
Net	R0200	7,227						7,227
Premiums earned								
Gross - Direct Business	R0210	156,294						156,294
Gross - Proportional reinsurance accepted	R0220							0
Gross - Non-proportional reinsurance accepted	R0230							0
Reinsurers' share	R0240	149,066						149,066
Net	R0300	7,227						7,227
Claims incurred								
Gross - Direct Business	R0310	55,203						55,203
Gross - Proportional reinsurance accepted	R0320							0
Gross - Non-proportional reinsurance accepted	R0330							0
Reinsurers' share	R0340	55,261						55,261
Net	R0400	-57						-57
Changes in other technical provisions								
Gross - Direct Business	R0410							0
Gross - Proportional reinsurance accepted	R0420							0
Gross - Non-proportional reinsurance accepted	R0430							0
Reinsurers' share	R0440							0
Net	R0500							0
Expenses incurred	R0550	6,376						6,376
Other expenses	R1200							-3,414
Total expenses	R1300							2,962

Appendix F.1.3.1

Annex I
S.12.01.02
Life and Health SLT Technical Provisions
Amounts in 000s

		Insurance with profit participation	Unit-linked or index-linked insurance			Other life insurance			Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insuranc	Accepted reinsurance	Total (Life other than health insurance, incl. Unit-Linked)
				Contracts without options and guarantees	Contracts with options or guarantees		Contracts without options and guarantees	Contracts with options or guarantees			
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0150
Technical provisions calculated as a whole	R0010										
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	R0020										
Technical provisions calculated as a sum of BE and RM											
Best Estimate											
Gross Best Estimate	R0030								6,945		6,945
Total Recoverables from reinsurance and SPV after the adjustment for expected losses due to counterparty default	R0080								6,181		6,181
Best estimate minus recoverables from reinsurance and SPV - Total	R0090								763		763
Risk Margin	R0100										
Amount of the transitional on Technical Provisions											
Technical Provisions calculated as a whole	R0110										
Best estimate	R0120										
Risk margin	R0130										
Technical provisions - Total	R0200								6,945		6,945

		Health [accepted non-proportional reinsurance]			Annuities stemming from non-life insurance contracts and relating to health insurance obli	Health reinsurance	Total (Health similar to life insurance)
			Contracts without options and guarantees	Contracts with options or guarantees			
		C0160	C0170	C0180	C0190	C0200	C0210
Technical provisions calculated as a whole	R0010						
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	R0020						
Technical provisions calculated as a sum of BE and RM							
Best Estimate							
Gross Best Estimate	R0030						
Total Recoverables from reinsurance and SPV after the adjustment for expected losses due to counterparty default	R0080						
Best estimate minus recoverables from reinsurance and SPV - Total	R0090						
Risk Margin	R0100						
Amount of the transitional on Technical Provisions							
Technical Provisions calculated as a whole	R0110						
Best estimate	R0120						
Risk margin	R0130						
Technical provisions - Total	R0200						

Appendix F.1.3.2

Annex I
S.17.01.02
Non-Life Technical Provisions
Amounts in 000s

		Direct business and accepted proportional reinsurance											
		Medical expense insurance [direct business]	**Income protection insurance [direct business]**	**Workers' compensation insurance [direct business]**	**Motor vehicle liability insurance [direct business]**	**Other motor insurance [direct business]**	**Marine, aviation and transport insurance [direct business]**	**Fire and other damage to property insurance [direct business]**	**General liability insurance [direct business]**	**Credit and suretyship insurance [direct business]**	**Legal expenses insurance [direct business]**	**Assistance [direct business]**	**Miscellaneous financial loss [direct business]**
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130
Technical provisions calculated as a whole	R0010												
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	R0050												
Technical provisions calculated as a sum of BE and RM													
Best estimate													
Premium provisions													
Gross	R0060							-23,256					
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	R0140							-27,488					
Net Best Estimate of Premium Provisions	R0150							4,232					
Claims provisions													
Gross	R0160				1,121	-1		17,429	2,477				
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	R0240				1,115	-1		16,435	2,301				
Net Best Estimate of Claims Provisions	R0250				6			994	177				
Total Best estimate - Gross	R0260				1,121	-1		-5,826	2,477				
Total Best estimate - Net	R0270				6			5,227	177				
Risk margin	R0280				1	2		170	5				
Amount of the transitional on Technical Provisions													
Technical Provisions calculated as a whole	R0290												
Best estimate	R0300												
Risk margin	R0310												
Technical provisions - Total													
Technical provisions - Total	R0320				1,122	1		-5,657	2,482				
Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - Total	R0330				1,115	-1		-11,053	2,301				
Technical provisions minus recoverables from reinsurance/SPV and Finite Re - Total	R0340				7	2		5,396	181				

