



PENSION INSURANCE  
CORPORATION

# REMOVING RISK FROM PENSION SCHEMES



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**PENSION INSURANCE CORPORATION GROUP LIMITED**

SOLVENCY AND FINANCIAL CONDITION REPORT 2016

# VALUING OUR CUSTOMERS

Pension Insurance Corporation is a specialist insurer, providing long-term security for our policyholders' pensions, based on superior customer service, robust risk management, and expertise in asset and liability management.

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Pension Insurance Corporation Group Limited is the ultimate parent company of Pension Insurance Corporation plc. Pension Insurance Corporation plc is registered in England and Wales under company number 05706720. It is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and Prudential Regulation Authority (FRN 454345). Its registered office is at 14 Cornhill, London EC3V 3ND.

SOLVENCY AND FINANCIAL CONDITION REPORT  
DIRECTORS' RESPONSIBILITY STATEMENT

We acknowledge our responsibility for preparing the insurer and Group Solvency and Financial Condition Report in all material respects in accordance with the Prudential Regulatory Authority Rules and the Solvency II Regulations.

We are satisfied that:

- a) throughout the financial year in question, the insurer and Group has complied in all material respects with the requirements of the PRA Rules and the Solvency II Regulations as applicable at the level of the insurer and Group; and
- b) it is reasonable to believe that the insurer and Group has continued so to comply subsequently and will continue so to comply in future.

A handwritten signature in black ink, appearing to be 'P. J. ...', written over a horizontal line.

Signed on behalf of the Board of Directors of Pension Insurance Corporation Group Limited

20 June 2017

# SOLVENCY AND FINANCIAL CONDITION REPORT

## REPORT OF THE INDEPENDENT AUDITOR

### Report of the external independent auditor to the Directors of Pension Insurance Corporation Group Limited ('the Group') pursuant to Rule 4.1 (2) of the External Audit Chapter of the PRA Rulebook applicable to Solvency II firms

Except as stated below, we have audited the following documents prepared by Pension Insurance Corporation Group Limited as at 31 December 2016:

- the 'Valuation for solvency purposes' and 'Capital Management' sections of the Group Solvency and Financial Condition Report of Pension Insurance Corporation Group Limited as at 31 December 2016, (**'the Narrative Disclosures subject to audit'**); and
- Group templates S.02.01.02, S.22.01.22, S.23.01.22, S.32.01.22 and Company templates S.02.01.02, S.12.01.02, S.22.01.21, S.23.01.01, 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 Group 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:

- information contained within the Relevant Elements of the Group Solvency and Financial Condition Report set out above which are, or derive from the Solvency Capital Requirement, as identified in the Appendix to this report;
- the 'Business and performance', 'System of governance' and 'Risk profile' sections of the Group Solvency and Financial Condition Report;
- Group templates S.05.01.02, S.05.02.01, S.25.03.22;
- Company templates S.05.01.02, S.05.02.01, S.25.03.21;
- information calculated in accordance with the previous regime used in the calculation of the transitional measure on technical provisions, and as a consequence all information relating to the transitional measures on technical provisions as set out in the Appendix to this report where disclosed;
- the written acknowledgement by the Directors of their responsibilities, including for the preparation of the Group Solvency and Financial Condition Report (**'the Responsibility Statement'**);
- information which pertains to an undertaking that is not a Solvency II undertaking and has been prepared in accordance with PRA Rules other than those implementing the Solvency II Directive or in accordance with an EU instrument other than the Solvency II Regulations (**'the sectoral information'**).

To the extent the information subject to audit in the Relevant Elements of the Group Solvency and Financial Condition Report includes amounts that are totals, sub-totals or calculations derived from the Other Information, we have relied without verification on the Other Information.

### Respective responsibilities of directors and auditor

As explained more fully in the Responsibility Statement, the Directors are responsible for the preparation of the Group Solvency and Financial Condition Report in accordance with the financial reporting provisions of the PRA Rules and Solvency II Regulations which have been modified by the modifications, and supplemented by the approvals and determinations made by the PRA under section 138A of FSMA, the PRA Rules and Solvency II Regulations on which they are based.

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

Our responsibility is to audit, and express an opinion on, the Relevant Elements of the Group Solvency and Financial Condition Report in accordance with applicable law and International Standards on Auditing (UK and Ireland) together with ISA (UK) 800 and ISA (UK) 805. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### Scope of the audit of the Relevant Elements of the Group Solvency and Financial Condition Report

A description of the scope of an audit is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate).

### Opinion on the Relevant Elements of the Group Solvency and Financial Condition Report

In our opinion, the information subject to audit in the Relevant Elements of the Group Solvency and Financial Condition Report of Pension Insurance Corporation Group Limited as at 31 December 2016 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 modified by relevant supervisory modifications, and as supplemented by supervisory approvals and determinations.

### Emphasis of Matter – Basis of Accounting

We draw attention to the 'Valuation for solvency purposes' and 'Capital Management' and sections of the Group Solvency and Financial Condition Report, which describe the basis of accounting. The Group 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 Group Solvency and Financial Condition Report may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

### Other Matter

The Company has authority to calculate its Group Solvency Capital Requirement using an internal model ("the Model") approved by the Prudential Regulation Authority in accordance with the Solvency II Regulations. In forming our opinion (and in accordance with PRA Rules), we are not required to audit the inputs to, design of, operating effectiveness of and outputs from the Model, or whether the Model is being applied in accordance with the Company's application or approval order.

### Opinion on other matter prescribed by the PRA Rulebook

In our opinion, in accordance with Rule 4.2 of the External Audit Chapter of the PRA Rulebook, the **sectoral information** has been properly compiled in accordance with the PRA Rules and EU instruments relating to that undertaking from information provided by members of the group and the relevant insurance group undertaking.

### Matters on which we are required to report by exception

In accordance with Rule 4.1 (3) of the External Audit Chapter 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 Pension Insurance Corporation Group Limited's and Pension Insurance Corporation plc'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.

### The purpose of our audit work and to whom we owe our responsibilities

This report of the external auditor is made solely to the company's directors, as its governing body, in accordance with the requirement in Rule 4.1(2) of the External Audit Part of the PRA Rulebook and the terms of our engagement. We acknowledge that the directors are required to submit the report to the PRA, to enable the PRA to verify that an auditor's report has been commissioned by the company's directors and issued in accordance with the requirement set out in Rule 4.1(2) of the External Audit Part of the PRA Rulebook and to facilitate the discharge by the PRA of its regulatory functions in respect of the company, conferred on the PRA by or under the Financial Services and Markets Act 2000.

Our audit has been undertaken so that we might state to the company's directors those matters we are required to state to them in an auditor's report issued pursuant to Rule 4.1(2) and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company through its governing body, for our audit, for this report, or for the opinions we have formed.

**KPMG LLP**

**KPMG LLP**

Chartered Accountants  
15 Canada Square,  
London,  
E14 5GL

20 June 2017

The maintenance and integrity of Pension Insurance Corporation's website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Solvency and Financial Condition Report since it was initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of Solvency and Financial Condition Reports may differ from legislation in other jurisdictions.

# SOLVENCY AND FINANCIAL CONDITION REPORT SUMMARY

The Solvency and Financial Condition Report ("SFCR") is an annual report that is required to be produced under European Union ("EU") and UK law, as part of the Solvency II regime.

A simplified structure chart of the Pension Insurance Corporation Group is shown in section A.1.

The Group is required to produce a single SFCR, covering both Pension Insurance Corporation plc ("PIC", or 'the Company') and Pension Insurance Corporation Group Limited ("PICG", or 'the Group'). This requirement is set out in a direction made by the Prudential Regulatory Authority ("PRA") on 19 December 2016. This direction is in force until 19 December 2019.

PIC is the principal operating company of the Group and is the regulated insurance company for which this Group SFCR is required.

The SFCR is a public document, and is required to be published on the Company's website. It also must be provided to the Company's prudential regulator, the PRA.

The content of the SFCR is prescribed by EU regulation, and must contain the following sections:

Section	Description of content
Business and performance	Provides the basic information on the Group and Company, and gives a summary of the business performance during the year in question.
System of governance	Provides governance information on the Group and Company including Board and Committee structure, responsibilities, and details of the principal process.
Risk profile	Provides qualitative and quantitative information regarding the risks that face the Group and Company, and how they are managed.
Valuation for solvency purposes	Provides values for the Group and Company's assets and liabilities in accordance with IFRS and Solvency rules, gives details on the assumptions used in the valuations, and provides differences on valuation differences between IFRS and Solvency II.
Capital management	Provides detail on the regulatory capital (Own Funds) which the Group and Company must hold in line with Solvency II rules, and the composition of such Own Funds.

A summary of the content of each of these sections is provided below:

## Business and performance

The Group and Company continued to trade profitably during 2016. The Group made an IFRS profit before tax of £266m (2015: £136m). This was primarily made up of profits before tax from PIC of £276m (2015: £104m), together with losses from other companies (primarily Group costs borne at top company level) of £10m (2015: £32m).

As set out in its IFRS Annual Report and Financial Statements, PIC considers its IFRS profit before tax on an "operating profit" basis, which is explained below.

Operating profit before tax has been defined to reflect the activities which are core to PIC's business, and to reflect the management choices and decisions around those activities. These encompass the writing and management of pension insurance contracts, the management of risk through reinsurance, and the day-to-day investment and management of the insurance assets and liabilities.

Within this, management have defined a measure of "underlying operating profit before tax" which captures the returns made from the

in-force book of insurance liabilities and expected long-term returns from surplus assets.

Non-operating profit includes the impacts of the external economic environment on the Company, as well as one-off expenses and the effects of actuarial assumption changes where PIC is required to recognise the overall impact of changes within one discrete accounting period.

The operating profit basis is more aligned to the way management view the business, and the decisions which management make around the Company's core activities.

A summary of the IFRS-based measures of profit or loss, and an explanation of the results of the Company expressed on this basis, follows below:

	2016 £m	2015 £m
Return earned on insurance book	122	87
Expected return earned on surplus assets	55	46
<b>Underlying operating profit before tax</b>	<b>177</b>	133
New business and reinsurance	(26)	59
Other changes to in-force business	(3)	(4)
<b>Operating profit before tax</b>	<b>148</b>	188
Non-operating profit/(loss) before tax	128	(84)
<b>IFRS profit before tax</b>	<b>276</b>	104

## Underlying operating profit before tax

Underlying operating profit before tax consists of the net returns the Company makes from its insurance liabilities and assets, and the return made from its surplus assets held above this level, estimated using a long-term assumption of the returns which these assets will generate.

Underlying operating profit before tax in 2016 was £177m (2015: £133m). The return earned from the insurance book (£122m) is higher than 2015, reflecting the growth in the value of financial investments over the past 12 months. The expected return on surplus assets (£55m) is higher than 2015, reflecting the increase in the amount of surplus assets during the year.

## Operating profit before tax

In addition to the items which constitute underlying operating profit before tax, operating profit before tax considers the impacts of new business and reinsurance transactions undertaken in the year, as well as any other changes to in-force business that are within management discretion.

During the year, PIC completed a further 17 (2015: 13) new transactions with pension schemes, with a total premium amount of £2.6bn (2015: £3.8bn).

PIC concluded two longevity swap (2015: three) reinsurance transactions during the year which covered longevity risk on c.£1.4bn (2015: £3.8bn) of insurance liabilities.

Taking into account the requirement to set up technical provisions in respect of liabilities acquired in new business transactions, together with the costs incurred, but offset by the impact of reinsurance completed during the year, these items contributed negative £26m (2015: £59m profit) to operating profits.

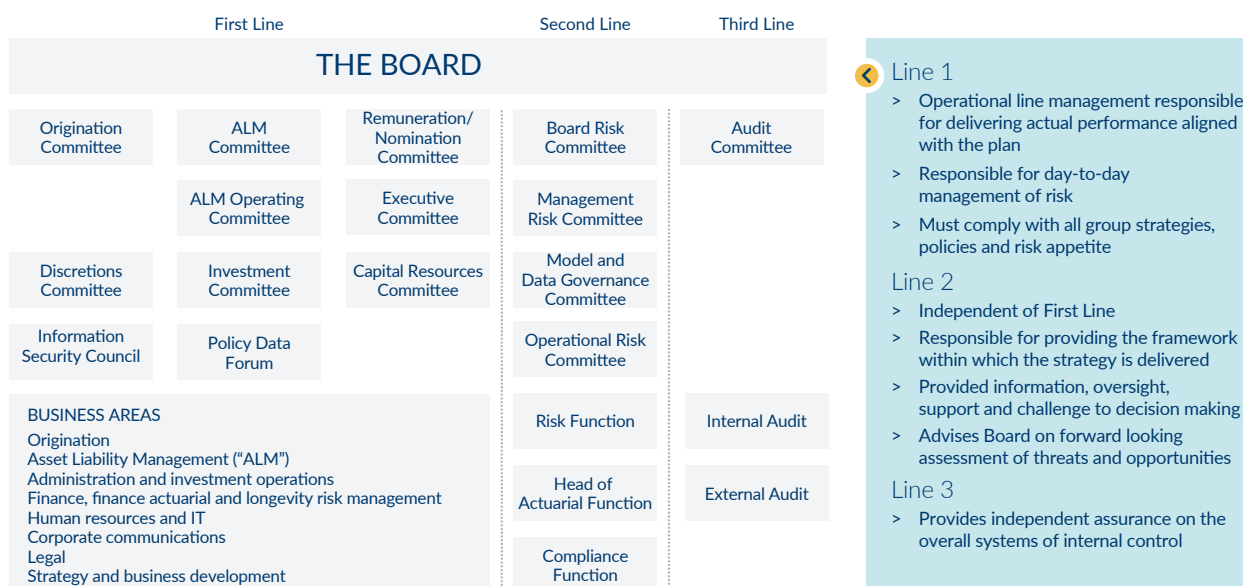
## Non-operating profit before tax

Non-operating profit before tax for the year was £128m (2015: £84m loss). Non-operating profit encompasses the impacts of the wider economic environment on the Company, as well as interest expense on subordinated loan notes, one-off expenses and the effects of actuarial assumption changes, where PIC is required to recognise the overall impact of changes within each discrete accounting period.

The Company's preferred hedging benchmark for interest rates and inflation rates is the regulatory Solvency II balance sheet. This does however create basis risk for the IFRS results. Significant interest and inflation rate volatilities seen during the year as well as narrowing credit spreads over the period resulted in a £153m IFRS profit. Such profits are not expected to arise to the same extent going forward as the hedging benchmarks across IFRS and Solvency II basis become more closely aligned. This gain was offset by a £22m interest expense and a net £3m loss from other minor items.

### System of governance

PIC's governance structure supports the "three lines of defence" model which is operated by the Group. This structure is summarised below:



### Risk profile

The Group and Company's risk profile is best measured by its Internal Model, which was approved for use by the PRA in December 2015.

The following table below shows the component risks which make up the Group's total Solvency Capital Requirement ("SCR"), which represents the amount of capital the firm must hold to protect it from extreme risk events and comply with EU regulation.

SCR - 31 December 2016	£m
Market risk	1,524
Counterparty risk	64
Insurance risk	1,227
Expense risk	115
Operational risk	171
<b>Total before diversification</b>	<b>3,101</b>
Diversification	(959)
<b>Total after diversification</b>	<b>2,142</b>
Loss absorbing capacity of deferred tax ("LACDT")	(230)
<b>Total SCR after LACDT</b>	<b>1,912</b>

### Valuation for solvency purposes

The table below summarises the Company and Group's asset and liabilities valued in accordance with its statutory accounting basis (IFRS), and the Solvency II regulatory basis at 31 December 2016:

£m	Group		Company	
	Solvency	IFRS	Solvency	IFRS
Total Assets	35,302	34,821	35,268	34,789
Total Liabilities	32,148	33,042	32,134	33,029
Own Funds/Equity	3,154	1,779	3,134	1,760

Differences in the valuation of assets and liabilities between the two bases are driven by the following:

- Subordinated debt issued by PIC, which is treated as a liability for IFRS purposes and Own Funds for Solvency purposes;
- Derivative assets and liabilities reported under IFRS include a net Exchange Rate Forward position. In order to meet Solvency currency reporting requirement's these amounts are not netted and both assets and liabilities are reported gross;
- Adjustments relating to differences between the IFRS and Solvency results related to liability, reinsurance and deferred tax positions; and
- Minor valuation differences between IFRS and Solvency results (such as valuation differences relating to fixed assets and intangible assets at a Group level).

### Capital management

The table below summarises the Group and Company's capital and solvency position as at 31 December 2016.

	Group	Company
Own Funds (£m)	3,154	3,134
SCR (£m)	1,912	1,912
SCR coverage ratio %	165%	164%

The Group and Company have been granted permission by the PRA to use an Internal Model for the purposes of calculating the SCR.

# A. BUSINESS AND PERFORMANCE (UNAUDITED)

## A.1 Business

The full legal name of the undertaking is Pension Insurance Corporation plc. It is a public limited company, registered in England and Wales with the company registration number 05706720.

The Company is a wholly owned subsidiary of PIC Holdings Limited. PIC Holdings Limited is a wholly owned subsidiary of PICG a company registered in England and Wales and the European registered company in the Group. PICG is regarded as the ultimate parent company of PIC.

Pension Services Corporation Limited ("PSC") is a subsidiary company of PIC Holdings Limited, and provides employees and other services to companies within the PICG.

The external auditor to the Group is KPMG LLP, 15 Canada Square, London E14 5GL.

PIC is authorised by the PRA, 20 Moorgate, London EC2R 6DA and regulated by the Financial Conduct Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS and PRA (FRN 454345).

The principal activity of PIC is providing insurance annuity products to UK defined benefit occupational pension funds and their members (commonly referred to as "pension insurance" or "bulk annuities"). Pension insurance products are used by pension funds to transfer to an insurance company the risks and liabilities arising from the benefit promises made to pension fund members. Insurance is also used as a means by which the ultimate responsibility to pay the benefits promised is transferred to the insurance company through the issuance of an individual annuity insurance policy to the pension fund member.

The Group and Company prepares their financial statements in accordance with International Financial Reporting Standards ("IFRS") and those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

### Summary of the IFRS Statement of comprehensive income for the year ended 31 December 2016

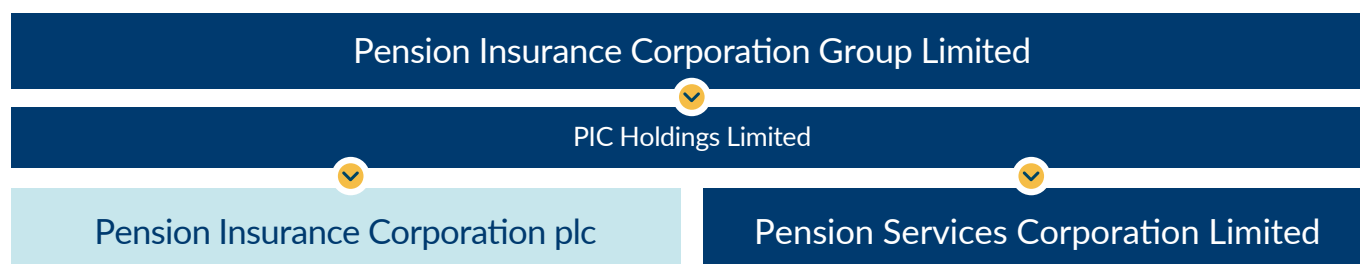
£m	Group		Company	
	2016	2015	2016	2015
Net premium revenue earned	<b>2,574</b>	3,557	<b>2,574</b>	3,912
Investment income	<b>607</b>	451	<b>607</b>	447
Net realised gains	<b>374</b>	543	<b>374</b>	445
Net unrealised gains/ (losses)	<b>2,239</b>	(1,240)	<b>2,239</b>	(1,144)
Net claims	<b>(768)</b>	(565)	<b>(768)</b>	(565)
Movement in net long-term business provision	<b>(4,656)</b>	(2,517)	<b>(4,656)</b>	(2,903)
Administrative expenses	<b>(104)</b>	(93)	<b>(94)</b>	(88)
<b>Profit before taxation</b>	<b>266</b>	136	<b>276</b>	104

The Company made an IFRS profit before tax of £276m in 2016 (2015: £104m), and the Group made an IFRS profit before tax of £266m in 2016 (2015: £136m).