		Accepted non-proportional reinsurance				
		Health [accepted non-proportional reinsurance]	**Casualty [accepted non-proportional reinsurance]**	**Marine, aviation, transport [accepted non-proportional reinsurance]**	**Property [accepted non-proportional reinsurance]**	**Total Non-Life obligation**
		C0140	C0150	C0160	C0170	C0180
Technical provisions calculated as a whole	R0010					
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	R0050					
Technical provisions calculated as a sum of BE and RM						
Best estimate						
Premium provisions						
Gross	R0060					-23,256
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	R0140					-27,488
Net Best Estimate of Premium Provisions	R0150					4,232
Claims provisions						
Gross	R0160					21,028
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	R0240					19,850
Net Best Estimate of Claims Provisions	R0250					1,177
Total Best estimate - Gross	R0260					-2,228
Total Best estimate - Net	R0270					5,410
Risk margin	R0280					177
Amount of the transitional on Technical Provisions						
Technical Provisions calculated as a whole	R0290					
Best estimate	R0300					
Risk margin	R0310					
Technical provisions - Total						
Technical provisions - Total	R0320					-2,052
Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - Total	R0330					-7,638
Technical provisions minus recoverables from reinsurance/SPV and Finite Re - Total	R0340					5,586

Appendix F.1.4

Annex I
S.19.01.21
Non-Life Insurance Claims Information
Amounts in 000s

Total Non-Life Business

Accident year / Underwriting year	**Z0020**	AY

Gross Claims Paid (non-cumulative)
(absolute amount)

Development Year

		0	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10&+**
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110
Prior	R0100											409
R0160	R0160	99,335	53,405	6,140	2,724	1,901	931	404	-302	262	-30	
R0170	R0170	90,397	43,313	5,528	3,056	1,710	885	480	188	330		
R0180	R0180	70,649	62,603	7,116	1,975	1,415	1,422	112	152			
R0190	R0190	58,405	25,154	3,069	1,543	998	603	474				
R0200	R0200	63,786	29,236	2,995	1,352	681	476					
R0210	R0210	48,480	30,044	3,595	1,207	369						
R0220	R0220	50,779	21,227	2,160	1,547							
R0230	R0230	39,115	20,306	2,461								
R0240	R0240	37,651	16,481									
R0250	R0250	35,587										

		In Current year	**Sum of years (cumulative)**
		C0170	C0180
	R0100	409	648,649
	R0160	-30	164,770
	R0170	330	145,886
	R0180	152	145,445
	R0190	474	90,247
	R0200	476	98,527
	R0210	369	83,695
	R0220	1,547	75,713
	R0230	2,461	61,882
	R0240	16,481	54,132
	R0250	35,587	35,587
Total	R0260	58,257	1,604,532

Gross undiscounted Best Estimate Claims Provisions
(absolute amount)

Development Year

		0	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10&+**
		C0200	C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0290	C0300
Prior	R0100											373
R0160	R0160									356	43	
R0170	R0170								1,917	1,302		
R0180	R0180							270	69			
R0190	R0190						838	277				
R0200	R0200					1,091	414					
R0210	R0210				710	549						
R0220	R0220			1,730	745							
R0230	R0230		3,680	1,017								
R0240	R0240	12,953	3,533									
R0250	R0250	12,982										

		Year end (discounted data)
		C0360
	R0100	367
	R0160	51
	R0170	1,243
	R0180	63
	R0190	272
	R0200	409
	R0210	539
	R0220	733
	R0230	1,000
	R0240	3,473
	R0250	12,877
Total	R0260	21,028

Appendix F.1.5

Annex I

S.22.01.21

Impact of long term guarantees and transitional measures

Amounts in 000s

		Amount with LG measures and transitionals	**Impact of transitional on technical provisions**	**Impact of transitional on interest rate**	**Impact of volatility adjustment set to zero**	**Impact of matching adjustment set to zero**
		C0010	C0030	C0050	C0070	C0090
Technical Provisions	R0010	4,893			472	
Basic Own Funds	R0020	66,510				
Eligible own funds to meet Solvency Capital Requirement	R0050	66,510				
Solvency Capital Requirement	R0090	4,971				
Eligible own funds to meet Minimum Capital Requirement	R0100	66,510				
Minimum Capital Requirement	R0110	3,251				

Appendix F.1.6

Annex I
S.23.01.01
Own Funds
Amounts in 000s

		Total	Tier 1 Unrestricted	Tier 1 Restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35						
Ordinary share capital (gross of own shares)	R0010	61,400	61,400			
Share premium account related to ordinary share capital	R0030					
Initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual-type undertakings	R0040					
Subordinated mutual member accounts	R0050					
Surplus funds	R0070					
Preference shares	R0090					
Share premium account related to preference shares	R0110					
Reconciliation reserve	R0130	5,110	5,110			
Subordinated liabilities	R0140					
An amount equal to the value of net deferred tax assets	R0160					
Other own fund items approved by the supervisory authority as basic own funds not specified above	R0180					
Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds						
Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds	R0220					
Deductions						
Deductions for participations in financial and credit institutions	R0230					
Total basic own funds after deductions	R0290	**66,510**	**66,510**			
Ancillary own funds						
Unpaid and uncalled ordinary share capital callable on demand	R0300					
Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual-type undertakings, callable on demand	R0310					
Unpaid and uncalled preference shares callable on demand	R0320					
A legally binding commitment to subscribe and pay for subordinated liabilities on demand	R0330					
Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	R0340					
Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	R0350					
Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	R0360					
Supplementary members calls other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	R0370					
Other ancillary own funds	R0390					
Total ancillary own funds - Solo	R0400					
Available and eligible own funds						
Total available own funds to meet the SCR	R0500	66,510	66,510			
Total available own funds to meet the MCR	R0510	66,510	66,510			
Total eligible own funds to meet the SCR	R0540	66,510	66,510			
Total eligible own funds to meet the MCR	R0550	66,510	66,510			
SCR	R0580	**4,971**				
MCR	R0600	**3,251**				
Ratio of eligible own funds to SCR	R0620	**13.3798**				
Ratio of eligible own funds to MCR	R0640	**20.4610**				

		C0060
Reconciliation Reserve		
Excess of assets over liabilities	R0700	66,510
Own shares (held directly and indirectly)	R0710	
Foreseeable dividends, distributions and charges	R0720	
Other basic own fund items	R0730	61,400
Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	R0740	
Reconciliation reserve	R0760	**5,110**
Expected profits		
Expected profits included in future premiums (EPIFP) - Life business	R0770	
Expected profits included in future premiums (EPIFP) - Non-life business	R0780	
Total expected profits included in future premiums (EPIFP)	R0790	

Appendix F.1.7

Annex I

S.25.01.21

Solvency Capital Requirement - For undertakings on Standard Formula

Amounts in 000s

		Gross solvency capital requirement	USP	Simplifications
		C0110	C0090	C0120
Market risk	R0010	9		None
Counterparty default risk	R0020	3,633		
Life underwriting risk	R0030	75	None	None
Health underwriting risk	R0040		None	None
Non-life underwriting risk	R0050	318	None	None
Diversification	R0060	-213		
Intangible asset risk	R0070			
Basic Solvency Capital Requirement	R0100	3,824		

Calculation of Solvency capital Requirement		C0100
Operational risk	R0130	1,147
Loss-absorbing capacity of technical provisions	R0140	
Loss-absorbing capacity of deferred taxes	R0150	
Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	R0160	
Solvency Capital Requirement excluding capital add-on	R0200	4,971
Capital add-ons already set	R0210	
Solvency capital requirement for undertakings under consolidated method	R0220	4,971
Other information on SCR		
Capital requirement for duration-based equity risk sub-module	R0400	
Total amount of Notional Solvency Capital Requirements for remaining part	R0410	
Total amount of Notional Solvency Capital Requirements for ring fenced funds	R0420	
Total amount of Notional Solvency Capital Requirements for matching adjustment portfolios	R0430	
Diversification effects due to RFF nSCR aggregation for article 304	R0440	