During 2016, the Company continued its strategy of providing pension insurance products to defined benefit schemes and their trustees.

## Group

A simplified Group structure chart, and a description of the Group as at 31 December 2016 is set out below:



Group undertakings	Country of Incorporation	Principal activity	2016 % equity holding	2015 % equity holding
Pension Insurance Corporation Group Limited	England	Holding company		
PIC Holdings Limited	England	Holding company	100%	100%
Pension Insurance Corporation plc	England	Bulk annuity insurance	100%	100%
Pension Services Corporation Limited	England	Service company	100%	100%



### Material lines of business and geographical areas

The principal activity of PICG is to act as the holding company for the other companies within the PICG Group. It has no employees, and incurs administrative expenses. It also holds any share incentive plans which are in existence for the Group.

PIC Holdings Limited is an intermediate holding company, and has no material assets or liabilities in the context of the Group.

The principal activity of PIC is providing insurance annuity products to UK defined benefit occupational pension funds and their members.

PSC is the service company of the Group, and employs all the staff which are responsible for the performance of the Group's activities. It also enters into material contracts (with the exception of pension insurance contracts) on behalf of the Group.

During 2016, PSC had income of £66,450k from other Group companies (primarily PIC) for the performance of its service contracts.

The tables in sections A.2 to A.4 below present extracts from the Group's and Company's IFRS Income Statements, splitting the IFRS income and expense items between underwriting activity (section A.2), investment activity (section A.3) and other activity (section A.4). Comparative information has been presented where available.

### A.2 Performance of underwriting activity

£m	Group		Company	
	2016	2015	2016	2015
Gross premiums written	<b>2,598</b>	3,755	<b>2,598</b>	3,755
Outward reinsurance premiums	<b>(24)</b>	157	<b>(24)</b>	157
<b>Net premium revenue earned</b>	<b>2,574</b>	3,912	<b>2,574</b>	3,912
Claims paid – gross	<b>(797)</b>	(581)	<b>(797)</b>	(581)
Reinsurers' share of claims paid	<b>29</b>	16	<b>29</b>	16
<b>Net claims</b>	<b>(768)</b>	(565)	<b>(768)</b>	(565)
Gross increase in insurance liabilities	<b>(5,261)</b>	(2,656)	<b>(5,261)</b>	(2,656)
Increase/(decrease) in reinsurers' share of insurance liabilities	<b>605</b>	(247)	<b>605</b>	(247)
<b>Movement in net long-term business provision</b>	<b>(4,656)</b>	(2,903)	<b>(4,656)</b>	(2,903)
Acquisition and other operating expenses	<b>(95)</b>	(84)	<b>(85)</b>	(79)
<b>Underwriting result</b>	<b>(2,945)</b>	360	<b>(2,935)</b>	365

The table above sets out a sub-section of the Group and Company's results for the year. The overall profit for the year is set out in the table in section A.1 above.

The underwriting result, as presented in the table above, is only a reflection of premiums written, claims paid, changes in insurance liabilities (whether arising from new business, or from changes in economic or non-economic assumptions) and expenses. It does not reflect any investment activity, or income and gains from the investment portfolio owned by the Group, which is presented in section A.3.

During the year, PIC completed a further 17 (2015: 13) new transactions with pension schemes, with a total premium amount of £2.6bn (2015: £3.8bn).

PIC concluded two longevity swap (2015: three) reinsurance transactions during the year which covered longevity risk on c.£1.4bn (2015: £3.8bn) of insurance liabilities.

The Company is now responsible for the pension payments of 134,900 individuals (2015: 132,100). Payment of annuities grew by 24% in 2016 to £600m (2015: £484m) mainly through new business written during the year and previous year. Total claim amounts paid were £797m (2015: £581m), an increase of 37%, as the growth in annuity payments was supplemented by a growth in lump sum payments and transfers out compared with the prior year.

At the end of 2016, PIC had 80,900 current individual policies in issue, in respect of 74 pension schemes, compared with 81,000 in respect of 64 schemes in 2015. The number of individual policies in issue reduced by 4,000 as a result of a winding up lump sum exercise carried out during the year, whilst a number of individual policies were written as schemes converted to full buyout. The remaining policies are either in the transition process, which includes the verification of policy data and finalisation of liabilities prior to individual policies being issued by PIC, or are buy-ins under which PIC's contract is with the pension scheme trustees and no individual policies are issued. The number of policies in issue will also be affected by reductions due to leavers, transfers and deaths.

At 31 December 2016, 68% of PIC's total longevity exposure on a regulatory solvency basis was reinsured to third party, investment grade reinsurer counterparties (2015: 71% on a comparable basis).

Group level expenses of £10m (2015: £5m) have been included within "Acquisition and other operating expenses" above.

### A.3 Performance of investment activity

IFRS £m	Group		Company	
	2016	2015	2016	2015
Interest income	<b>562</b>	370	<b>562</b>	368
Other investment income	<b>45</b>	81	<b>45</b>	79
Realised gains	<b>416</b>	648	<b>416</b>	554
Realised losses	<b>(42)</b>	(105)	<b>(42)</b>	(109)
Unrealised gains	<b>3,012</b>	15	<b>3,012</b>	15
Unrealised losses	<b>(773)</b>	(1,255)	<b>(773)</b>	(1,159)
Investment management expenses	<b>(9)</b>	(9)	<b>(9)</b>	(9)
<b>Total</b>	<b>3,211</b>	(255)	<b>3,211</b>	(261)

The table above sets out a sub-section of the Group and Company's results for the year. The overall profit for the year is set out in the table in section A.1 above.

The investment performance, as presented in the table above, is only a reflection on income, gains, losses and expenses arising from the investment portfolio owned by the Group. It does not reflect any insurance activity, which is presented in section A.2.

## A. BUSINESS AND PERFORMANCE (UNAUDITED)

CONTINUED

Investment income: by Solvency II Asset Class £m	Group and Company 2016
Government bonds	1,506
Corporate bonds	2,178
Collective Investment undertakings	73
Cash and deposits	(8)
Collateralised securities	17
Mortgages and loans	94
Property	6
Derivative based instruments	(646)
<b>Total</b>	<b>3,220</b>

Derivative instruments are held by the Group for the purposes of risk management and hedging, and accordingly the losses reflected above are more than offset by, and should be viewed in the context of, gains recognised on other classes of assets.

Solvency asset class information is collated from the implementation date of 1 January 2016.

**A.4 Performance of other activities****Pension Insurance Corporation plc**

The Company incurred tax charges of £55m for the year ended 31 December 2016.

**Pension Insurance Corporation Group Limited**

Group tax charges, including those incurred by PIC, were £54m during the year.

**A.5 Any other information**

None.

# B. SYSTEM OF GOVERNANCE (UNAUDITED)

## B.1 General Information on the system of governance

### Board of Directors

Pension Insurance Corporation Group Limited

PICG is governed by its Board of Directors (the "Board") consisting of 13 Directors, 12 of whom are non-executive. A majority of PICG's Directors are independent.

Of the non-executive Board members, two are appointed by Reinet PC Investments (Jersey) Limited which indirectly holds a 43.48% interest in PIC, one is appointed by PIC Holdings (Cayman) Limited, a JC Flowers entity, which indirectly holds a 21.411% interest in PIC, and one is appointed by Blue Grass Holdings Limited, a CVC entity, which indirectly holds a 12.93% interest in PIC.

The Board maintains overall responsibility for PICG and an oversight responsibility for the Pension Insurance Corporation Group (the Group) in the best interests of its policyholders, shareholders, employees and other stakeholders and to set the Group's long-term objectives and commercial strategy.

The main activities of the Group are conducted through its principal operating subsidiary, PIC.

The Board has delegated the day-to-day management and administration of the Company to the Chief Executive Officer ("CEO") who established the Executive Committee at the operating entity level, PIC, to assist the CEO in day-to-day running of PIC.

### PICG

Director	Approved function
Jon Aisbitt	SIMF 7 Group Entity Senior Insurance Manager Function, SIMF 9 Chairman
Tracy Blackwell	SIMF 1 Chief Executive Function, SIMF 7 Group Entity Senior Insurance Manager Function
Mike Eves	Non-Executive Director
Ed Giera	Non-Executive Director
Tim Hanford	SIMF 7 Group Entity Senior Insurance Manager Function
Arno Kitts	Non-Executive Director
Jing Li	SIMF 7 Group Entity Senior Insurance Manager Function
Nick Lyons	SIMF 12 Chair of the Remuneration Committee, SIMF 14 Senior Independent Director
Josua Malherbe	SIMF7 Group Entity Senior Insurance Manager Function
Roger Marshall	Non-Executive Director
Eloy Michotte	SIMF 7 Group Entity Senior Insurance Manager Function
Peter Rutland	SIMF 7 Group Entity Senior Insurance Manager Function
Mark Stephen	Non-Executive Director

### Pension Insurance Corporation plc

PIC is governed by its Board of Directors (the "Board") consisting of 13 Directors, 11 of whom are non-executive. A majority of PIC's Directors are independent.

Of the non-executive Board members, two are appointed by Reinet PC Investments (Jersey) Limited which indirectly holds a 43.48% interest in PIC, one is appointed by PIC Holdings (Cayman) Limited, a JC Flowers entity, which indirectly holds a 21.411% interest in PIC, and one is appointed by Blue Grass Holdings Limited, a CVC entity, which indirectly holds a 12.93% interest in PIC.

The Board has overall responsibility for the operations of PIC and oversees the management of the Company in the best interests of its policyholders, shareholders, employees and other stakeholders and to set the Company's long-term objectives and commercial strategy.

The Board has delegated responsibility for a number of functions to Board Committees as set out below. The Committees all have Terms of Reference setting out in more detail their responsibilities.

The Board has delegated the day-to-day management and administration of the Company to the Chief Executive Officer ("CEO") who has established the Executive Committee to assist the CEO with day-to-day running of PIC.

### PIC

Director	Approved function
Jon Aisbitt	SIMF 7 Group Entity Senior Insurance Manager Function, SIMF 9 Chairman
Tracy Blackwell	SIMF 1 Chief Executive Function, SIMF 7 Group Entity Senior Insurance Manager Function
Amanda Bowe	Non-Executive Director
Timothy Hanford	SIMF 7 Group Entity Senior Insurance Manager Function
Arno Kitts	Non-Executive Director
Nick Lyons	SIMF 12 Chair of the Remuneration Committee SIMF 14 Senior Independent Director
Roger Marshall	SIMF 11 Chair of the Audit Committee
Eloy Michotte	SIMF 7 Group Entity Senior Insurance Manager Function
Peter Rutland	SIMF 7 Group Entity Senior Insurance Manager Function
Steve Sarjant	SIMF 10 Chair of the Risk Committee
Rob Sewell	SIMF 2 Chief Finance Function
Mark Stephen	Non-Executive Director
Wilhelm Van Zyl	SIMF 7 Group Entity Senior Insurance Manager Function

### Audit Committee

The Audit Committee's key role is to assist the Board with the discharge of its responsibilities with regard to oversight of the financial reporting process, the system of internal controls, internal and external audits, and system of governance and compliance.

The Audit Committee comprises four Non-Executive Directors and is chaired by Roger Marshall. The Board is satisfied that members of the Audit Committee have relevant accounting and financial reporting experience.

### Financial reporting

The Audit Committee oversees the financial reporting process, monitors integrity of the financial statements which includes the annual financial statements of the Company, half yearly results, regulatory returns and any significant estimates and judgements made as well as a review whether the Company has followed appropriate accounting standards.

### Internal controls

The Audit Committee oversees and, where necessary, challenges the framework, effectiveness and adequacy of the Company's systems of internal control. The Committee reviews findings and recommendations of the Internal Audit and External Auditors and receives an Integrated Assurance Report which forms basis to the statements included in the annual report and financial statements with regard to the effectiveness of the internal controls system.

# B. SYSTEM OF GOVERNANCE (UNAUDITED)

CONTINUED

## Financial crime and whistleblowing

The Audit Committee reviews the adequacy and security of the Company's arrangements for its employees and contractors to raise concerns about possible wrongdoing in financial reporting and other matters. It also reviews the Company's arrangements for detection of fraud, and systems and controls for the prevention of bribery and anti-money laundering.

## Internal audit

The Audit Committee reviews the effectiveness of the Company's internal audit function in the context of the Company's overall risk management system and its performance against agreed objectives, approves and removes the Head of Internal Audit. The Committee receives, reviews and approves the annual internal audit plan, which forms part of the annual Integrated Assurance programme; and monitors management's responsiveness to the Internal Audit's findings.

## External audit

The Audit Committee considers and makes recommendations to the Board in relation to the appointment, re-appointment and removal of the Company's external auditor, its terms of engagement and fees. The Audit Committee also reviews of non-audit services fees and monitors that these are in accordance with the Company's non-audit services policy and assesses the External Auditor's independence and objectivity. The Audit Committee reviews and approves the annual audit plan, reviews the External Auditor's findings with the auditor and with the Company.

## Risk Committee

The Risk Committee has primary responsibility to the Board for the Risk Management Framework which includes the Company's current and likely risk exposures, risk tolerances and appetite, risk measurement, risk management performance, and its risk policies and procedures, as well as recommending the risk policies to the Board.

## Risk strategy, appetite and policy

The Risk Committee advises the Board on the Company's overall risk exposures, and the current and future risk strategy. The Committee reviews and recommends to the Board the design and implementation of Risk Management Frameworks and measurement strategies for the Company. It further reviews and recommends to the Board for approval the risk appetite and tolerances.

## Risk oversight and monitoring

The Risk Committee keeps under review the Company's overall risk identification, assessment and management process that inform the Board's decision making. The Committee is responsible for oversight of the Internal Model and for reporting to the Board on any areas needing improvement, and updating the Board on the status of efforts to improve previously identified weaknesses.

The Committee advises the Board on the risks to the business plan and capital implications making sure that these are adequately identified and assessed as part of the business planning process through stress testing and scenario analysis. The Committee also works with the Nomination and Remuneration Committee to ensure that risk management is taken into consideration in objective setting and the design of overall remuneration. It further provides advice, oversight and challenge necessary to embed and maintain a supportive risk culture throughout the Company.

The Risk Committee also reviews reports on any material breaches of risk and compliance limits and material incidents, and monitors the adequacy of proposed actions and management's responsiveness to remedial actions proposed by the Chief Risk Officer.

## Risk Function and the Chief Risk Officer

The Risk Committee considers and approves the Risk Function mandate and reviews and assesses performance of the Chief Risk Officer.

## Asset Liability Management Committee

The Asset Liability Management Committee oversees the management of all aspects of investment policy and strategy for PIC and provides oversight of the operation of PIC's investment portfolios within established strategy and risk frameworks.

## Origination Committee

The Origination Committee's role is to oversee all aspects of PIC's new business and reinsurance origination within established strategy, business plan and risk frameworks including conduct risk. The Committee also oversees all aspects of interaction with policyholders including administration, tracing, and complaints and recommends to the Board any actions needed to ensure policyholders are treated fairly.

The Committee at least annually approves the pricing assumptions used by the Pricing Committee and approves the pricing authority for the Pricing Committee. The Committee also provides additional oversight of the outsourced administration of policies.

## Nomination and Remuneration Committee

The Nomination and Remuneration Committee's role is to regularly review the structure, size and composition (including the skills, knowledge, experience and diversity) of the Board and make recommendations to the Board with regard to any changes and determine and agree with the Board the framework or broad policy for the remuneration of all employees and the specific compensation in respect of the Company's Chairman, Non-Executive Directors, Chief Executive, the executive directors and such other members of the executive management as it is designated to consider.

## Executive Committee

The Executive Committee consists of the CEO and senior management of the Company. Its role is to propose strategy to the Board and, once approved, implement it together with operational plans, policies, procedures and budgets. The Committee's purpose is also to shape, embed and maintain a culture which safeguards PIC's values by promoting attitudes and behaviours of high ethical standards and integrity in everyday conduct of PIC's business. The Committee further ensures that appropriate systems and controls are in place; monitors operating and financial performance, assesses and controls risks. The Committee also reviews resources and prioritises their use and allocation.

## Executive Committee

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Chief Executive Officer ("CEO")  
 Chief Financial Officer ("CFO")  
 Chief Risk Officer ("CRO")  
 Chief Operating Officer ("COO")  
 General Counsel ("GC")  
 Head of Strategic Development ("HSD")  
 Chief Origination Officer ("COrigO")  
 Chief Administration Officer ("CAO")  
 Chief Investment Officer ("CIO")  
 Head of Internal Audit ("HIA")

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### Material changes to the governance structure over the reporting period

#### Pension Insurance Corporation Group Limited

The Board of Directors of PICG all served from 1 January 2016 to the date of this report, with the exception of the following appointments or resignations:

- Harriet Maunsell was appointed on 4 February 2016 and resigned on 31 December 2016;
- Nick Lyons and Mark Stephen were both appointed on 24 May 2016;
- Mustafa Beg and Ian Crosby both resigned on 31 May 2016;
- Arno Kitts was appointed on 1 July 2016;
- Jing Li was appointed on 1 September 2016;
- Roger Le Tissier resigned on 21 September 2016;
- Jon Aisbitt was appointed on 14 October 2016, replacing Sir Mark Weinberg who resigned on 14 October 2016;
- Roger Marshall was appointed on 1 April 2017; and
- Peter Rutland was appointed on 5 May 2017.

On 21 March 2017 the Board of PICG decided to disband its Audit and Risk Committee and delegate its risk and audit responsibilities to the PIC Risk Committee and PIC Audit Committee respectively. The decision was taken in order to streamline the governance structure of the PIC Group and reduce governance overlap.

#### Pension Insurance Corporation plc

The Board of Directors of PIC all served from 1 January 2016 to the date of this report, with the exception of the following appointments or resignations:

- Nick Lyons was appointed on 26 February 2016;
- Arno Kitts was appointed on 1 July 2016, replacing Chris McKechnie who resigned on 25 May 2016;
- Jon Aisbitt was appointed on 14 October 2016, replacing Sir Mark Weinberg who resigned on 14 October 2016;
- Harriet Maunsell resigned on 31 December 2016;
- Amanda Bowe was appointed on 1 January 2017;
- Peter Rutland was appointed on 5 May 2017; and
- John Coomber resigned on 22 May 2017.

### Remuneration policies and practices

#### Governance of remuneration

The PIC Nominations and Remuneration Committee (the "RemCo"), which is a sub-committee of the Board, has responsibility for setting the remuneration policy of the Company and for its implementation. Reports on Committee activity are provided to the Board as appropriate.

The RemCo fully consists of Non-Executive Directors and is chaired by an independent Non-Executive Director. The RemCo is governed by its Terms of Reference, which sets out its duties, which are reviewed regularly.

The RemCo is responsible for the determination, regular review and implementation of the remuneration policy. The RemCo is also responsible for individual remuneration arrangements and outcomes for the Company's Chairman, Chief Executive, executive directors and such other members of the executive management as it is designated to consider (all Solvency II Identified Staff). To minimise the risk of any conflicts of interest, no individual is involved in decisions regarding their own remuneration.

In its oversight of the remuneration structures, the RemCo takes full account of strategic objectives and stakeholder views, as well as the interests of the customer/policyholder. The alignment of risk and reward is a prominent consideration, and the RemCo seeks input from the CRO, Chair of the Board Risk Committee ("BRC"), and the Chair of the Audit Committee in the design of remuneration policies and in determining collective and individual reward outcomes.

The RemCo also has responsibility for compliance with all relevant legal and regulatory requirements on remuneration, including Solvency II which came into force on 1 January 2016. The RemCo has undertaken significant work in relation to ensuring that its remuneration policies and practices are suitably aligned with the requirements of Solvency II, and is now responsible for the oversight of individual remuneration arrangements and outcomes in respect of all Solvency II Identified Staff.

## B. SYSTEM OF GOVERNANCE (UNAUDITED)

CONTINUED

## Remuneration policy

The Company's remuneration policy is designed to enable the Company to recruit, retain and motivate employees of the appropriate calibre to deliver its strategy over the long term. The policy is intended to be consistent with and promote sound and effective risk management and to ensure that it does not encourage risk taking that exceeds the tolerated risk appetite of the Company.

A description of the different remuneration elements for 2016 is set out below.

<b>Base salary</b>	<p>Salaries are reviewed annually and are set to be market competitive taking into account the individual's skills, the size and scope of their role, and that of the Company.</p> <p>Salaries are set at such a level that employees are not overly dependent on variable pay and to allow the Company to operate a fully flexible bonus policy.</p>
<b>Benefits</b>	<p>The following benefits are offered to all permanent employees: Private health cover; annual travel insurance; interest free loans (up to £10,000) for season tickets; death in service life assurance; and participation in the Save As You Earn Plan.</p>
<b>Pension</b>	<p>All employees are eligible to participate in the stakeholder pension scheme. Employees who have reached their lifetime or annual allowance limit for pensions for tax purposes may receive a cash alternative in lieu of the Company's contribution that otherwise would have been made under the stakeholder pension arrangement.</p>
<b>Annual bonus</b>	<p>The annual bonus plan provides participants with an opportunity to receive a cash amount, subject to performance measured in respect of the relevant financial year. All employees may be invited to participate in the plan.</p> <p>Awards are based on the achievement of annual objectives. At all levels within the Company, individual performance metrics include compliance with standards relating to risk and compliance set by the Board. Other performance metrics assess alignment with the Company's core values, (and good conduct both within the firm and in dealings with customers). Typical measures that corporate performance may be assessed against include embedded value, profit, premium, expense management, risk management, customer service measures and conduct. No measures are judged on an exclusive basis.</p> <p>For staff in assurance functions, at least 75% of the maximum annual bonus award is based on the achievement of objectives related to the individual's assurance function. The remaining 25% will relate to the performance of the Company. Awards for this population are subject to a prevailing affordability underpin, and no bonuses will be paid if overall financial performance is not sufficient to fund awards.</p> <p>The bonus opportunity will be expressed as a percentage of salary, and will depend on an individual's role and responsibilities. The normal maximum annual bonus available is 100% of base salary, but may be amended at the determination of the RemCo.</p> <p>The CRO, with input from the Chairman of the BRC and the Chairman of the Audit Committee, assesses the financial performance of the year against the firm's risk appetite and behaviours and attitude to risk and compliance. If the performance has been achieved by exceeding the risk appetite of the firm, as stated and approved by the Board and the BRC, the bonus pool and/or individual outcomes may be adjusted downwards, potentially to zero.</p>
<b>Performance Share Plan ("PSP")</b>	<p>Under this plan selected senior individuals are invited, at the discretion of the RemCo, to receive share awards. These individuals are those tasked with delivering PICG's long-term strategic goals and generating long-term shareholder value.</p> <p>The awards, granted based on annual performance, vest over a three year period and have a further post-vesting retention period of up to three years. Awards vest at the end of the three year period if the embedded value of the Company is not less than it was at the beginning to ensure maintained growth. This plan is designed to align variable remuneration for senior management with the long-term interests of the Company, and meet the Solvency II requirements for at least 40% of variable pay for Solvency II Identified Staff to be deferred over three years.</p> <p>The size of awards granted to individuals upfront will be determined by the RemCo each year, based on an assessment of performance (individual and corporate) in the financial year prior to grant. This performance will include reference to the annual bonus performance assessment for the relevant financial year, although may include other factors the RemCo determines should be taken into consideration. The normal maximum annual PSP grant is normally 100% of salary, but may be amended at the determination of the RemCo.</p> <p>PSP awards include malus and clawback provisions which apply for four years from grant, in the event of any of the following:</p> <ul style="list-style-type: none"> <li>• a significant financial loss in, or material misstatement of the accounts of, the Company or any group company for any period that the Committee determines is relevant;</li> <li>• reasonable evidence of any act or omission by an individual which in the opinion of the Remuneration Committee: <ul style="list-style-type: none"> <li>– has contributed to material losses or serious reputational damage to the Company or any group company or business area; or</li> <li>– has amounted to serious misconduct, fraud or misstatement (whether by exaggeration of financial performance or mismarking the valuation of any asset or otherwise) so as to undermine the effective risk management or accuracy of the financial reporting of the Company or any group company.</li> </ul> </li> </ul>
<b>Legacy 2012 Growth Share Plan</b>	<p>During 2012, certain senior employees and Directors participated in legacy growth share arrangements put in place in 2012. These awards were based on growth in the value of PICG above a minimum level. These awards vested in October 2016.</p>

#### Link between pay and risk management

The Company's Remuneration Policy includes the following elements which are intended to align employees' reward to the Company's risk management:

- Maintaining an appropriate ratio between fixed and variable pay.
- Performance measures – Variable remuneration is subject to an assessment of financial and non-financial performance. Financial targets are set at a level consistent with the Company's risk appetite. For all employees, there is consideration of performance against risk and compliance criteria, thereby ensuring that there is risk adjustment at an individual level.
- Long-term incentives – Alignment with the long-term interests of the Company for senior management is achieved by the award of variable remuneration in shares for a three-year vesting period, followed by a post-vesting holding period of up to three years.
- Risk adjustment process – The RemCo, in formulating its recommendation on aggregate variable pay to the Board for approval, will review progress against strategic goals and financial targets, and seek input from the CRO and Chairman of the BRC and Chairman of the Audit Committee for an assessment of risk and compliance within established risk appetite limits as stated and approved by the Board and the Risk Committee. If the performance has been achieved out of line with risk appetite, the variable incentive pool may be adjusted downwards, including to zero.
- Malus and clawback provisions apply to all share-based variable remuneration paid to employees whereby awards may be reduced, withheld or reclaimed in certain circumstances, as outlined in the table above.
- For staff engaged in assurance functions, variable remuneration is mainly determined by reference to performance against functional/ individual performance. The RemCo signs off on all remuneration for senior assurance staff, ensuring independent review of achievements.

#### Material transactions during the reporting period

##### Transactions with Directors and key management personnel

During 2016, certain share based payment schemes operated by PICG in respect of employees of PSC have vested.

Ten of the key management personnel of the Group, including certain Directors, were participants in these schemes and received a total of 24,259,080 ordinary shares of PICG upon vesting in line with the scheme rules.

In addition, the Group settled tax liabilities on behalf of certain employees, including Directors and key management personnel, who exercised their options upon vesting of PSP. The settlement was made on the condition that the employees would repay this amount to the Group within 90 days after the end of the 2016/17 tax year. The Group recognised a loan asset of £1,112k due from the Directors and key management personnel at 31 December 2016. The loans do not bear any interest, and except for the repayment period, do not have any other condition attached to it. As at 31 December 2016, no repayments had been made and the full balance was outstanding.

#### Transactions with shareholders

The following share capital transactions took place during 2016:

##### Pension Insurance Corporation plc

The Company issued 150m £1 ordinary shares at par on 13 July 2016 and a further 93m £1 ordinary shares at par on 27 September 2016.

##### Pension Insurance Corporation Group Limited

The Company issued 128,869,501 £1 ordinary shares at £1.9388 on 2 June 2016 and a further 130,499 £1 ordinary shares at £1.9388 on 3 June 2016. Both share issues were fully paid and wholly subscribed for cash consideration. The issue of shares resulted in new share capital of £129m and share premium of £118m (net of £3m share issue costs).

Certain share based payment schemes operated by the Company have vested during the year. The Company issued 2,788,683 £1 ordinary shares at par on 13 June 2016 to satisfy the vesting of these awards.

On 21 October 2016, the Company passed a special resolution to reduce the Company's ordinary shares from 1,056,788,683 £1 ordinary shares to 1,056,788,683 ordinary shares each of £0.00161678179673884 nominal value. The resulting difference was credited to the capital reduction reserve.

On the same date, the Company passed an ordinary resolution to consolidate 446,500 £0.10 B shares into one £44,650 B share. Subsequently, one £44,650 B share was subdivided into 27,616,590 B shares each of £0.00161678179673884 nominal value. These B shares were then immediately converted into an equivalent number of ordinary shares.

#### B.2 Fit and proper requirements

PIC has in place procedures to ensure its staff are:

- (a) Fit – Their professional qualifications, knowledge and experience are adequate to enable sound and prudent management; and
- (b) Proper – They are of good repute and integrity.

In respect of each role PIC compiles a detailed job description including the roles competencies and required qualifications. Potential recruits are interviewed by people experienced in these areas and confirmation is obtained from external agencies that they have the qualifications claimed. References from previous employers are taken up if available.

PIC carries out CRB checks and also credit checks on all staff who are involved in finance, investments or administration or who are senior.

PIC also monitors staff throughout the year and review their performance by way of an appraisal. Staff are expected to keep up to date with relevant changes in applicable technical competencies and their Continuing Professional Development ("CPD") hours are recorded.

A list of the approved persons of the Company is held on the Financial Services Register website, maintained by the Financial Conduct Authority, and is available from the following link:

<http://www.fsa.gov.uk/register/firmIndivSearch.do?pageNumber=1&sid=173742&searchType=1&surname>

# B. SYSTEM OF GOVERNANCE (UNAUDITED)

CONTINUED

## B.3 Risk management system including the Own Risk and Solvency Assessment

PIC adopts a holistic enterprise-wide perspective on risk facilitated through a strong risk culture. The Company's ambition is to protect its obligations to policyholders and treat them fairly, whilst growing shareholder value through making better risk-return based business decisions resulting from a balanced awareness of the opportunities and threats, only taking risks that the Company has the capability to understand and manage.

PIC achieves this through linking its business strategy objectives and its approach to risk management through the key business processes operated, including setting the business plans, seeking new business opportunities, selecting investments and implementing risk mitigation techniques such as hedges and reinsurance.

The Company's Board and committee structure, and the "three lines of defence" model by which its internal control system operates, are more fully described in the "General information on the system of governance" section earlier.

The Board controls and monitors risk through the application of a risk governance framework, and through setting risk appetites and risk limits for the principal risk types to which the Company is exposed.

The Risk Appetite Framework ("RAF") considers the material risks to the business in the context of the achievement of its strategic objectives. As such, the RAF covers:

- Capital and liquidity requirements;
- The Company's reputation with customers, advisers and investors;
- Internal capacity and the capability to deliver on promises and plans;
- The corporate delivery of risk-adjusted growth in the value of the business; and
- The impact of changes in regulation and legislation.

PIC's risk management framework outlines how risks are identified, assessed, controlled and managed; and is organised as follows:



All employees relating to PIC have a responsibility to identify risks in their area, engage to ensure they are appropriately assessed and controls are put in place to manage the risks within the Company's risk appetite. The risks identified are documented, and a log is maintained known as the Risk Register.

The Risk Register contains all material risks. At least quarterly a formal assessment is carried out by the Management Risk Committee to ensure that all material risks are included. Furthermore, the Management Risk Committee reviews whether there has been a change in status of existing risks, and whether there are new and emerging risks that should be added to the Register.

Risks in the Risk Register are assessed by the CRO, with all material and quantifiable risks to which PIC is exposed over the coming year for which capital is an appropriate risk mitigating technique incorporated within PIC's Internal Model.

The Register is maintained by the CRO and is updated whenever a new risk is identified.

The regular BRC meetings receive details of key risks, as well as new and emerging risks that have been identified. Furthermore, the BRC receives an Internal Model dashboard which monitors trigger points at which the Internal Model may need to be reviewed to ensure the measurement of risks remains appropriate.

Those quantifiable and material risks for which capital is not held as part of their risk mitigation treatment or are expected to occur at a future date over the planning horizon, in excess of the 12 month horizon of the SCR calculation, are not included within PIC's Internal Model, and are instead measured by considering their impact as part of the stress and scenario testing programme; and also discussed in risk and solvency reports, such as the own risk and solvency assessment ("ORSA").

Non-quantifiable and material risks are also considered by measuring their impact as part of the stress and scenario testing programme; and also discussed in risk and solvency reports, such as the ORSA.



Of note, Conduct Risk is the risk that actions will have a detrimental effect on the Company's customers or will impact one of the FCA's other objectives relating to financial crime or competition. These risks often also fall across multiple risk categories.

The dimensions not best addressed through holding additional capital on the balance sheet, but through other risk management techniques, are outlined below.

#### **B.3.1 Liquidity risk**

PIC does not hold capital for liquidity risk but instead prefers to set a risk appetite limit for the amount of liquid assets that it needs to hold as PIC believes this to be a more appropriate approach to the management of this risk. PIC also uses a monthly liquidity stress test to check that the level of liquid assets can withstand a reasonable adverse scenario.

#### **B.3.2 Regulatory and legislative risk**

PIC does not hold capital against regulatory and legislative risk as management prefer to monitor this activity and do not see this as a risk that can be readily quantified. In the event that such a risk is likely to crystallise, the Board would meet to discuss the best way forward.

#### **B.3.3 Brand and reputation risk**

PIC does not explicitly hold capital for reputational and brand risks as the Company prefers to manage this with an appropriate governance structure. Reputational damage is most likely to reduce the quantum of future new business flows, which would have a beneficial effect on solvency, because new business generally consumes capital, whereas managing the in-force policies only over their lifetime generally releases capital.

#### **B.3.4 The annual ORSA process**

The annual ORSA process runs alongside the existing business strategy and business planning process. If there is a key decision or change which results in a business plan refresh being required, the ORSA process is re-run. Management has established triggers for when the business plan refresh may be required, which take account of PIC's risk profile and the volatility of its overall solvency needs relative to its capital position.

Within the annual ORSA process, the Board:

- Requests the commencement of the strategy, business planning and ORSA process;
- Challenges the strategy proposed by management;
- Establishes its preferences for taking various types of risks;
- Establishes the risk appetite and limit framework within which it wishes the strategy to be managed;
- Reviews and challenges the stress and scenario testing programme (including reverse stress tests) developed to support the ORSA; and
- Challenges the business plan and the associated ORSA report.

#### **B.3.5 Capital buffer**

In addition to managing the profile of its assets to meet the Company's objectives to ensure it can meet its obligations to policyholders and providers of capital in a timely manner, the Board determines its own view of the amount of capital it believes the business needs to hold.

The Board's assessment of the capital buffer held over the regulatory capital requirement serves to:

- provide an extra layer of security to policyholder benefits;
- provide an extra layer of security to debt investors;
- safeguard the franchise value for equity investors;
- act as a buffer against quantitative risks and absorb short-term balance sheet volatility, such as from credit spreads, interest inflation or exchange rate movements;
- act as a buffer against qualitative risks that do not readily lend themselves to statistical quantification but for which capital is an appropriate risk mitigant; and
- ensure financial flexibility by maintaining strong liquidity and access to a range of capital markets.

This assessment is based on an economic view of the business requirements, with the final assessment including consideration of other constraints such as regulatory requirements, external analyst perceptions, competitor positioning and pricing. Presently, this amount of capital is expressed as a buffer over the regulatory capital requirement which serves to define the overall capital needs. The Board reviews the capital buffer on an annual basis as a part of the review of the Risk Appetite.

The ranking and categorisation of risks for internal economic capital assessment and regulatory reporting through the use of an Internal Model is undertaken in a consistent manner.

#### **B.4 Internal control system**

The Board takes responsibility for the implementation of a comprehensive framework of controls across the Company supported by a continuous monitoring process to ensure that key policy objectives are met. Each committee reviews and oversees processes and procedures established by management to provide an appropriate control environment that supports the key processes for which the committee is responsible for oversight.