Appendix F.1.8

Annex I

S.28.01.01

Minimum Capital Requirement - Only life or only non-life insurance or reinsurance activity

Amounts in 000s

Linear formula component for non-life insurance and reinsurance obligations

		C0010
MCRNL Result	R0010	1,064

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0020	C0030
Medical expense insurance and proportional reinsurance	R0020		
Income protection insurance and proportional reinsurance	R0030		
Workers' compensation insurance and proportional reinsurance	R0040		
Motor vehicle liability insurance and proportional reinsurance	R0050	6	
Other motor insurance and proportional reinsurance	R0060		
Marine, aviation and transport insurance and proportional reinsurance	R0070		
Fire and other damage to property insurance and proportional reinsurance	R0080	5,227	7,010
General liability insurance and proportional reinsurance	R0090	177	217
Credit and suretyship insurance and proportional reinsurance	R0100		
Legal expenses insurance and proportional reinsurance	R0110		
Assistance and proportional reinsurance	R0120		
Miscellaneous financial loss insurance and proportional reinsurance	R0130		
Non-proportional health reinsurance	R0140		
Non-proportional casualty reinsurance	R0150		
Non-proportional marine, aviation and transport reinsurance	R0160		
Non-proportional property reinsurance	R0170		

Linear formula component for life insurance and reinsurance obligations

		C0040
MCRL Result	R0200	16

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
		C0050	C0060
Obligations with profit participation - Guaranteed benefits	R0210		
Obligations with profit participation - Future discretionary benefits	R0220		
Index-linked and unit-linked insurance obligations	R0230		
Other life (re)insurance and health (re)insurance obligations	R0240	763	
Total capital at risk for all life (re)insurance obligations	R0250		

Overall MCR calculation

		C0070
Linear MCR	R0300	1,080
SCR	R0310	4,971
MCR cap	R0320	2,237
MCR floor	R0330	1,243
Combined MCR	R0340	1,243
Absolute floor of the MCR	R0350	3,251
		C0070
Minimum Capital Requirement	R0400	3,251

F.2 Glossary of Abbreviations and Definitions

99.5% percentile	An event that would be expected to occur once in every 200 years
AIL	Aviva Insurance Ltd
ALCO	Asset and liability committee
Alternative valuation methods	Valuation methods that are consistent with Article 75 of the SII Directive other than those which solely use the quoted market prices for the same or similar assets or liabilities[ii]
Basis risk	The risk resulting from the situation in which the exposure covered by the risk-mitigation technique does not correspond to the risk exposure of the insurance or reinsurance undertaking[ii]
CEO	Chief Executive Officer
CFO	Chief Finance Officer
Collateral arrangements	Arrangements under which collateral providers do one of the following: (a) transfer full ownership of the collateral to the collateral taker for the purposes of securing or otherwise covering the performance of a relevant obligation; (b) provide collateral by way of security in favour of, or to, a collateral taker, and the legal ownership of the collateral remains with the collateral provider or a custodian when the security right is established[ii]
Concentration risk	All risk exposures with a loss potential which is large enough to threaten the solvency or the financial position of insurance and reinsurance undertakings[i]
Credit risk	The risk of loss or of adverse change in the financial situation, resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors to which insurance and reinsurance undertakings are exposed, in the form of counterparty default risk, or spread risk, or market risk concentrations[i]
CRO	Chief Risk Officer
Diversification effects	The reduction in the risk exposure of insurance and reinsurance undertakings and groups related to the diversification of their business, resulting from the fact that the adverse outcome from one risk can be offset by a more favourable outcome from another risk, where those risks are not fully correlated[i]
EEA	European Economic Area
EIOPA	European Insurance and Occupational Pensions Authority
ENID	Events Not in Data are events not deemed to be captured by the data which need to be separately allowed for within the best estimate calculations to take appropriate account of uncertainty.
Expected profit included in future premium	The expected present value of future cash flows which result from the inclusion in technical provisions of premiums relating to existing insurance and reinsurance contracts that are expected to be received in the future, but that may not be received for any reason, other than because the insured event has occurred, regardless of the legal or contractual rights of the policyholder to discontinue the policy[ii]
FCA	Financial Conduct Authority
GAAP	Generally accepted accounting principles
GBP	British pound sterling
The Group	Aviva plc and its subsidiary companies
IFRS	International Financial Reporting Standards (used to prepare the Company's financial statements)
IMMMR	Identify, Measure, Manage, Monitor and Report risks
Liquidity risk	The risk that insurance and reinsurance undertakings are unable to realise investments and other assets in order to settle their financial obligations when they fall due[i]
Longevity risk	The risk associated with annuitants living longer than expected.
Market risk	The risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments[i]
MCR	Minimum Capital Requirement
Operational risk	The risk of loss arising from inadequate or failed internal processes, personnel or systems, or from external events[i]