These processes and procedures encapsulate specific principles of the Internal Control Framework which are exercised in the operation of the Company's day-to-day activities in particular in the following areas:

- Staff recruitment, appraisal and training;
- Segregation of duties: The authorisation, custody, execution and record keeping for transactions is segregated between personnel;
- Authorisation of transactions;
- Retention of records;
- Physical safeguards;
- Performance reviews;
- Information security;
- Safeguarding and maintenance of data;
- Fraud detection;
- Reporting; and
- Re-performance

PIC's internal control framework is designed to provide reasonable assurance that the Company's activities are focused on ensuring the Company's objectives are achieved in an effective and efficient manner and with due regard to managing Conduct Risk. The daily control activities include approvals, reconciliations, management reviews, appropriate measurements applicable to each business area, physical access controls, compliance with agreed limits, and compliance with operating principles/instructions and procedures. The control activities should be proportionate to the risks stemming from the controlled activities and processes. They consist of a number of control activities which are deemed appropriate to the business and examples of their application are shown overleaf:

# B. SYSTEM OF GOVERNANCE (UNAUDITED)

CONTINUED

Control activity	Examples of application
<b>Existence:</b> Only valid or authorised transactions are processed and appropriate assets and liabilities recorded.	Reconciliation of records for assets held by external custodian to statements provided by independent third party investment managers to ensure assets held in custody match the expected holdings.
<b>Occurrence:</b> Transactions are correctly processed and recorded in the period to which they relate on a timely basis.	Controls over outsourcing arrangements to ensure pensions are paid and recorded in the correct month.  Premiums and liabilities recorded when the Company goes on risk for a specific scheme.
<b>Completeness:</b> All valid transactions are processed without omissions.	Checks to ensure all pensioners are paid each month. Outsourced pension administration function with agreed service standards. Monitored by management on a monthly basis and subject to regular review by Internal Audit.  Records for assets maintained by outsourced custodian are checked to ensure completeness and accuracy.
<b>Valuation:</b> The value of each transaction and balance in the Company's accounts is calculated using an appropriate methodology and is computationally accurate.	Investment valuation policy agreed with the audit committee. Consistently applied by third party custodians and reviewed by management.  The Head of the Actuarial Function and the audit committee review liability model and assumptions as set out in the Valuation Basis Paper for appropriateness.  Quotations for new business are priced appropriately and the effect on the Company's solvency and value are considered and approved before commitment.
<b>Security:</b> The Company's assets and data are held in a secure environment with adequate safeguards over misuse and misappropriation.	Fixed asset register maintained. Checks over physical existence performed. Reconciliation of investments in custody accounts at the custodian to third party confirmations from investment managers.  An Information Security Committee ("ISC") has been established with a mandate to ensure the security of all information held within the Company and specifically data that relates to our policyholders. The ISC reports to the CEO and Audit Committee on all information security matters and is the ultimate owner of the Information Security Policy. Further details are contained within the Company's data policy.
<b>Rights and obligations:</b> Assets and liabilities are properly recorded and valued. Assets represent the rights of the Company, and liabilities its obligations, as at a given date.	See above re custody of investments, fixed assets and calculation of insurance liabilities.
<b>Presentation and disclosure:</b> Components of financial statements (or other reporting) shall be properly classified (by type or account) and described appropriately.	Approval of financial statements, embedded value reports and regulatory returns by the audit committee. Audit trail from financial statements to internal management reports.
<b>Competence:</b> Staff employed by the Company have the skills appropriate to their role and responsibilities and are supported by a suitable training programme to augment their skills as necessary.	Established staff job descriptions for all roles.  Monitoring and support of staff to participate in CPD programmes.  Annual performance reviews.  Annual independent assessment of "fit and proper" person for all SIFs and critical finance functions as detailed in the Company's Fit and Proper Persons policy.
<b>Regulation:</b> The Company's affairs are conducted at all times in compliance with the rules of the regulatory bodies of which it is a member.	Established compliance function supported by staff training and regular monitoring of key parameters by which compliance is measured (e.g. treating customers fairly, breach reporting).

Control activity	Examples of application
<b>Risk:</b> The Company identifies and considers the operational and financial risks it runs in the course of managing its business and identifies and implements appropriate mitigating procedures.	<p>The Board set a risk framework for the Company which includes risk appetite and tolerance limits. Board Risk, Risk Management and Operational Risk Committees meet on a regular basis. Meetings are minuted and action points followed up by Chief Risk Officer and Operational Risk Manager.</p> <p>Hedging of assets and liabilities to minimise risk of mismatch of liquidity and exposures to inflation and interest rate movements.</p> <p>Risk of pensioners living longer than assumed when pricing schemes is mitigated by the use of longevity reinsurance swap and quota share arrangements on appropriate tranches of liabilities.</p>
<b>Continuity:</b> Business continuity plans are produced, maintained and regularly tested.	Latest disaster recovery test in February 2017, updated by quarterly departmental testing.

#### B.4.1 Compliance

The operation of the Company's internal control framework is supported by the Company's Compliance Function. The Compliance Function sits with the General Counsel of the Company, who reports to the CEO. The role of the Compliance Function includes advisory services to the business to support it in discharging regulatory obligations and managing conduct risk, to run processes to manage personal conflicts of interests including personal dealing, gifts and entertainment and outside business activities. The function also coordinates and delivers compliance training to PIC staff, management and the Board and is responsible for tracking regulatory developments and their impact on PIC. Furthermore, the function carries out a number of monitoring reviews across the business each year, liaising with the Risk Function, Internal Audit and the Head of the Actuarial Function to ensure each area is properly monitored, reporting findings to the Audit Committee. Compliance Monitoring programme forms part of the annual Integrated Assurance programme.

#### B.5 Internal audit function

The Head of Internal Audit is responsible for providing internal audit services supported by co-sourced specialist expertise as required. The purpose of internal audit is to provide independent and objective assurance that the governance processes, management of risk and systems of internal control are adequate and effective to mitigate the most significant risks, both current and emerging, that threaten the achievement of the organisation's objectives, and in doing so help improve the control culture of the Company. In addition, Internal Audit helps the Board and Executive Management to protect the assets, reputation and sustainability of the organisation.

The scope of Internal Audit activities encompasses but is not limited to the examination and evaluation of the adequacy and effectiveness of the organisation's governance, risk management and internal control processes in relation to the organisation's defined goals and objectives. The scope includes:

- Independent assessment of risk and the design and operational effectiveness of controls implemented to mitigate the risks identified. Including that the risk appetite has been established and reviewed through the active involvement of the Board and Executive Management. Internal Audit assesses whether risk appetite is embedded within the activities, limits and reporting of the organisation.
- An assessment of whether the information presented to the Board and Executive Management for strategic and operational decision making fairly represents the benefits, risks and assumptions associated with the strategy and corresponding business model.
- An assessment of the management of the organisation's capital and liquidity risks.

- An assessment of the adequacy and effectiveness of the Risk Management, Compliance and Finance functions. Effectiveness and efficiency of operations and employment of resources.
- Compliance with significant policies, plans, procedures, laws and regulations.
- Reliability and integrity of management and financial information processes, including the means to identify, measure, classify, and report such information.
- Safeguarding of assets.
- Assisting in the investigation of significant suspected fraudulent activities within the organisation and notify management and the Audit Committee of the results.
- Key corporate events such as the introduction of new products and services, outsourcing decisions and acquisitions/divestments to determine whether key risks are being adequately addressed and reported.
- The risk and control culture of the organisation.
- An evaluation as to whether the design and control of products, services and supporting processes deliver appropriate customer outcomes.
- An evaluation of the design and operating effectiveness of the organisation's internal governance, policies and processes, and that they are in line with the objectives, risk appetite and values of the organisation.
- Making objective and appropriate recommendations to improve the organisation's control environment and assist the business achieve their strategies.
- Focusing on not just the design and operation of business processes operated by management but also on the outcomes produced by the operation of such business processes.
- Reporting significant matters arising to Audit Committee and the Board.
- Providing assurance that issues raised are addressed and resolved to mitigate the risks reported on a timely basis.

Internal Audit adheres to the Institute of Internal Auditors ("IIA") requirements as set out in the IIA's "Code of Ethics" and "International Standards for the Professional Practice of Internal Auditing", and the Chartered Institute of Internal Auditor's ("CIIA") guidance, "Effective Internal Audit in the Financial Services Sector".

To provide for independence, Internal Audit reports functionally to the Chairman of the Audit Committee and administratively to the Chief Executive Officer. Financial independence, essential to the effectiveness of internal auditing, is provided by the Audit Committee approving a budget to allow Internal Audit to meet the requirements of this Policy.

# B. SYSTEM OF GOVERNANCE (UNAUDITED)

CONTINUED

Internal Audit is functionally independent and objective from the activities audited and the day-to-day internal control processes of the organisation, and shall be able to conduct an assignment on its own initiative, with free and unfettered access to people and information, in respect of any relevant department, establishment or function of the organisation, including the actions of outsourced activities.

Internal Audit is represented on, or has full access to, minutes and presentations to all of the major committees, so as to keep abreast of the Company's strategic direction, developments and risk/control breakdowns.

In addition to internal audit reports of activity and regular updates to committees and the Board, Internal Audit provides an annual written assessment of the adequacy and effectiveness of PIC's risk management, internal control and governance processes and systems. In addition, Internal Audit co-ordinates activity with other assurance functions as part of an "Integrated Assurance Approach", this includes agreeing a co-ordinated assurance plan, aligning audit and assurance work where relevant and completing integrated assurance reporting of thematic issues to committees and the Board.

## B.6 Actuarial function

The Company manages its actuarial function through a combination of internal and external resources. The role of Head of the Actuarial Function ("AFH") is outsourced to Mr Paul Whitlock, a senior qualified actuary employed by Willis Towers Watson. Mr Whitlock is supported by other Willis Towers Watson actuaries. The AFH reports to the Company's Chief Executive, and has direct access to the Board. The AFH attends the PIC Audit Committee and PIC BRC.

The AFH has no day-to-day management responsibilities within the Company, including in relation to the production of technical provisions or direct involvement in decisions relating to underwriting or reinsurance. The work of the AFH in these areas is supported by the in-house actuarial teams employed by PSC on behalf of the Company and working in the areas of regular financial reporting, longevity risk management and reinsurance, asset/liability management and actuarial aspects of new business development. These teams are responsible for the development of the underlying models, methodologies and assumptions, and operation of these on a day-to-day basis to produce technical provisions, capital requirements, new business pricing and associated management information. The AFH maintains regular close oversight of these activities through scheduled monthly meetings with the in-house actuarial team under the Company's internal Chief Actuary, at which each month end's valuation results and profit/loss attribution are discussed along with the projected short-term financial position of the Company, and by receiving regular information from other areas of the business including the Risk Function and other assurance functions.

In this way, the AFH is able to discharge the Actuarial Function's responsibilities under Article 48 of the Solvency II Directive and Article 272 of the Solvency II delegated acts relating to the co-ordination of the calculation of technical provisions, providing an opinion on underwriting policy and adequacy of reinsurance arrangements, and contributing to the effective implementation of the risk management systems.

## B.7 Outsourcing

PIC has a number of outsource providers, noting always that it maintains responsibility for the services they provide. The material functions which are outsourced are administration of policies, investment management, custodian services, and certain IT related services.

When choosing a material outsource provider, PIC's policy requires it to ensure the following issues are considered and documented in the legal arrangements between it and its chosen outsourcer:

- Ability, capacity, and authorisation
- Financial resources
- Staff
- Change management and future proofing
- Control framework
- Conflicts
- Rights and obligations
- Sub outsourcers
- Data protection
- Operational risks
- Authorisation
- Contingency plans
- Exit plans
- Cost

PIC also maintains sufficiently qualified staff to monitor the provision of these services and to carry out checks against the above areas and provide reports on their performance to the relevant Board Committee.

Depending on the function outsourced, the relevant Board Committee must approve the outsourcing or any material change to the outsourcing, of critical, important, or material functions or activities.

All proposals for outsourcing, or material changes to the outsourcing, of critical, important or material functions or activities are reviewed by the BRC who will recommend approval or otherwise to the Board.

PIC's compliance, risk and internal audit functions also carry out reviews throughout the year both of the outsource providers and also of the internal department that monitors the providers.

The Group's service company, PSC, provides all staff and certain services to PIC under the terms of a services agreement. The provision of these services is overseen by the Board. PSC charges to PIC during 2016 totalled £63m.

The following key functions and activities have been outsourced:

- Policyholder payroll and administration services to Mercer
- Head of Actuarial Function – Willis Towers Watson
- Tax advisory – PwC
- Payroll and other HR services to CBHC
- Custodian and investment accounting to JP Morgan
- Custodian and trade management to Northern Trust
- Asset management to Henderson Global Investors, JP Morgan and Schroders
- IT support to Endava

All of the outsourcers utilised are located within the EU.

## B.8 Any other information

### Adequacy of systems of governance

The Board continues to believe that the systems of governance operated by the Group and Company remain appropriate given the nature, scale and complexity of the risks inherent in the business.

# SOLVENCY AND FINANCIAL CONDITION REPORT

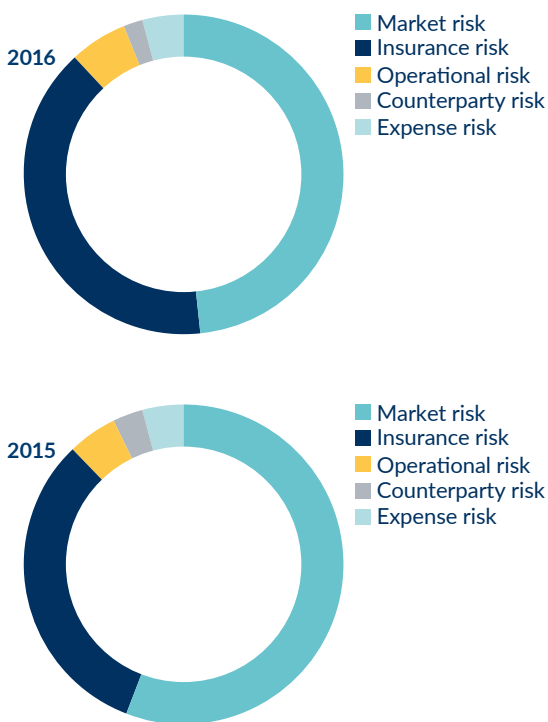
## C. RISK PROFILE (UNAUDITED)

The SCR for both PICG and PIC was £1.912bn as at 31 December 2016 (31 December 2015: £1.574bn), as measured by the Group's Internal Model.

In order of relative size of contribution to the SCR, the most important risks to the Company are:

- Market risk (see C.2)
- Insurance risk (see C.1)
- Operational risk (see C.5)
- Counterparty default risk (see C.3)
- Expense risk (see C.6)

This can be expressed graphically, as shown below:



The various components of the Risk profile are discussed in further detail below.

### C.1 Underwriting risk

Underwriting risk, classified internally as insurance risk, is the risk that mortality experience of the Company's policyholders is lighter than assumed, thus requiring pensions to be paid for a longer period than anticipated, resulting in a higher than expected cost to the Company.

In order to help minimise this risk and also uncertainty arising through future longevity experience, PIC adopts an active approach to reinsuring these risks where it is economic to do so. This reinsurance can be classified into two broad categories:

#### Longevity only reinsurance

Under these contracts, the Company has committed to pay the reinsurer a fixed line of cash flows for specified sets of liabilities relating to members/former members of particular pension schemes, based on an assumed future rate of mortality. The reinsurer undertakes to reimburse the actual cost of claims to the Company, based on the actual mortality of the reinsured lives. Separately, there is also an insurance fee for which the Company is liable. Settlement of the contract is on a net basis. These contracts also transfer the contingent longevity risk relating to any eligible dependents of relevant policyholders.

#### Longevity reinsurance via the transfer of assets

Under such contracts, in return for a single premium the reinsurer agrees to reimburse the actual cost of a defined portion of future claims to the Company in respect of an agreed set of policyholders. These contracts also transfer the contingent risks relating to eligible dependents of relevant policyholders.

The Company monitors the levels of its counterparty risk and actively seeks to reinsure with a range of providers to help mitigate its exposure to any one such entity.

One aspect of deriving overall best estimate longevity assumptions is to establish the "current" or "initial" rates of mortality. These assumptions are set by applying appropriate mortality factors to each individual member/policyholder. Individual variations are subject to a number of factors including, but not limited to, an individual's gender, age and pension amount.

The other aspect is the allowance for future improvements in mortality. The pattern in which mortality is expected to improve over time is an important but complex assumption for cash flow and liability calculations. This is regularly reviewed in the light of a number of factors including evolving methodologies for these projections together with views from industry and professional bodies on the factors driving mortality change.

### C.2 Market risk

The Company is exposed to market risk as a consequence of fluctuations in values or returns on assets and liabilities which are influenced by one or more external factors. These include changes in (and volatility of) interest rates, credit spreads, inflation expectations and currency exchange rates.

The Company manages market risk through an asset liability management ("ALM") framework that has been developed to closely match the investment portfolio duration and income to its obligations under insurance contracts.

Within the context of the ALM framework the Company uses derivative financial instruments to reduce market risk. Interest rate and inflation swaps are entered into to improve the matching of asset and liability cash flows, and ensure that risk driver sensitivities are aligned across the maturity spectrum. The quality of the interest rate and inflation matching strategies is carefully monitored by management, and is operated within tightly defined limits. Currency forwards and swaps are entered into to eliminate the majority of the currency risk on financial assets invested in non-sterling based debt securities where liabilities are denominated in sterling.

SOLVENCY AND FINANCIAL CONDITION REPORT  
**C. RISK PROFILE (UNAUDITED)**  
CONTINUED

**C.3 Credit risk**

Credit risk is the risk of loss due to the default of another party in performing its financial obligations to the Company. The Company is primarily exposed to credit risk through its investment in debt securities and cash deposits. Credit risk also arises in respect of derivative contracts to the extent that there is the potential for counterparties to default on their obligations.

The Company manages exposure to credit risk by placing limits on exposures to individual counterparties as well as groups of counterparties. Counterparty risk on derivatives is controlled through establishment of collateral agreements and master netting agreements on interest rate and currency swaps. To further minimise credit risk, the financial condition of counterparties is monitored on a regular basis.

**C.4 Liquidity risk**

Liquidity risk is the risk that the Company may not have sufficient liquid assets available at the right times to be able to pay its liabilities, despite the fact that it meets its regulatory solvency requirements. This would typically arise if derivative contracts to manage inflation and interest rates required collateral to be posted, a large proportion of deferred policyholders opted to take transfer values, or if a large proportion of assets were invested in assets which were not easy or straightforward to liquidate.

In order to manage this, projected cash flows for all new policy liabilities taken on are determined as a part of the new business origination process to identify the expected profile of liability payments, including expected mortality experience. This is then used to identify appropriate assets, which provide matching cash flows at an acceptable price.

The Company's risk policies define a minimum proportion of its assets to be held in highly liquid cash and gilts, and stress testing is conducted to ensure that there are sufficient liquid assets at all times to meet potential demands from derivative movements under extreme scenarios.

The projected cash flows are updated regularly, and assumptions are updated at least annually, taking into account factors such as mortality experience and how this affects the required cash flows in the future.

**C.5 Operational risk**

Operational risk is the potential for loss resulting from inadequate or failed internal processes, people and systems, or from external events. The Company's internal control processes are supported by an operational risk committee, the maintenance of a central risk register and an independent internal audit review. The risk of internal fraud is managed through a number of processes including the screening of staff at recruitment, a continuous training programme, segregation of duties and whistleblowing policies.

The Company has significant outsourcing arrangements in respect of pension administration and other functions. These arrangements are subject to agreements with formal service levels, operate within agreed authority limits and are subject to regular review by senior management.

Emergency and business continuity plans have also been established to counter adverse occurrences.

**C.6 Other material risks**

The only other risk category within the Internal Model not mentioned above is expense risk. This is the risk that the Company's expenses are higher than expected. This includes investment management expenses and policy maintenance expenses. Expenses are managed through a strict internal budgeting and monitoring process and through careful oversight of external investment managers and other outsourced service providers.

**C.7 Any other information**

The risk exposures highlighted above are the same in nature to those the Group was exposed to in the previous year. No material new risk exposures have been introduced during 2016.

# D. VALUATION FOR SOLVENCY PURPOSES

## D.1 Assets

### D.1.1 Assets: PIC

The value of each material class of assets of the Company for solvency purposes at the reporting date is as follows. The valuation basis used is the same for the solvency valuation as for the statutory accounts valuation.