ORSA	Own Risk and Solvency Assessment
Outsourcing	An arrangement of any form between an insurance or reinsurance undertaking and a service provider, whether a supervised entity or not, by which that service provider performs a process, a service or an activity, whether directly or by sub-outsourcing, which would otherwise be performed by the insurance or reinsurance undertaking itself[i]
PPO	Periodic Payment Orders (annuities stemming from non-life insurance contract)
PRA	Prudential Regulatory Authority
Qualifying holding	A direct or indirect holding in an undertaking which represents 10 % or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of that undertaking
QRT	Quantitative Reporting Templates
RCSA	Risk and control self assessment
Risk Margin	An estimate of the amount, in addition to the Best Estimate Liability that a third party would expect to receive in order to assume ownership of the Company's insurance obligations.
Risk-mitigation techniques	All techniques which enable insurance and reinsurance undertakings to transfer part or all of their risks to another party[i]
SCR	Solvency Capital Requirement
Scenario analysis	The analysis of the impact of a combination of adverse events[ii]
SF	Standard Formula
SII	Solvency II Regulatory Regime
SII Directive	Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 which was subsequently amended by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 (the so-called "Omnibus II Directive"). This Directive lays down rules concerning the following: (1) the taking-up and pursuit, within the Community, of the self- employed activities of direct insurance and reinsurance; (2) the supervision of insurance and reinsurance groups; (3) the reorganisation and winding-up of direct insurance undertakings.
SII Regulations	The directly applicable EU Regulations adopted in accordance with the Solvency II Directive
SPV/Special Purpose Vehicle	Any undertaking, whether incorporated or not, other than an existing insurance or reinsurance undertaking, which assumes risks from insurance or reinsurance undertakings and which fully funds its exposure to such risks through the proceeds of a debt issuance or any other financing mechanism where the repayment rights of the providers of such debt or financing mechanism are subordinated to the reinsurance obligations of such an undertaking [i]
SST	Stress and Scenario Testing
Subrogation	Subrogation is the right for an insurer to legally pursue a third party that caused an insurance loss to the insured. This is done as a means of recovering the amount of the claim paid by the insurance carrier to the insured for the loss.
The commission delegated regulation	The Commission Delegated Regulation (EU) 2015/35 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking up and pursuit of the business of Insurance and Reinsurance (Solvency II) ("the Delegated Acts").
Underwriting risk	The risk of loss or of adverse change in the value of insurance liabilities, due to inadequate pricing and provisioning assumptions[i]

i Article 13 SII Directive
ii Article 1 SII Regulations

F.3 Directors' Statement

We acknowledge our responsibility for preparing the Solvency and Financial Condition Report of Gresham Insurance Company Limited at 31 December 2017 in all material respects in accordance with the PRA Rules and the Solvency II Regulations.

The Board is satisfied that to the best of its knowledge and belief:

(a) throughout the financial year to 31 December 2017, the Company has complied in all material respects with the requirements of the PRA rules and Solvency II Regulations as applicable to the Company; and

(b) it is reasonable to believe that in respect of the period from 31 December 2017 to the date of the publication of the SFCR, the Company has continued so to comply and that it will continue so to comply for the remainder of the financial year to 31 December 2018.

R Barker

Director

27 April 2018

Report of the external independent auditors to the Directors of Gresham Insurance Company Limited ('the Company') pursuant to Rule 4.1 (2) of the External Audit Part of the PRA Rulebook applicable to Solvency II firms

Report on the Audit of the relevant elements of the Solvency and Financial Condition Report

Opinion

We have audited the following documents prepared by the Company as at 31 December 2017:

- The 'Valuation for Solvency Purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Company as at 31 December 2017, ('**the Narrative Disclosures subject to audit**'); and

- Company templates S.02.01.02, S.12.01.02, S.17.01.02, S.22.01.21, S.23.01.01, S.25.01.21 and S.28.01.01 ('**the Templates subject to audit'**).

The Narrative Disclosures subject to audit and the Templates subject to audit are collectively referred to as the '**relevant elements of the Solvency and Financial Condition Report'**.

We are not required to audit, nor have we audited, and as a consequence do not express an opinion on the **Other Information** which comprises:

- The 'Summary', 'Business and Performance', 'System of Governance' and 'Risk Profile' elements of the Solvency and Financial Condition Report;

- Company templates S.05.01.02, S.05.02.01 and S.19.01.21;

- The written acknowledgement by management of their responsibilities, including for the preparation of the Solvency and Financial Condition Report ('**Directors' Statement**').

In our opinion, the information subject to audit in the relevant elements of the Solvency and Financial Condition Report of the Company as at 31 December 2017 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based, as supplemented by supervisory approvals.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) including ISA (UK) 800 and ISA (UK) 805, and applicable law. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the Solvency and Financial Condition Report in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the Solvency and Financial Condition Report is not appropriate; or
- the directors have not disclosed in the Solvency and Financial Condition Report any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the Solvency and Financial Condition Report is authorised for issue.

Emphasis of Matter - Basis of Accounting

We draw attention to the 'Valuation for Solvency Purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report, which describe the basis of accounting. The Solvency and Financial Condition Report is prepared in compliance with the financial reporting provisions of the PRA Rules and Solvency II regulations, and therefore in accordance with a special purpose financial reporting framework. The Solvency and Financial Condition Report is required to be published, and intended users include but are not limited to the Prudential Regulation Authority. As a result, the Solvency and Financial Condition Report may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

Other Information

The Directors are responsible for the Other Information.

Our opinion on the relevant elements of the Solvency and Financial Condition Report does not cover the Other Information and we do not express an audit opinion or any form of assurance conclusion thereon.

In connection with our audit of the Solvency and Financial Condition Report, our responsibility is to read the Other Information and, in doing so, consider whether the Other Information is materially inconsistent with the relevant elements of the Solvency and Financial Condition Report, or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the relevant elements of the Solvency and Financial Condition Report or a material misstatement of the Other Information. If, based on the work we have performed, we conclude that there is a material misstatement of this Other Information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Directors for the Solvency and Financial Condition Report

The Directors are responsible for the preparation of the Solvency and Financial Condition Report in accordance with the financial reporting provisions of the PRA rules and Solvency II regulations which have been supplemented by the approvals made by the PRA under the PRA Rules and Solvency II regulations on which they are based, as detailed below:

- Approval to use the volatility adjustment in the calculation of technical provisions.

The Directors are also responsible for such internal control as they determine is necessary to enable the preparation of a Solvency and Financial Condition Report that is free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report

It is our responsibility to form an independent opinion as to whether the information subject to audit in the relevant elements of the Solvency and Financial Condition Report is prepared, in all material respects, in accordance with financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based.

Our objectives are to obtain reasonable assurance about whether the relevant elements of the Solvency and Financial Condition Report are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decision making or the judgement of the users taken on the basis of the Solvency and Financial Condition Report.

A further description of our responsibilities for the audit is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

This report, including the opinion, has been prepared for the Directors of the Company to comply with their obligations under External Audit rule 2.1 of the Solvency II firms Sector of the PRA Rulebook and for no other purpose. We do not, in providing this report, accept or assume responsibility for any other purpose save where expressly agreed by our prior consent in writing.

Report on Other Legal and Regulatory Requirements

In accordance with Rule 4.1 (3) of the External Audit Part of the PRA Rulebook for Solvency II firms we are also required to consider whether the Other Information is materially inconsistent with our knowledge obtained in the audit of the Company's statutory financial statements. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

PricewaterhouseCoopers LLP
Chartered Accountants
London
27 April 2018