31 December 2016	Solvency II value (£m)	Statutory accounts value (£m)	Valuation basis	Explanation of valuation difference
Property	97	97	Marked to market	
Bonds	20,662	20,662	Marked to market	
Investment funds	1,297	1,297	Marked to market/model	
Derivative assets*	10,733	9,320	Marked to market/model	Cross currency derivatives represented as net values under IFRS are included gross under Solvency II.
<b>Total investments</b>	<b>32,789</b>	<b>31,376</b>		
Loans and mortgages	554	554	Marked to market	
Reinsurance recoverables	1,590	2,523	Marked to model	Solvency II Regulations
Prepayments	48	48	Marked to market	
Receivables	40	40	Marked to market	
Cash and cash equivalents	248	248	Marked to market	
	<b>35,269</b>	<b>34,789</b>		

\* A presentational difference exists between IFRS and Solvency II in respect of certain derivative contracts, which are presented net for IFRS purposes and gross for solvency purposes. The overall value of derivative assets and liabilities is the same under both bases.

### D.1.2 Assets: PICG

The value of each material class of assets of the Group for solvency purposes at the reporting date is as follows. The valuation basis used is the same for the solvency valuation as for the statutory accounts valuation.

31 December 2016	Solvency II value (£m)	Statutory accounts value (£m)	Valuation basis	Explanation of valuation difference
Property	97	97	Marked to market	
Bonds	20,662	20,662	Marked to market	
Investment funds	1,297	1,297	Marked to market/model	
Derivative assets*	10,733	9,320	Marked to market/model	Cross currency derivatives represented as net values under IFRS are included gross under Solvency II.
<b>Total investments</b>	<b>32,789</b>	<b>31,376</b>		
Loans and mortgages	554	554	Marked to market	
Reinsurance recoverables	1,590	2,523	Marked to model	Solvency II Regulations
Prepayments	49	49	Marked to market	
Receivables	43	43	Marked to market	
Cash and cash equivalents	276	276	Marked to market	
Own shares held directly	1	-	Marked to model	Solvency II Regulations
	<b>35,302</b>	<b>34,821</b>		

\* A presentational difference exists between IFRS and Solvency II in respect of certain derivative contracts, which are presented net for IFRS purposes and gross for solvency purposes. The overall value of derivative assets and liabilities is the same under both bases.

### D.1.3 Asset recognition and derecognition

The basis for recognition and derecognition of financial instruments is as follows:

A financial instrument is recognised if the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Company's contractual rights to the cash flows from the financial assets expire, or if either the Company transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset are transferred to another party. Regular purchases and sales of financial assets are accounted for at the date of trading. Financial liabilities are derecognised when the Company's obligations specified in the contract expire or are discharged or cancelled.

# D. VALUATION FOR SOLVENCY PURPOSES

## CONTINUED

### D.1.4 Asset valuation basis

The general valuation basis applied to each material class of investments is as follows:

The fair values of investments quoted in an active market are based on their bid market prices. For unlisted securities and all other financial assets for which there is no active market, the Company establishes fair value using appropriate valuation techniques. These include the use of quoted prices, reference to other instruments that are substantially the same, and discounted cash flow analysis. These assessments are based largely on observable market data.

Where an active market does not exist for a financial instrument, the Company uses financial modelling to ascertain fair value. The models consider the anticipated future cash flows expected to be derived from the assets, and discount them to reflect the timing of payments and, for debt assets, the likelihood of default given the relative seniority of the holding in order of repayment.

#### Property (other than for own use)

Investments in freehold properties not for occupation by the Company are carried at fair value, which is calculated using discounted cash flow techniques on a mark to model basis. Refer to D.4 for more details.

#### Government and corporate bonds

The Group's and the Company's investments in government and corporate bonds are valued for Solvency II purposes on the same basis as the annual financial statements, which follow IFRS. The fair value of government bonds and the majority of corporate bonds is determined by reference to their quoted bid price at the reporting date.

Fair values of unlisted corporate bonds, such as bilateral investments, are determined as the present value of future cash flows, discounted at the market rate of interest at the reporting date. The details of the valuation method are provided in D.4.

The difference in valuation between IFRS and Solvency II relates to the allocation of accrued interest, which for the purposes of Solvency II has been included in the value of the bonds.

Assets valued on this basis are included in the tables above as "Bonds".

#### Collateralised securities

This asset class contains mortgage backed securities, other asset backed securities, and other collateralised securities.

The fair value of mortgage backed and other asset backed securities is determined by reference to their listed market price.

The fair value of the unlisted collateralised securities is determined using alternative valuation methods as described in D.4.

Assets valued on this basis are included in the tables above within the "Investment Funds" or "Loans and Mortgages" headings.

#### Collective investment undertakings

The fair value of collective investment undertakings is determined by reference to their quoted bid price at the reporting date where available.

Fair values of unlisted collective investments are calculated using alternative valuation methods as described in D.4.

Assets valued on this basis are included in the tables above within the "Investment Funds" or "Loans and Mortgages" headings.

#### Derivatives

Derivative financial instruments are measured at fair value.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. The fair values of foreign exchange forward contracts, futures and swaps are based on market prices. The difference in value above is offset by an equal and opposite difference in value on derivative liabilities (see section D.3), reflecting the different classifications used under the two bases.

#### Deposits other than cash equivalents, and cash and cash equivalents

The fair value of deposits held with credit institutions represents their cash value in current terms. All deposits are redeemable within three months and consequently no discounting adjustment is made at period end.

#### Reinsurance recoverables

As this asset is directly related to the regulatory technical provisions, the valuation is discussed in the technical provisions section D.2.

#### Prepayments and receivables

These assets are held at the values for which they could be exchanged between knowledgeable willing parties in an arm's length transaction, which is equivalent to the value for IFRS accounting purposes.

#### Own shares directly held

These assets are treated as a deduction from equity in the IFRS financial statements of PICG. For regulatory purposes, they are held as an asset and are marked to model in accordance with Solvency II regulations, using an estimate of the valuation of PICG as a whole. The amounts involved are considered not to be material.

#### Other assets

There are no other material tangible assets.

### D.2 Technical provisions

PIC writes only one line of business, i.e. bulk annuities in relation to UK defined benefit pension schemes. All of the Company's insurance liabilities represent contracts that provide immediate annuities for current pensioners and deferred annuities for members who have not yet reached pensionable age. Annuities are payable for the life of the policyholder, with in some cases a reversionary annuity paid to spouses or other dependants on the death of the main member.

Annuities in deferment and in payment can be level, subject to fixed increases or increases linked to inflation, or a mixture of the three. In many cases, the increases applied are also subject to defined caps and floors, so-called limited price indexation or LPI.

The insurance liabilities also include a limited number of member options, such as the option to commute part of the pension for a tax-free cash lump sum on vesting, the option to transfer deferred benefits to another pension scheme and the option to take early or late retirement. In these cases, the bulk of the options are set on a basis which is broadly financially neutral to the Company. There are no other material options and guarantees such as guaranteed annuity options.

The Company's insurance contracts are a mixture of "buy-in" policies, where the policyholder is the pension scheme and the insured liabilities cover defined benefits within the scheme, and "buyout" policies, where the policyholder is an individual.



### D.2.1 Technical provisions on regulatory solvency basis

The following table summarises the technical provisions of PIC as at 31 December 2016 on the regulatory solvency basis. The equivalent figures for 31 December 2015 are also shown.

Technical provisions, Solvency II basis (£m)	31 December 2016	31 December 2015 (unaudited)
Best estimate liabilities ("BEL")		
• Liabilities gross of reinsurance	<b>18,911</b>	14,654
• Value of reinsurance recoverables	<b>(1,590)</b>	(1,220)
• Net-of-reinsurance liabilities	<b>17,321</b>	13,434
Risk margin ("RM")	<b>2,176</b>	1,543
Transitional measures deduction ("TMTP")	<b>(1,270)</b>	(1,355)
Total net technical provisions	<b>18,227</b>	13,622

Technical provisions represent the value of policyholder obligations if these were to be transferred to a third party in an arm's length transaction at the valuation date. The technical provisions comprise a best estimate liability and a risk margin, reduced by the transitional measures deduction.

The total technical provisions, gross of reinsurance, as at 31 December 2016 were £19,817m.

There are no additional technical provisions maintained by the Group outside PIC.

### D.2.2 Valuation methods and assumptions for the solvency valuation

The principal methods and assumptions used in the valuation of the technical provisions for solvency purposes are as follows:

#### Valuation methodology for BEL:

For the vast majority of the business, the best estimate liability is calculated as the present value of future annuity and other benefit payments plus an allowance for future expenses. This calculation involves projecting each individual policy for its expected natural lifetime and discounting the resultant cash flows to the valuation date at the valuation discount rate, using methodology which confirms to the requirements of Section 3, subsection 1 (and in particular Articles 22 – 26) of Chapter III of the Solvency II Delegated Acts.

For a very small proportion of the best-estimate liabilities, approximate methods are used which are appropriate to the nature of the liabilities in question.

#### Valuation discount rate:

The discount rate used is derived from the basic risk free rate, which is taken as the swaps rate less the prescribed credit risk adjustment. For all of the business in force, this is increased by use of either a matching adjustment or a volatility adjustment as described below.

#### Mortality and demographic assumptions:

The base mortality assumptions as at 31 December 2016 inherent in the projected cash flows used in the valuation of insurance contract liabilities are set with reference to the S2 series of mortality tables published by the Continuous Mortality Investigation ("CMI", a research body with strong links to the Institute and Faculty of Actuaries in the UK).

The assumption for future improvements to mortality is modelled using the CMI 2012 table for improvements to the end of 2015 followed by the CMI 2014 table thereafter. The long-term improvement rate is assumed to taper from 2.6% p.a. at age 60 to zero at age 120 for both men and women.

Adjustments are applied according to a number of factors including, but not limited to, an individual's gender, age, pension amount, occupation and place of residence. In addition, an adjustment is made to allow for the risk of anti-selection.

Assumptions are also made in respect of the take-up rates on policyholder options, such as the option to take a pension contribution lump sum payment on vesting and certain early retirement options. For policyholder options where the observed take-up rates are very low and the financial impact is broadly neutral, no assumptions are applied in the actuarial valuation.

In addition other, less material assumptions are required for items such as the age difference between main members and spouses and proportions married, in cases where the relevant information is not available from the valuation data.

#### Inflation assumptions:

Assumptions for expected future Retail Price Index ("RPI") inflation are based on a curve derived from market prices of inflation-linked swap contracts. Assumptions for expected Consumer Price Index ("CPI") inflation are based on the RPI curve less a flat deduction. The projected liabilities for annuities linked to RPI or CPI use these curves.

The most common type of LPI – linked benefit is LPI(0,5), under which increases are capped at 5.0% and floored at zero, but a range of other types of LPI exist. These are not regarded as "options" in the sense that neither the policyholder nor the Company can elect to change the benefit, but are simply a special form of indexation. However, an option-based methodology is required to allow for the reserving and capital impacts of the caps and floors. PIC uses a mark-to-model approach to derive appropriate inflation curves for each LPI type to allow for the inherent optionality, as there is currently no deep and liquid market in appropriate swap contracts.

#### Expense assumptions:

The internal costs of maintaining the existing insurance contracts, the fees payable to third-party administrators engaged to manage payments due under the in-force policies, fees due to reinsurers, investment management expenses and certain specific project costs are factored into the calculation of liabilities by adding appropriate allowances, and include an estimate of the impact of future inflation where this is applicable. No allowances are included for expenses incurred by the Company in relation to the generation of new business.

#### Risk margin:

The risk margin is determined as the amount that would be required in addition to best estimate liabilities by a hypothetical third party (the "reference undertaking") taking on the Company's insurance obligations, to provide an amount of eligible Own Funds equal to the capital necessary to support those obligations over their future lifetime and assuming that all hedgeable risks had been eliminated.

The risk margin is calculated by estimating the SCR of the reference undertaking in each future year over the period in which the in-force business runs off. A cost-of-capital calculation is then performed using a prescribed rate of 6.0% per annum on each future year's estimated reference SCR, with the results discounted at the basic risk free rate.

## D. VALUATION FOR SOLVENCY PURPOSES

CONTINUED

The principal drivers underlying the estimate of reference undertaking's SCR are longevity risk, counterparty credit risk (with respect to reinsurance contracts and other material exposures), expense risk, and residual economic risk relating to inflation volatility, in particular LPI and the basis between RPI and CPI and operational risk. Longevity risk is assessed by considering separately the risk of mis-estimation of base mortality rates, future mortality improvement rates and other, less material influences on future demographic experience, and allowing for the mitigation afforded by existing reinsurance arrangements.

The projection of the reference SCR over the lifetime of the business is carried out by approximate means allowing for the expected changes in the size and relative impacts of the respective risk drivers as the in-force business continues to mature.

#### Transitional measures deduction on technical provisions (unaudited):

PIC applies a transitional measures deduction in respect of technical provisions (TMTP). The deduction, which is consistent with the requirements of Article 308d of the Solvency II directive, is expected to amortise linearly to zero over a 16-year period starting from 1 January 2016.

#### Uncertainty in the valuation of technical provisions:

The best estimate liabilities are calculated using data and assumptions which reflect the Company's best estimate of the position as at the valuation date. However, there are a number of uncertainties in the valuation. In particular:

- A key assumption is the rate of future policyholder mortality, which is expressed as a combination of a base mortality rate (reflecting the current observed experience) and a rate of future mortality improvements. Changes in these assumptions could have a material impact on the BEL calculation.
- For deferred annuity policyholders, assumptions have to be made about the extent to which certain options will be taken up prior to retirement. The most important option is the commutation of part of the pension benefit for a lump sum. While this take up is highly predictable based on past experience, there remains uncertainty as to whether future take-up rates will be as expected.
- The discount rate used in the valuation is determined allowing implicitly for an assumed level of future defaults arising in relation to the supporting assets. The allowance, which is stipulated by EIOPA, may not be a good representation of the actual level of defaults arising in practice, and variations in experience (positive or negative) will arise as a result.
- A significant proportion of the annuity benefits escalate in line with defined inflation indices. A range of indices applies including CPI and LPI linkages, and assumptions have to be made as to how these indices will relate to the standard retail prices index going forward.
- The expenses allowed for in the valuation are based on the Company's view of its likely expense outgo required to manage the business in force. Variations in these expense levels and in the impact of inflation of these expense levels also introduce uncertainty.

In addition, projection of the run-off over time of the reference SCR used in the risk margin calculation requires a significant degree of judgement, given the length and nature of PIC's annuity liability cash flows.

#### D.2.3 Use of matching adjustment

In December 2015, PIC was granted permission by the PRA to apply a matching adjustment in relation to the value of its insurance liabilities. PIC applied the matching adjustment to all of its annuity-in-payment and deferred annuity policy liabilities as at 31 December 2016.

The assets used comprise a mixture of UK government bonds and UK and overseas corporate bonds, together with a relatively small amount of cash and cash equivalents, loans and mortgages and property assets. In addition, the assets include derivatives designed to transform overseas cashflows to sterling, and to transform floating rate cashflows to fixed rates. All of the assets, once transformed through the use of appropriate derivatives, meet the requirements of Article 77b(1) of the Solvency II Delegated Acts.

PIC holds all assets and liabilities for which the matching adjustment applies in a clearly ring-fenced fund, the MA Fund. The matching adjustment calculation relies on close matching of the asset cash flows and the liability cash flows in this fund. In making this assessment, the liability cash flows are the net-of-reinsurance best estimate liability cash flows for the business taken from the Company's liability projection model, and the asset cash flows are the aggregate of the cash flows on each individual asset adjusted for the default component of the "fundamental spread" to allow for the credit risks retained by the Company.

The initial matching adjustment is then calculated as a difference between two annual effective internal rates of return, i.e. (a) the flat discount rate which, if applied to the liability cash flows, would equate these to the market value of the matching assets; and (b) the flat rate which, if applied to the liability cash flows, would equate these to the value of those liability cash flows calculated using the basic risk-free rate curve.

The matching adjustment is then further adjusted for the cost-of-downgrade component of the fundamental spread.

The assets in the MA Fund used in the matching adjustment calculation can be summarised as follows:

MA Fund assets (£m)	31 December 2016
Property	84
Government bonds	6,950
Corporate bonds	12,378
Derivative assets	1,664
Loans and mortgages	518
Cash and cash equivalents	175
Total assets	21,769
Less derivative liabilities	(4,439)
Net value of assets	17,330

PIC maintains close control of the asset and liability cash flow matching in order to ensure that at all times it can meet the requirements of Article 77(b)(i)(c) of the Solvency II Delegated Acts. In addition, PIC monitors the asset and liability matching of the MA Fund against the three specific tests required by its local regulator, the PRA. As at 31 December 2016, all of the PRA test results were within the required limits.

As at 31 December 2016, the impact of not applying the matching adjustment but instead valuing the liabilities using the basic risk-free curve would have been as follows:

Impact of matching adjustment (£m)	Including matching adjustment	Excluding matching adjustment	Impact of not applying MA
Solvency II Own Funds available to meet SCR	3,134	(38)	(3,172)
SCR	1,912	4,665	2,753
<b>SCR Excess assets</b>	<b>1,222</b>	<b>(4,703)</b>	<b>(5,925)</b>
Solvency II Own Funds available to meet MCR	2,636	(1,047)	(3,683)
MCR	478	1,166	688
<b>MCR Excess assets</b>	<b>2,158</b>	<b>(2,213)</b>	<b>(4,371)</b>

#### D.2.4 Use of volatility adjustment

In December 2015, PIC was granted permission by the PRA to apply a volatility adjustment in relation to the value of its insurance liabilities.

As at 31 December 2016, all the business in force was eligible for use with the matching adjustment and was held within the MA Fund. An immaterial amount of liabilities was held outside the matching adjustment fund and valued using the volatility adjustment.

The impact of not applying the volatility adjustment to these liabilities but instead valuing them using the basic risk-free curve would be to increase the net-of-reinsurance technical provisions by £469,000. There would have been no impact on either the SCR or the MCR.

#### D.2.5 Use of transitional measures adjustment

PIC does not apply any adjustment to the risk-free interest rate term structure referred to in Article 308c of Directive 2009/138/EC.

In December 2015, PIC was granted permission to apply a transitional measures deduction to technical provisions (TMTP) in accordance with Article 308d of Directive 2009/138/EC.

PIC calculated the TMTP as at 31 December PIC 2015 as £1,355m. This amount, which is gross of any deferred tax impacts, has since been amortised on a 16-year basis to £1,270m. The impact of deferred tax is to reduce the benefit of the TMTP on Own Funds, but also to reduce the SCR by increasing the loss absorbing capacity of deferred tax. PIC has not recalculated the TMTP to date, but expects to do so no later than 31 December 2017 in line with the PRA's published expectations for UK life insurers.

As at 31 December 2016, the impact of not applying the TMTP would have been as follows:

Impact of TMTP (£m)	Including TMTP	Excluding TMTP	Impact of excluding TMTP
Solvency II Own Funds available to meet SCR	3,134	2,079	(1,055)
SCR	1,912	2,087	175
SCR Excess assets	1,222	(7)	(1,229)
<b>Solvency ratio based on SCR</b>	<b>164%</b>	<b>100%</b>	
Solvency II Own Funds available to meet MCR	2,636	1,549	(1,087)
MCR	478	522	44
MCR Excess assets	2,158	1,027	(1,131)
<b>Solvency ratio based on MCR</b>	<b>551%</b>	<b>297%</b>	

#### D.2.6 Reinsurance arrangements

PIC seeks to limit its exposure to longevity risk by entering into reinsurance arrangements with third party reinsurers. As at 31 December 2016, approximately 68% (as measured by best-estimate liabilities) of the longevity risk was reinsured (2015: 71%).

PIC has entered into two types of reinsurance arrangements:

- Longevity swap arrangements, whereby PIC pays to the reinsurer a fixed, agreed stream of annuity benefit cash flows, together with a defined reinsurance fee, and the reinsurer pays PIC annuity benefits based on the actual mortality experience of the lives in question. All of the longevity swap arrangements are similar in nature. PIC has entered into these arrangements with six reinsurers. The total net value of the longevity swap asset, excluding the fees payable to the reinsurers, was £100m as at 31 December 2016.
- Quota share reinsurance arrangements, whereby in return for an up-front single premium PIC will receive from the reinsurer a percentage share of a defined sub-set of the annuity liabilities paid out in future. PIC has entered into these arrangements with two reinsurers. The total value of the quota share reinsurance asset was £1,524m as at 31 December 2016.

The value of the amounts recoverable from reinsurance is calculated using the same projection model and assumptions as are used for the gross best estimate liabilities, by projecting forward both the payments due to reinsurers and the payments expected from reinsurers, in each case calculated on a policy-by-policy basis.

The value of the reinsurance recoverables is reduced by a counterparty default adjustment of £42m, which is calculated by applying (for each reinsurer) an assumed probability of default to an estimated loss given default, allowing for an assumed rate of recovery, measured over the lifetime of the reinsurance contracts in question.

In addition, there is a recoverable amount of £7m in respect of a small tranche of annuities where PIC has undertaken inwards reinsurance.

Therefore, the total value of the reinsurance recoverables asset is £1,590m.

PIC does not have any arrangements with special purpose vehicles in respect of its gross or net liabilities.

#### D.2.7 Review of valuation methods and assumptions

PIC reviews its technical provisions valuation assumptions and methodology regularly to ensure that they are fit for purpose and meet the requirements of Section 3.1 of Chapter III of the Solvency II Delegated Acts.

For the purposes of the valuation as at 31 December 2016, no material changes were applied to the methodology used in the calculation of the technical provisions. A number of changes were made to the assumptions used in order to reflect emerging experience better – the most material of these changes were in respect of the margin between CPI and RPI inflation, the anti-selection adjustment for deferred lives taking up pensions at retirement, the rates of commutation of pension at retirement and investment management fees. In aggregate, the assumption changes applied reduced technical provisions by around £98m.

In addition, the valuation assumptions were updated to reflect current expectations of future interest rates and inflation rates, and to reflect the changes to the prescribed fundamental spread assumptions underlying the derivation of the matching adjustment.

# D. VALUATION FOR SOLVENCY PURPOSES

CONTINUED

## D.2.8 Valuation methods and assumptions for the financial statements

Apart from the valuation discount rate, the methods and assumptions used to value the technical provisions for the purposes of the financial statements are derived from the same best-estimate assumptions as are used in the valuation for solvency purposes. To these assumptions, prudential margins are added – these margins are consistent with those previously used under the regulatory regime which preceded the introduction of Solvency II. PIC's practice at the time was to use the same margins in the calculation of its technical provisions for the purposes of the financial statements as in statutory reporting, and for this reason PIC is satisfied that the basis used continues to meet the relevant requirements of IFRS.

As the impact of applying these prudential margins is to change the cash flow profile of the liabilities, it is not possible simply to use the same matching asset profile as is used for the best-estimate liabilities. Instead, PIC notionally hypothecates a basket of assets for backing the liabilities and calculates the valuation rate of interest using a "portfolio IRR" approach which considers the yield for the whole basket. Using this approach, PIC is able to take into account both the level of the risk-adjusted yields on the assets and the terms over which the returns would be received.

The projected asset cash flows are also adjusted to allow for credit risk to take account of the specific rules on risk-adjustments to asset yields and reinvestment rates that applied under the regulatory regime which preceded the introduction of Solvency II. Using this methodology, the valuation rate of interest derived for the valuation for the financial statements was LIBOR swaps plus 76 bps, equivalent to a flat rate of 2.11% p.a. (2015: 2.95%).

The impact of applying the prudential margins is summarised in the following table, which shows the transition from the Own Funds under Solvency II to the IFRS net assets presented in the Company's financial statements. The equivalent figures as at 31 December 2015 are shown for comparison.

Reconciliation between Solvency II and IFRS technical provisions balance sheets (£m)	31 December 2016	31 December 2015 (Unaudited)
Solvency II technical provisions (gross or reinsurance)	19,817	14,842
Less:		
• Value of reinsurance recoverables on Solvency II basis	(1,590)	(1,220)
Solvency II technical provisions (net of reinsurance)	18,227	13,622
Less:		
• Risk margin	(2,176)	(1,543)
• Transitional measures deduction	1,270	1,355
Solvency II best estimate liability (net of reinsurance)	17,321	13,434
Add:		
• Impact of valuation discount rate margin	1,031	610
• Impact of other IFRS valuation margins	867	519
IFRS technical provisions (net of reinsurance)	19,219	14,563
Add:		
• Value of reinsurance recoverables on IFRS basis	2,522	1,917
IFRS technical provisions (gross of reinsurance)	21,741	16,480

## D.3 Other liabilities

Other liabilities at 31 December 2016 reflect derivative liabilities, deferred tax and accounting accruals and creditors, as follows:

	2016 IFRS value		2016 Regulatory value	
	Group £m	Company £m	Group £m	Company £m
Derivative liabilities	10,653	10,653	12,066	12,066
Insurance and other payables	101	89	89	76
Deferred tax	4	4	175	175
Subordinated debt instruments	542	542	594	594
<b>Other liabilities</b>	<b>11,300</b>	<b>11,288</b>	<b>12,924</b>	<b>12,911</b>

Other than as noted below, other liabilities are valued at fair value for the purposes of solvency rules, which is equivalent to the IFRS values in the Group's and Company's financial statements. There are no significant estimates or judgements in the valuation of these liabilities.

### D.3.1 Derivative liabilities

This represents the liability valuation, at fair value, of derivatives held by the Company for managing its currency, interest and inflation exposures. These are 'level 2' valuations for IFRS purposes, and the value of overall derivative assets and liabilities is the same under IFRS as under Solvency II. The difference in value above is offset by an equal and opposite difference in value on derivative assets (see section D.1), reflecting the different classifications used under the two bases.

### D.3.2 Insurance and other payables

This represents amounts payable, at fair value, relating to sundry business creditors and accruals, current taxation payments due and reinsurance fees payable. These items are payable within the next year. Given the short timescales, no discounting has been applied.

### D.3.3 Deferred tax liabilities

A deferred tax asset or liability is recognised to the extent that there is a temporary difference between the Company's tax base balance sheet (which is IFRS) and the balance sheet for Solvency II purposes. At 31 December 2016, this resulted in a deferred tax liability of £175m (including a deferred tax liability of £4m held on the IFRS balance sheet, relating to transitional arrangements on the UK Life tax regime).

At 31 December 2016, an unrecognised deferred tax asset of £2,879,000 existed within the Group, representing an estimate of the potential future tax deduction available on vesting of existing share incentive schemes.

There are no other unused tax losses or unused tax credits for which no deferred tax asset or liability has been recognised on the balance sheet.

### D.3.4 Subordinated debt instruments

For regulatory purposes, the subordinated debt instruments issued by the Company are valued in accordance with Article 75 of Directive 2009/138/EC, taking no adjustment to take account of the own credit standing of the Company. This differs from the valuation used for IFRS accounting purposes, where the subordinated debt instruments are valued at amortised cost.

In addition, the subordinated debt instruments are treated as liabilities for the purposes of IFRS accounting: for the purposes of regulatory accounting, whilst they are shown on the balance sheet (S.02.01) within liabilities, they form a part of the Own Funds of the Company (S.23.01).

The subordinated debt instruments fall due in 2024 (£300m face value) and 2026 (£250m face value).

#### D.3.5 Reconciliation between regulatory value and financial statements value of other liabilities

At 31 December 2016, differences between the value of other liabilities for regulatory reporting and IFRS financial statements arise as follows:

	2016	
	Group £m	Company £m
<b>Regulatory solvency "other liabilities"</b>	<b>12,924</b>	<b>12,911</b>
Reduction in derivative liabilities (included within derivative assets for IFRS purposes)	(1,413)	(1,413)
Reduction in subordinated debt valuation (held at amortised cost for IFRS purposes) and removal of associated accrued interest.	(40)	(40)
Deferred tax (as above)	(171)	(171)
<b>Other liabilities under IFRS</b>	<b>11,300</b>	<b>11,288</b>

#### D.3.6 Leases and contingent liabilities

PIC does not have any material liabilities in respect of leases, or contingent liabilities.

PICG does not have any material contingent liabilities. The Group has an operating lease for the floors of 14 Cornhill which it occupies. Future payments totalling £16m, will fall due over the coming eight years. There are no other material lease arrangements.

#### D.3.7 Employee benefits

The Company pays expenses to a service company owned by the Group holding company, which funds employee benefits.

There are no defined benefit obligations in connection with employees.

#### D.4. Alternative methods for valuation

The Group and the Company use alternative valuation methods, as defined in the Solvency II Regulations, to determine the fair values of certain investments as explained in section D.1.4. Given the methodology used below is the same as the one used to value the investments for IFRS purposes, no differences arise between IFRS and Solvency II values, except for the accrued interest, which is allocated to the individual security under Solvency II.

The details of these alternative valuation methods are provided below; the values shown represent the fair value for the assets where alternative methods for valuation have been used.

#### Property (other than for own use) – £97m

Fair value of the properties are determined annually by professional external valuers using the Royal Institution of Chartered Surveyors ("RICS") guidelines. The RICS guidelines apply separate assumptions to the value of the land, buildings and tenancy associated with each property.

The external valuers also consider changes in market conditions and the status of the tenants in determining whether a full physical inspection is required each year. Irrespective of such considerations, each property is fully inspected periodically as part of the valuation process. The cost of additions and renovations is capitalised and considered when estimating fair value.

The main inputs used in the valuation model relate to the rental income, property's tenure, location, lease length and other factors specific to each property.

Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific property.

#### Unlisted corporate bonds (bilateral investment) – £1,660m

Under both IFRS and Solvency II, unlisted corporate bonds are valued using discounted cash flow techniques on a mark to model basis. The models consider the anticipated future cash flows expected to be derived from the assets and discount them to reflect the timing of payments and the likelihood of default given the relative seniority of the holding in order of repayment. The discount rate is derived based on the credit spreads observed on other, quoted instruments that are substantially the same.

#### Unlisted collateralised securities – £68m

The fair value of unlisted collateralised securities is calculated using discounted cash flow techniques on a mark to model basis.

The valuation models use the security specific observable (interest rates and yield curves) and unobservable (implied volatilities, loss given default) inputs.

The unobservable inputs reflect the assumptions market participants would use in pricing the asset or liability based on sources independent of the entity pricing the asset or liability.

In addition, unobservable inputs are developed based on the best information available relating to a particular security and can be adjusted if information indicating that market participants would use different assumptions is reasonably available without undue cost and effort or when corroborated by evidence such as market transactions or quoted prices of other similar securities where available.

#### Unlisted collective investment undertakings – £46m

The fair value of unlisted collective investments is determined using the discounted cash flow method, which calculates the present value of future cash flows, discounted at the market rate of interest at the reporting date. The main inputs used in these calculations relate to interest rates, which are market observable.

#### Own shares held directly – £1m (PICG)

This is determined using a modelled valuation of the PICG Group, derived from its audited Market Consistent Embedded Value at the valuation date.

#### D.5 Any other information

There is no other material information to disclose regarding the valuation of assets and liabilities for solvency purposes.

# SOLVENCY AND FINANCIAL CONDITION REPORT

## E. CAPITAL MANAGEMENT

### E.1 Own Funds

#### E.1.1 Objectives, policies and processes

The objectives, policies and processes employed by the Group and Company to manage its Own Funds are set out in its Capital Management Policy, which is approved by the Company's Board.

As a part of this, the Board ensures that a Medium Term Capital Plan is prepared on an annual basis for approval as part of the overall Business Planning cycle. The Medium Term Capital Plan covers at least a five year period, and includes consideration of the need for further Own Funds, the type of Own Funds, repayment of any Own Funds and Dividend/Distribution Policy.

The Company's regulatory solvency ratio (measured as its SCR divided by its eligible Own Funds) is a key metric in the management of the financial position of the Company and Group.

The Board has a risk appetite limit and tolerance for the Company's solvency level, and monitors this regularly. Where solvency is above 140%, no formal action is deemed necessary. Where solvency is between 130% and 140%, information should be provided to the Board explaining the current solvency level and its outlook, together with information on the actions that can be taken if required. Where solvency falls below 130% of SCR, action should be taken to rectify the position.

As a part of its day-to-day management of the Company's solvency position, management employs solvency monitoring techniques and measurements which are run at a minimum weekly, or more often where required. Management is also able to employ various techniques to manage its capital and solvency, including (but not limited to):

- Managing the type and volume of new business written;
- Reinsurance of existing business;
- Risk mitigation techniques;
- Hedging strategies to manage key exposures such as credit risk, interest rate risk or inflation risk;
- Efficient asset management strategy; and
- Seeking further external debt or equity capital.

#### E.1.2 Own Funds at the reporting date

The amount of Own Funds of the Group and Company at the end of the reporting period was:

2016 (£m)	Group				Company			
	Tier 1	Tier 2	Tier 3	Total	Tier 1	Tier 2	Tier 3	Total
Balance at 31 December 2016	2,560	594	-	3,154	2,540	594	-	3,134
Amount of basic Own Funds available to cover SCR	2,560	594	-	3,154	2,540	594	-	3,134
Amount of basic Own Funds available to cover MCR	2,560	96	n/a	2,656	2,540	96	n/a	2,636

As at 31 December 2016, the ratio of eligible Own Funds to SCR of PICG was 165% (31 December 2015: 152%) and of PIC was 164% (31 December 2015: 151%).

There are no items of ancillary Own Funds at 31 December 2016.

No restrictions have been made to the amounts of basic Own Funds which can be used to cover the Company's SCR requirement.

For the purposes of MCR coverage, the amount of Tier 2 basic Own Funds which can be used to cover MCR has been restricted to £96m (or 20% of the MCR amount). In the event that any Tier 3 basic Own Funds items were held by the Group, no Tier 3 basic Own Funds could be used to provide MCR coverage.

#### E.1.3 Reconciliation of opening and closing Own Funds

##### E.1.3.1 Reconciliation of opening and closing Own Funds: PICG

2016 (£m)	Tier 1			Tier 2	Total
	Share capital	Share premium	Reconciliation reserve	Subordinated debt	
At start of year	925	-	1,136	325	2,386
Issued in year	129	-	-	250	379
Movements in year	(1,052)	118	1,304	19	389
<b>At end of year</b>	<b>2</b>	<b>118</b>	<b>2,440</b>	<b>594</b>	<b>3,154</b>

### E.1.3.2 Reconciliation of opening and closing Own Funds: PIC

2016 (£m)	Tier 1		Tier 2	Total
	Share capital	Reconciliation reserve	Subordinated debt	
At start of year	757	1,288	325	2,370
Issued in year	243	-	250	493
Movements in year	-	252	19	271
<b>At end of year</b>	<b>1,000</b>	<b>1,540</b>	<b>594</b>	<b>3,134</b>

### E.1.4 Restrictions to Own Funds and capital tiering

No restrictions have been made to the amount of basic Own Funds available to cover the Company's SCR as a result of the impact of limits on eligible Tier 2 and Tier 3 capital, and on restricted Tier 1 capital.

The Company's Tier 2 capital consists of £300m nominal of subordinated loan notes due 2024 with a fixed coupon of 6.5% paid annually in arrears that were issued at 99.107% of par in July 2014, and £250m nominal of subordinated loan notes due 2026 with a fixed coupon of 8% paid annually in arrears that were issued at 98.916% of par in November 2016. The notes represent direct, unsecured and subordinated obligations of the Company, and are classified as qualifying dated Tier 2 securities for the purposes of regulatory capital requirements.

The Tier 2 instruments are valued in accordance with Article 75 of Solvency II directive, being economic value, and therefore at a different value than that used in the Company's IFRS financial statements. Changes arising from movements in the risk-free rate between the dates of issue (3 July 2014, 23 November 2016) and the reporting date have led to an increase in the value of the subordinated debt (including accrued interest) of £40m. The difference in value between the two bases is offset by an equal and opposite amount included within the Reconciliation Reserve.

The Tier 2 instruments are classified as Tier 2 Capital, in line with Solvency II requirements, as opposed to financial liabilities, as classified in the Company's IFRS financial statements.

### E.1.5 Reconciliation of Own Funds to IFRS Equity

The following differences exist between Equity as shown in the Company's IFRS Financial Statements at the reporting date, and Own Funds under regulatory classifications:

£m	Group		Company	
	2016	2015 (unaudited)	2016	2015 (unaudited)
<b>Equity per IFRS financial statements</b>	<b>1,779</b>	1,312	<b>1,760</b>	1,296
Add: Reclassification of subordinated debt as Tier 2 capital for regulatory purposes, included at regulatory value	<b>594</b>	325	<b>594</b>	325
* Adjustment of subordinated debt value between IFRS and regulatory value	<b>(40)</b>	(21)	<b>(40)</b>	(21)
* Decrease in technical provisions under regulatory rules	<b>1,925</b>	1,639	<b>1,925</b>	1,638
* Increase in deferred tax liability under regulatory rules	<b>(171)</b>	(171)	<b>(171)</b>	(171)
* Decrease in reinsurance recoverable asset under regulatory rules	<b>(933)</b>	(697)	<b>(934)</b>	(697)
<b>Own Funds per regulatory requirements</b>	<b>3,154</b>	2,387	<b>3,134</b>	2,370

Items marked with a "\*" above form part of the regulatory Reconciliation Reserve (see E.1.6 below), which totals £1,540m for PIC, and £2,440m for PICG at 31 December 2016.

There are no restrictions on the availability and transferability of Own Funds within the Company or Group.

### E.1.6 Constituents of reconciliation reserve

The reconciliation reserve at 31 December 2016 is formed of the following elements:

£m	Group	Company
IFRS retained earnings per financial statements	605	699
Capital contribution reserve per financial statements	-	60
Capital reduction reserve per financial statements	1,055	-
Differences between IFRS rules and Solvency II rules (marked with "*" above)	781	781
Treasury shares per financial statements	(1)	-
<b>Reconciliation reserve at 31 December 2016</b>	<b>2,440</b>	<b>1,540</b>

# SOLVENCY AND FINANCIAL CONDITION REPORT

## E. CAPITAL MANAGEMENT

### CONTINUED

#### E.2 SCR and MCR (Unaudited)

As at 31 December 2016, PICG's and PIC's SCR amounted to £1,912m, and its MCR amounted to £478m.

The SCR was calculated using an internal model which was agreed by the PRA in December 2015 – other than updating for changes in economic conditions and other natural business movements, no changes were made to this internal model during 2016. PIC is therefore satisfied that the SCR as at 31 December 2016 is not subject to supervisory assessment.

No adjustment to the SCR has been made by the PRA, in respect of the third subparagraph of Article 51(2) of Directive 2009/138/EC.

Over 2016, the SCR has increased from £1,574m to £1,912m, and the MCR has increased from £394m to £478m.

The principal reasons for the increases in these items are:

- A general increase in the volume of business in force, due to insurance contracts written during 2016;
- The impact of changes in economic conditions over the year, in particular the reduction in interest rates; and
- The impact of the reinsurance programme effected by the Company, which has served to reduce the insurance risk element of the SCR.

These reasons reflect the natural progression of the business. There have been no material changes to the underlying methodology or assumptions used on the calculation of either item.

#### E.2.1 Components of SCR

PIC uses an internal model agreed with the PRA to calculate its SCR. It does not apply the Standard Formula in the business.

The split of the SCR by risk category as at 31 December 2016 is summarised in the following table. The equivalent amounts as at 31 December 2015 are provided for comparison.

Summary of SCR as at 31 December 2016 (£m)	31 December 2016	31 December 2015
Risk capital before diversification:		
– Market risk	1,524	1,410
– Counterparty credit risk	64	82
– Insurance risk	1,227	795
– Expense risk	115	90
– Operational risk	171	135
<b>Total before diversification</b>	<b>3,101</b>	2,512
Diversification benefit	(959)	(740)
Loss absorbing capacity of deferred tax	(230)	(198)
<b>Total diversified SCR after LACDT</b>	<b>1,912</b>	1,574

#### E.2.2 Key inputs for the calculation of the MCR

The MCR has been calculated as follows:

1. The higher of 2.1% of the value of best-estimate liabilities net of reinsurance recoverables and 25% of the SCR
2. The lower of the result from Step 1 and 45% of the SCR.

#### E.3 Use of the duration-based equity risk sub module in the calculation of the SCR

This section is not applicable to PIC & PICG. PIC and PICG do not use the duration-based equity risk sub-module.

#### E.4 Difference between the Standard Formula and any internal model used (unaudited)

The Internal Model is used to calculate PIC's regulatory capital requirements. The output from the Internal Model also helps support strategic decision making including in the following areas:

- Business planning
- Pricing of new business
- Asset allocation
- Reinsurance transactions and hedging activities

PIC uses a full Internal Model.

PIC uses a variety of methods to calculate the probability distribution forecast and the SCR, ranging from statistical analysis of historic data (e.g. market risk) to expert judgements determined by panels of experts (e.g. insurance risk). Each method is appropriate to the particular risk in question.

PIC's Internal Model methodologies and assumptions use a more bespoke and granular approach than the "one-size-fits-all" approach underpinning the Standard Formula. The main differences are as follows:

**Insurance risk:** PIC's risk profile includes substantial long-term liabilities so the Internal Model applies capital stresses for base mortality and future mortality improvement risk, rather than solely base mortality as prescribed by the Standard Formula, to ensure we more accurately capture the nature of insurance risks for annuities. PIC also holds capital against uncertainty in second life assumptions and lump sum commutation assumptions, which are excluded from the Standard Formula.

**Operational risk:** PIC's Internal Model for operational risk is based on an assessment of the actual operational risks that PIC is exposed to, including underwriting, asset management, hedging, reserving and outsourcer-related risks. By comparison the Standard Formula for operational risk is a function of premium income received in the previous year which can bear little relationship to where operational risks may arise.

PIC uses the same risk measure and time period as set out in Article 101(3) of the Solvency II, namely the Value-at-Risk of basic Own Funds subject to a confidence level of 99.5% over a one-year period.

PIC uses a variety of data sources in its Internal Model, both internal and external. Internal data includes policyholder data and PIC's own historic company experience. External data are used to support the calibration of market, insurance and counterparty default risk. For market risk the main external providers of data are organisations such as Moody's, Merrill Lynch and Bloomberg who provide the majority of historical market data to support the calibration of the SCR. The counterparty default risk module also uses Moody's historical data. For insurance risk the primary external data source is the Office for National Statistics which provides national population data and data on the number of deaths.

All data sources are reviewed internally for completeness, appropriateness and accuracy prior to use in the Internal Model.



#### E.4.1 Comparison of the Company's Internal Model with the Standard Formula (Unaudited)

The following table compares the SCR calculated on the Standard Formula basis and using the Company's Internal Model.

	Internal Model with matching adjustment End-16 £m	Standard Formula with matching adjustment End-16 £m
Market risk	1,524	2,042
Insurance risk	1,227	465
Operational risk	171	104
Expense risk	115	144
Counterparty default risk	64	51
Benefit of diversification	(959)	(435)
Loss absorbing capacity of deferred tax	(230)	(382)
<b>SCR</b>	<b>1,912</b>	<b>1,989</b>

Of note, the Standard Formula was calibrated with respect to an average European insurance entity. As PIC is a UK specialist insurance provider, the Company's business is not well represented by the Standard Formula. Using a risk capital model that does not represent the risks to the business does not incentivise good risk management, with actions being taken to optimise a position under a formula rather than aligned to the risks.

In particular, the design and calibration of the Standard Formula is not deemed appropriate to reflect PIC's internal view of its main risk drivers – market risk, including inflation risk and basis risk, and insurance risk, particularly the allowance for the risks associated with mortality improvements. PIC's Internal Model adopts a more granular approach to determining the capital requirements for both of these major risks as well as incorporating additional risks such as those associated with taking on liabilities with inflation-linked benefits.

For PIC's less important risks the Internal Model calibration is also more bespoke than the Standard Formula. For operational risk the capital is based on an assessment of the actual operational risks that PIC is exposed to, including underwriting, asset management, hedging, reserving and outsourcer-related risks. By comparison the Standard Formula for operational risk is a function of premium income received in the previous year which can bear little relationship to where operational risks may arise. For counterparty default risk PIC uses a bespoke stochastic model allowing for all risk mitigants it deploys to manage such risks. For expense risk PIC again has a bespoke calibration reflecting the key source of expense risk such as investment management fees and policy maintenance costs.

PIC uses its Internal Model within the key business processes outlined below:

Key business processes	Responsible oversight committee
Strategy and business planning (including ORSA)	Board
Origination of new business and ceding of reinsurance	Origination Committee
Risk management	BRC
Asset liability management	ALM Committee
Performance management	Nomination and Remuneration Committee
Financial reporting	Audit Committee

Each "responsible oversight committee" performs an assessment of their use of the model in decision making and any areas for enhancement. Additionally, the Board performs an assessment based on its enterprise-wide responsibilities.

The nature of their assessments includes the extent to which:

- the Board or Committee feels it has sufficient understanding of the Internal Model
- the Internal Model is embedded in all relevant decision-making processes
- The papers and proposals presented to the Board/Committee and resulting minutes from discussions reflect the Internal Model

Suitable and clearly defined governance and oversight structures exist within PIC to support the use of the Internal Model.

#### E.5 Non-compliance with the MCR and significant non-compliance with the SCR

Both PIC and PICG have been fully compliant with both the MCR and the SCR throughout 2016 and up to the date of approval of this report.

# SOLVENCY AND FINANCIAL CONDITION REPORT

## APPENDIX A

### Appendix A Glossary of terms

#### **BEL**

Best Estimate Liability.

#### **EIOPA**

European Insurance and Occupational Pensions Authority. This is the European regulator that sets Solvency II Regulations.

#### **IFRS**

International Financial Reporting Standards, also known as International Accounting Standards. The accounting framework used by the Group and Company in their statutory accounts.

#### **LACDT**

Loss absorbing capacity of deferred tax. A reduction to the capital requirements to allow for tax losses that may arise as a result of a shock event.

#### **ORSA**

The name given to the entirety of the processes and procedures employed by an insurer to identify, assess, monitor, manage and report the short and long-term risks it faces or may face and to determine the capital necessary to ensure that the insurers overall solvency needs are met at all times.

#### **Own Funds**

Own Funds represent the equity base of the Company under the Solvency II regime. Own Funds can be classified as "basic Own Funds" and "ancillary Own Funds", and are structured into tiers (Tier 1, Tier 2, and Tier 3) which broadly represent the quality and permanency of the capital.

#### **QRT**

Quantitative Reporting Templates. Quarterly solvency returns submitted to the national regulator.

#### **Risk margin**

The Risk Margin is a regulatory requirement introduced by Solvency II. Although it forms a part of the Technical Provisions, can be thought of as a part of the wider capital requirements of a regulated insurance company. It is designed to represent the amount which another insurer would require to take on the insurance obligations of an insurer, in the event that it used up all of its surplus and capital as a result of a shock.

#### **SCR**

Solvency Capital Requirement – the risk based capital assessment under Solvency II. Can either be set by Standard Formula or a regulatory-approved internal model.

#### **SFCR**

A public disclosure report which is required to be published annually by all insurers and will contain detailed quantitative and qualitative elements.

#### **Technical provisions**

The liabilities arising under insurance contracts. Under the Solvency II framework, these represent the sum of best estimate liability, risk margin and the TMTP.

#### **TMTP**

Transitional Measures on Technical Provisions. A transitional arrangement whereby differences between the Solvency II regime and an insurer's previous regulatory capital regime can be phased in over a period, generally a maximum of 16 years.

## APPENDIX B

PENSION INSURANCE CORPORATION PLC

Pension Insurance Corporation plc	
QRT Ref	QRT Template name
S.02.01.02	Balance sheet
S.05.01.02	Premiums, claims and expenses by line of business
S.05.02.01	Premiums, claims and expenses by country
S.12.01.02	Life and Health SLT Technical Provisions
S.22.01.21	Impact of long term guarantees measures and transitionals
S.23.01.01	Own Funds
S.25.03.21	SCR – for undertakings on Full Internal Models
S.28.01.01	MCR – Only life or only non-life insurance or reinsurance activity

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

S.02.01.02

Balance sheet – 31 December 2016

Solvency II value  
C0010

Assets		
R0010	Goodwill	
R0020	Deferred acquisition costs	
R0030	Intangible assets	
R0040	Deferred tax assets	
R0050	Pension benefit surplus	
R0060	Property, plant & equipment held for own use	0
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	<b>32,788,578,879</b>
R0080	<i>Property (other than for own use)</i>	96,753,310
R0090	<i>Holdings in related undertakings, including participations</i>	0
R0100	<i>Equities</i>	<b>0</b>
R0110	<i>Equities – listed</i>	0
R0120	<i>Equities – unlisted</i>	0
R0130	<i>Bonds</i>	<b>20,662,233,902</b>
R0140	<i>Government Bonds</i>	7,935,572,166
R0150	<i>Corporate Bonds</i>	12,550,472,992
R0160	<i>Structured notes</i>	0
R0170	<i>Collateralised securities</i>	176,188,744
R0180	<i>Collective Investments Undertakings</i>	1,297,016,375
R0190	<i>Derivatives</i>	10,732,575,292
R0200	<i>Deposits other than cash equivalents</i>	0
R0210	<i>Other investments</i>	0
R0220	Assets held for index-linked and unit-linked contracts	
R0230	Loans and mortgages	<b>554,431,537</b>
R0240	<i>Loans on policies</i>	0
R0250	<i>Loans and mortgages to individuals</i>	
R0260	<i>Other loans and mortgages</i>	554,431,537
R0270	Reinsurance recoverables from:	<b>1,589,615,970</b>
R0280	<i>Non-life and health similar to non-life</i>	<b>0</b>
R0290	<i>Non-life excluding health</i>	
R0300	<i>Health similar to non-life</i>	
R0310	<i>Life and health similar to life, excluding index-linked and unit-linked</i>	1,589,615,970
R0320	<i>Health similar to life</i>	0
R0330	<i>Life excluding health and index-linked and unit-linked</i>	1,589,615,970
R0340	<i>Life index-linked and unit-linked</i>	0
R0350	Deposits to cedants	0
R0360	Insurance and intermediaries receivables	3,640,464
R0370	Reinsurance receivables	
R0380	Receivables (trade, not insurance)	36,392,564
R0390	Own shares (held directly)	0
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	0
R0410	Cash and cash equivalents	248,281,772
R0420	Any other assets, not elsewhere shown	47,608,409
R0500	<b>Total assets</b>	<b>35,268,549,595</b>

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

S.02.01.02 – continued  
Balance sheet – 31 December 2016

Solvency II value  
C0010

Liabilities		
R0510	Technical provisions – non-life	
R0520	<i>Technical provisions – non-life (excluding health)</i>	
R0530	<i>TP calculated as a whole</i>	
R0540	<i>Best Estimate</i>	
R0550	<i>Risk margin</i>	
R0560	<i>Technical provisions – health (similar to non-life)</i>	
R0570	<i>TP calculated as a whole</i>	
R0580	<i>Best Estimate</i>	
R0590	<i>Risk margin</i>	
R0600	Technical provisions – life (excluding index-linked and unit-linked)	<b>19,816,929,695</b>
R0610	<i>Technical provisions – health (similar to life)</i>	
R0620	<i>TP calculated as a whole</i>	
R0630	<i>Best Estimate</i>	
R0640	<i>Risk margin</i>	
R0650	Technical provisions – life (excluding health and index-linked and unit-linked)	<b>19,816,929,695</b>
R0660	<i>TP calculated as a whole</i>	
R0670	<i>Best Estimate</i>	18,911,004,589
R0680	<i>Risk margin</i>	905,925,106
R0690	Technical provisions – index-linked and unit-linked	
R0700	<i>TP calculated as a whole</i>	
R0710	<i>Best Estimate</i>	
R0720	<i>Risk margin</i>	
R0730	Other technical provisions	
R0740	Contingent liabilities	
R0750	Provisions other than technical provisions	
R0760	Pension benefit obligations	
R0770	Deposits from reinsurers	
R0780	Deferred tax liabilities	175,005,392
R0790	Derivatives	12,066,274,903
R0800	Debts owed to credit institutions	
R0810	Financial liabilities other than debts owed to credit institutions	10,853,599
R0820	Insurance & intermediaries payables	26,592,923
R0830	Reinsurance payables	
R0840	Payables (trade, not insurance)	38,736,865
R0850	Subordinated liabilities	<b>594,241,544</b>
R0860	<i>Subordinated liabilities not in BOF</i>	
R0870	<i>Subordinated liabilities in BOF</i>	594,241,544
R0880	Any other liabilities, not elsewhere shown	
R0900	<b>Total liabilities</b>	<b>32,728,634,921</b>
R1000	<b>Excess of assets over liabilities</b>	<b>2,539,914,674</b>

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

S.05.01.02

Premiums, claims and expenses by line of business – 31 December 2016

Life		Line of Business for: life insurance obligations				Total C0300
		Health insurance C0210	Insurance with profit participation C0220	Index-linked and unit-linked insurance C0230	Other life insurance C0240	
<b>Premiums written</b>						
R1410	Gross				2,597,706,299	<b>2,597,706,299</b>
R1420	Reinsurers' share				23,583,744	<b>23,583,744</b>
R1500	Net	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,574,122,555</b>	<b>2,574,122,555</b>
<b>Premiums earned</b>						
R1510	Gross				2,597,706,299	<b>2,597,706,299</b>
R1520	Reinsurers' share				23,583,744	<b>23,583,744</b>
R1600	Net	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,574,122,555</b>	<b>2,574,122,555</b>
<b>Claims incurred</b>						
R1610	Gross				796,504,807	<b>796,504,807</b>
R1620	Reinsurers' share				28,681,343	<b>28,681,343</b>
R1700	Net	<b>0</b>	<b>0</b>	<b>0</b>	<b>767,823,464</b>	<b>767,823,464</b>
<b>Changes in other technical provisions</b>						
R1710	Gross				5,260,887,306	<b>5,260,887,306</b>
R1720	Reinsurers' share				605,425,080	<b>605,425,080</b>
R1800	Net	<b>0</b>	<b>0</b>	<b>0</b>	<b>4,655,462,226</b>	<b>4,655,462,226</b>
R1900	Expenses incurred	<b>0</b>	<b>0</b>	<b>0</b>	<b>71,730,751</b>	<b>71,730,751</b>
R2500	Other expenses					646,424
R2600	<b>Total expenses</b>					<b>72,377,176</b>

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

**S.05.02.01**

Premiums, claims and expenses by country – 31 December 2016

		C0150	C0160	C0170	C0180	C0190	C0200	C0210
R1400		Home Country	Top 5 countries (by amount of gross premiums written) – life obligations					Total Top 5 and home country
	Life	C0220	C0230	C0240	C0250	C0260	C0270	C0280
	<b>Premiums written</b>							
R1410	Gross	2,597,706,299						<b>2,597,706,299</b>
R1420	Reinsurers' share	23,583,744						<b>23,583,744</b>
R1500	Net	<b>2,574,122,555</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,574,122,555</b>
	<b>Premiums earned</b>							
R1510	Gross	2,597,706,299						<b>2,597,706,299</b>
R1520	Reinsurers' share	23,583,744						<b>23,583,744</b>
R1600	Net	<b>2,574,122,555</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,574,122,555</b>
	<b>Claims incurred</b>							
R1610	Gross	796,504,807						<b>796,504,807</b>
R1620	Reinsurers' share	28,681,343						<b>28,681,343</b>
R1700	Net	<b>767,823,464</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>767,823,464</b>
	<b>Changes in other technical provisions</b>							
R1710	Gross	5,260,887,306						<b>5,260,887,306</b>
R1720	Reinsurers' share	605,425,080						<b>605,425,080</b>
R1800	Net	<b>4,655,462,226</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>4,655,462,226</b>
R1900	Expenses incurred	71,730,751						<b>71,730,751</b>
R2500	Other expenses							646,424
R2600	Total expenses							<b>72,377,176</b>

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

S.12.01.02

Life and Health SLT Technical Provisions – 31 December 2016

		Other life insurance		Total
	C0060	Contracts without options and guarantees C0070	Contracts with options or guarantees C0080	(Life other than health Insurance, Incl Unit-linked) C0150
R0010	Technical provisions calculated as a whole			0.00
R0020	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole			0.00
	Technical provisions calculated as a sum of BE and RM			
	Best estimate			
R0030	Gross Best Estimate		18,911,004,589	18,911,004,589
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default		1,589,615,970	1,589,615,970
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re	17,321,388,619	0.00	17,321,388,619
R0100	Risk margin	2,176,328,864		2,176,328,864
	Amount of the transitional on Technical Provisions			
R0110	Technical Provisions calculated as a whole			0.00
R0120	Best estimate			0.00
R0130	Risk margin	-1,270,403,758		-1,270,403,758
R0200	Technical provisions – total	19,816,929,695		19,816,929,695



SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

**S.22.01.21**

Impact of long term guarantees measures and transitionals - 31 December 2016

		Amount with Long Term Guarantee measures and transitionals <b>C0010</b>	Impact of transitional on technical provisions <b>C0030</b>	Impact of transitional on interest rate <b>C0050</b>	Impact of volatility adjustment set to zero <b>C0070</b>	Impact of matching adjustment set to zero <b>C0090</b>
R0010	Technical provisions	19,816,929,695	1,270,403,758	0	469,303	4,436,884,301
R0020	Basic own funds	3,134,156,218	-1,054,435,119	0	-389,521	-3,170,895,281
	Eligible own funds to meet					
R0050	Solvency Capital Requirement	3,134,156,218	-1,054,435,119	0	-389,521	-3,170,895,281
R0090	Solvency Capital Requirement	1,912,253,055	175,005,392	0	0	2,752,724,235
	Eligible own funds to meet					
	Minimum Capital					
R0100	Requirement	2,635,527,327	-1,086,648,097	0	-469,303	-3,682,719,548
R0110	Minimum Capital Requirement	478,063,264	43,751,348	0	0	688,181,059

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
PENSION INSURANCE CORPORATION PLC CONTINUED

**S.23.01.01**  
**Own Funds – 31 December 2016**

	Total C0010	Tier 1 unrestricted C0020	Tier 1 restricted C0030	Tier 2 C0040	Tier 3 C0050
<b>Basic own funds before deduction for participations in other financial sector as foreseen in Article 68 of Delegated Regulation 2015/65</b>					
R0030 Ordinary share capital (gross of own shares)	999,810,351	999,810,351	0	0	0
R0030 Share premium account related to ordinary share capital	0	0	0	0	0
R0040 Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual type undertakings	0	0	0	0	0
R0050 Subordinated mutual member accounts	0	0	0	0	0
R0070 Surplus funds	0	0	0	0	0
R0090 Preference shares	0	0	0	0	0
R0110 Share premium account related to preference shares	0	0	0	0	0
R0130 Reconciliation reserve	1,540,104,323	1,540,104,323	0	0	0
R0140 Subordinated liabilities	594,241,544	0	0	594,241,544	0
R0160 An amount equal to the value of net deferred tax assets	0	0	0	0	0
R0180 Other items approved by supervisory authority as basic own funds not specified above	0	0	0	0	0
<b>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</b>					
R0220 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	0	0	0	0	0
<b>Deductions</b>					
R0230 Deductions for participations in other financial and credit institutions	0	0	0	0	0
R0290 <b>Total basic own funds after deductions</b>	<b>3,134,156,218</b>	<b>2,539,914,674</b>	<b>0</b>	<b>594,241,544</b>	<b>0</b>
<b>Ancillary own funds</b>					
R0300 Unpaid and uncalled ordinary share capital callable on demand	0	0	0	0	0
R0310 Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual-type undertakings, callable on demand	0	0	0	0	0
R0320 Unpaid and uncalled preference shares callable on demand	0	0	0	0	0
R0330 A legally binding commitment to subscribe and pay for subordinated liabilities on demand	0	0	0	0	0
R0340 Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	0	0	0	0	0
R0350 Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	0	0	0	0	0
R0360 Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0	0	0	0	0
R0370 Supplementary members calls – other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0	0	0	0	0
R0390 Other ancillary own funds	0	0	0	0	0
R0400 <b>Total ancillary own funds</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Available and eligible own funds</b>					
R0500 <b>Total available own funds to meet the SCR</b>	<b>3,134,156,218</b>	<b>2,539,914,674</b>	<b>0</b>	<b>594,241,544</b>	<b>0</b>
R0510 <b>Total available own funds to meet the MCR</b>	<b>3,134,156,218</b>	<b>2,539,914,674</b>	<b>0</b>	<b>594,241,544</b>	<b>0</b>
R0540 <b>Total eligible own funds to meet the SCR</b>	<b>2,635,527,327</b>	<b>2,539,914,674</b>	<b>0</b>	<b>95,612,653</b>	<b>0</b>
R0550 <b>Total eligible own funds to meet the MCR</b>	<b>2,635,527,327</b>	<b>2,539,914,674</b>	<b>0</b>	<b>95,612,653</b>	<b>0</b>
R0580 SCR	1,912,253,055				
R0600 MCR	478,063,264				
R0620 Ratio of Eligible own funds to SCR	163.90%				
R0640 Ratio of Eligible own funds to MCR	551.29%				
<b>Reconciliation reserve</b>					
R0700 Excess of assets over liabilities	C0060				
R0710 Own shares (held directly and indirectly)	2,539,914,674				
R0720 For-seable dividends, distributions and charges	0				
R0730 Other basic own fund items	999,810,351				
R0740 Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring-fenced funds	0				
R0760 <b>Reconciliation reserve</b>	<b>1,540,104,323</b>				
<b>Expected profits</b>					
R0770 Expected profits included in future premiums (EPIFP) – Life business					
R0780 Expected profits included in future premiums (EPIFP) – Non-life business					
R0790 <b>Total Expected profits included in future premiums (EPIFP)</b>	<b>0</b>				

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC  
CONTINUED

S.25.03.21

Solvency Capital Requirement – for undertakings on Full Internal Models – 31 December 2016

	Unique number of component C0010	Component description C0020	Calculation of the Solvency Capital Requirement C0030
1	10320I	Interest rate risk – interest rate up more onerous	698,767,996
2	10600I	Property Risk	4,406,772
3	10700I	Spread risk – if matching adjustment impact not identified	1,512,063,677
4	10900I	Currency risk	315,779,608
5	11010I	Other market risk – inflation risk	282,876,240
6	11020I	Other market risk – implied volatility risk	595,909,299
7	11030I	Other market risk – RPI/CPI basis risk	249,217,484
8	11090I	Other market risk – funds risk	132,626,163
9	19900I	Diversification within market risk	-2,267,353,690
10	20120I	Type 1 counterparty risk – external reinsurance	26,018,144
11	20190I	Type 1 counterparty risk – asset counterparty	37,570,899
12	30210I	Longevity risk – longevity mis-estimation	344,911,733
13	30220I	Longevity risk – longevity trend	1,163,861,504
14	30290I	Longevity risk – other longevity risks	249,953,930
15	30299I	Longevity risk – longevity diversification	-531,022,884
16	30600I	Expense risk	183,496,307
17	39900I	Life underwriting risk diversification	-68,466,481
18	70100I	Operational risk	170,827,000
19	80300I	Loss-absorbing capacity of deferred tax	-230,220,097
<b>Calculation of Solvency Capital Requirement</b>			<b>C0100</b>
R0110	Total undiversified components		<b>2,871,223,604</b>
R0060	Diversification		-958,970,549
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC		
R0200	<b>Solvency capital requirement excluding capital add-on</b>		<b>1,912,253,055</b>
R0210	Capital add-ons already set		
R0220	<b>Solvency capital requirement</b>		<b>1,912,253,055</b>
<b>Other information on SCR</b>			
R0300	Amount/estimate of the overall loss-absorbing capacity of technical provisions		
R0310	Amount/estimate of the overall loss-absorbing capacity of deferred taxes		-230,220,097
R0410	Total amount of Notional Solvency Capital Requirements for remaining part		-683,614,933
R0420	Total amount of Notional Solvency Capital Requirement for ring fenced funds		
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios		2,595,867,988
R0440	Diversification effects due to RFF nSCR aggregation for Article 304		
R0460	Net future discretionary benefits		

SOLVENCY AND FINANCIAL CONDITION REPORT

APPENDIX B

PENSION INSURANCE CORPORATION PLC

CONTINUED

**S.28.01.01**

Minimum Capital Requirement – Only life or only non-life insurance or reinsurance activity – 31 December 2016

Linear formula component for non-life insurance and reinsurance obligations				C0010
R0010	MCR <sub>NL</sub> Result			0.00
		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months	
		<b>C0020</b>	<b>C0030</b>	
R0020	Medical expense insurance and proportional reinsurance			
R0030	Income protection insurance and proportional reinsurance			
R0040	Workers' compensation insurance and proportional reinsurance			
R0050	Motor vehicle liability insurance and proportional reinsurance			
R0060	Other motor insurance and proportional reinsurance			
R0070	Marine, aviation and transport insurance and proportional reinsurance			
R0080	Fire and other damage to property insurance and proportional reinsurance			
R0090	General liability insurance and proportional reinsurance			
R0100	Credit and suretyship insurance and proportional reinsurance			
R0110	Legal expenses insurance and proportional reinsurance			
R0120	Assistance and proportional reinsurance			
R0130	Miscellaneous financial loss insurance and proportional reinsurance			
R0140	Non-proportional health reinsurance			
R0150	Non-proportional casualty reinsurance			
R0160	Non-proportional marine, aviation and transport reinsurance			
R0170	Non-proportional property reinsurance			
Linear formula component for life insurance and reinsurance obligations				C0040
R0200	MCR <sub>NL</sub> Result			363,749,161
		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk	
		<b>C0050</b>	<b>C0060</b>	
R0210	Obligations with profit participation – guaranteed benefits			
R0220	Obligations with profit participation – future discretionary benefits			
R0230	Index-linked and unit-linked insurance obligations			
R0240	Other life (re)insurance and health (re)insurance obligations	17,321,389		
R0250	Total capital at risk for all life (re)insurance obligations			
Linear formula component for life insurance and reinsurance obligations				C0040
	MCRL Result			363,749,16
	Overall MCR calculation			<b>C0070</b>
R0300	Linear MCR			363,749,161
R0310	SCR			1,912,253,055
R0320	MCR cap			860,513,875
R0330	MCR floor			478,063,264
R0340	Combined MCR			478,063,264
R0350	Absolute floor of the MCR			<b>3,331,850</b>
R0400	Minimum Capital Requirement			478,063,264

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
PENSION INSURANCE CORPORATION GROUP LIMITED

Pension Insurance Corporation Group Limited	
QRT Ref	QRT Template name
S.02.01.02	Balance sheet
S.05.01.02	Premiums, claims and expenses by line of business
S.05.02.01	Premiums, claims and expenses by country
S.22.01.22	Impact of long term guarantees measures and transitionals
S.23.01.22	Own Funds
S.25.03.22	SCR – for undertakings on Full Internal Models
S.32.01.22	Undertakings in the scope of the group

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
PENSION INSURANCE CORPORATION GROUP LIMITED  
CONTINUED

**S.02.01.02**

Balance sheet – 31 December 2016

Solvency II value  
**C0010**

<b>Assets</b>		
R0010	Goodwill	
R0020	Deferred acquisition costs	
R0030	Intangible assets	
R0040	Deferred tax assets	
R0050	Pension benefit surplus	
R0060	Property, plant & equipment held for own use	237,841
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	<b>32,788,675,730</b>
R0080	<i>Property (other than for own use)</i>	96,850,160
R0090	<i>Holdings in related undertakings, including participations</i>	0
R0100	<i>Equities</i>	<b>0</b>
R0110	<i>Equities – listed</i>	0
R0120	<i>Equities – unlisted</i>	0
R0130	<i>Bonds</i>	<b>20,662,233,902</b>
R0140	<i>Government Bonds</i>	7,935,572,166
R0150	<i>Corporate Bonds</i>	12,550,472,992
R0160	<i>Structured notes</i>	0
R0170	<i>Collateralised securities</i>	176,188,744
R0180	<i>Collective Investments Undertakings</i>	1,297,016,375
R0190	<i>Derivatives</i>	10,732,575,292
R0200	<i>Deposits other than cash equivalents</i>	0
R0210	<i>Other investments</i>	0
R0220	Assets held for index-linked and unit-linked contracts	0
R0230	Loans and mortgages	<b>554,431,537</b>
R0240	<i>Loans on policies</i>	0
R0250	<i>Loans and mortgages to individuals</i>	
R0260	<i>Other loans and mortgages</i>	554,431,537
R0270	Reinsurance recoverables from:	<b>1,589,615,970</b>
R0280	<i>Non-life and health similar to non-life</i>	<b>1,589,615,970</b>
R0290	<i>Non-life excluding health</i>	
R0300	<i>Health similar to non-life</i>	1,589,615,970
R0310	<i>Life and health similar to life, excluding index-linked and unit-linked</i>	0
R0320	<i>Health similar to life</i>	
R0330	<i>Life excluding health and index-linked and unit-linked</i>	
R0340	<i>Life index-linked and unit-linked</i>	
R0350	Deposits to cedants	0
R0360	Insurance and intermediaries receivables	3,640,464
R0370	Reinsurance receivables	
R0380	Receivables (trade, not insurance)	38,976,099
R0390	Own shares (held directly)	712,996
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	0
R0410	Cash and cash equivalents	276,371,267
R0420	Any other assets, not elsewhere shown	49,263,264
R0500	<b>Total assets</b>	<b>35,301,925,167</b>

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
PENSION INSURANCE CORPORATION GROUP LIMITED  
CONTINUED

**S.02.01.02** – continued  
Balance sheet – 31 December 2016

Solvency II value  
**C0010**

<b>Liabilities</b>	<b>0</b>
R0510 Technical provisions – non-life	<b>0</b>
R0520 <i>Technical provisions – non-life (excluding health)</i>	
R0530 <i>TP calculated as a whole</i>	
R0540 <i>Best Estimate</i>	
R0550 <i>Risk margin</i>	
R0560 <i>Technical provisions – health (similar to non-life)</i>	<b>0</b>
R0570 <i>TP calculated as a whole</i>	
R0580 <i>Best Estimate</i>	
R0590 <i>Risk margin</i>	
R0600 Technical provisions – life (excluding index-linked and unit-linked)	<b>19,816,929,695</b>
R0610 <i>Technical provisions – health (similar to life)</i>	<b>0</b>
R0620 <i>TP calculated as a whole</i>	
R0630 <i>Best Estimate</i>	
R0640 <i>Risk margin</i>	
R0650 Technical provisions – life (excluding health and index-linked and unit-linked)	<b>19,816,929,695</b>
R0660 <i>TP calculated as a whole</i>	
R0670 <i>Best Estimate</i>	18,911,004,589
R0680 <i>Risk margin</i>	905,925,106
R0690 Technical provisions – index-linked and unit-linked	<b>0</b>
R0700 <i>TP calculated as a whole</i>	
R0710 <i>Best Estimate</i>	
R0720 <i>Risk margin</i>	
R0730 Other technical provisions	
R0740 Contingent liabilities	
R0750 Provisions other than technical provisions	
R0760 Pension benefit obligations	
R0770 Deposits from reinsurers	
R0780 Deferred tax liabilities	175,005,392
R0790 Derivatives	12,066,274,903
R0800 Debts owed to credit institutions	
R0810 Financial liabilities other than debts owed to credit institutions	10,853,599
R0820 Insurance & intermediaries payables	40,958,140
R0830 Reinsurance payables	
R0840 Payables (trade, not insurance)	37,209,717
R0850 Subordinated liabilities	<b>594,241,544</b>
R0860 <i>Subordinated liabilities not in BOF</i>	
R0870 <i>Subordinated liabilities in BOF</i>	594,241,544
R0880 Any other liabilities, not elsewhere shown	
R0900 <b>Total liabilities</b>	<b>32,741,472,990</b>
R1000 <b>Excess of assets over liabilities</b>	<b>2,560,452,177</b>

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
 PENSION INSURANCE CORPORATION GROUP LIMITED  
 CONTINUED

**S.05.01.02**

Premiums, claims and expenses by line of business – 31 December 2016

Life	Line of Business for: life insurance obligations	Other life insurance C0240	Total C0300
<b>Premiums written</b>			
R1410 Gross		2,597,706,299	<b>2,597,706,299</b>
R1420 Reinsurers' share		23,583,744	<b>23,583,744</b>
R1500 Net		<b>2,574,122,555</b>	<b>2,574,122,555</b>
<b>Premiums earned</b>			
R1510 Gross		2,597,706,299	<b>2,597,706,299</b>
R1520 Reinsurers' share		23,583,744	<b>23,583,744</b>
R1600 Net		<b>2,574,122,555</b>	<b>2,574,122,555</b>
<b>Claims incurred</b>			
R1610 Gross		796,504,807	<b>796,504,807</b>
R1620 Reinsurers' share		28,681,343	<b>28,681,343</b>
R1700 Net		<b>767,823,464</b>	<b>767,823,464</b>
<b>Changes in other technical provisions</b>			
R1710 Gross		5,260,887,306	<b>5,260,887,306</b>
R1720 Reinsurers' share		605,425,080	<b>605,425,080</b>
R1800 Net		<b>4,655,462,226</b>	<b>4,655,462,226</b>
R1900 Expenses incurred		<b>71,730,751</b>	<b>71,730,751</b>
R2500 Other expenses			646,424
R2600 Total expenses			<b>72,377,176</b>



SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
PENSION INSURANCE CORPORATION GROUP LIMITED  
CONTINUED

**S.05.02.01**

Premiums, claims and expenses by country – 31 December 2016

		C0150	C0160	C0170	C0180	C0190	C0200	C0210
		Home Country	Top 5 countries (by amount of gross premiums written) – life obligations					Total Top 5 and home country
R1400	Life	C0220	C0230	C0240	C0250	C0260	C0270	C0280
<b>Premiums written</b>								
R1410	Gross	2,597,706,299						<b>2,597,706,299</b>
R1420	Reinsurers' share	23,583,744						<b>23,583,744</b>
R1500	Net	<b>2,574,122,555</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,574,122,555</b>
<b>Premiums earned</b>								
R1510	Gross	2,597,706,299						<b>2,597,706,299</b>
R1520	Reinsurers' share	23,583,744						<b>23,583,744</b>
R1600	Net	<b>2,574,122,555</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,574,122,555</b>
<b>Claims incurred</b>								
R1610	Gross	796,504,807						<b>796,504,807</b>
R1620	Reinsurers' share	28,681,343						<b>28,681,343</b>
R1700	Net	<b>767,823,464</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>767,823,464</b>
<b>Changes in other technical provisions</b>								
R1710	Gross	5,260,887,306						<b>5,260,887,306</b>
R1720	Reinsurers' share	605,425,080						<b>605,425,080</b>
R1800	Net	<b>4,655,462,226</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>4,655,462,226</b>
R1900	Expenses incurred	71,730,751						<b>71,730,751</b>
R2500	Other expenses							646,424
R2600	Total expenses							<b>72,377,176</b>

**S.22.01.22**

Impact of long term guarantees measures and transitionals – 31 December 2016

		Amount with Long Term Guarantee 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
R0010	Technical provisions	19,816,929,695	1,270,403,758	0	469,303	4,436,884,301
R0020	Basic own funds	3,153,980,725	-1,054,435,352	0	-389,521	-3,170,895,281
R0050	Eligible own funds to meet					
	Solvency Capital Requirement	3,153,980,725	-1,054,435,351	0	-389,521	-3,170,895,281
R0090	Solvency Capital Requirement	1,912,253,055	175,005,392	0	0	2,752,724,235

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**

PENSION INSURANCE CORPORATION GROUP LIMITED CONTINUED

**S.23.01.22**  
**Own Funds – 31 December 2016**

	Total C0010	Tier 1 unrestricted C0020	Tier 1 restricted C0030	Tier 2 C0040	Tier 3 C0050
<b>Basic own funds before deduction for participations in other financial sector</b>					
R0010 Ordinary share capital (gross of own shares)	1,753,247	1,753,247	0	0	0
R0020 Non-avoidable called but not paid in ordinary share capital at group level	0	0	0	0	0
R0030 Share premium account related to ordinary share capital	118,211,894	118,211,894	0	0	0
R0040 Initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual-type undertakings	0	0	0	0	0
R0050 Subordinated initial member accounts	0	0	0	0	0
R0060 Non-avoidable subordinated mutual member accounts at group level	0	0	0	0	0
R0070 Surplus funds	0	0	0	0	0
R0080 Non-avoidable surplus funds at group level	0	0	0	0	0
R0090 Preference shares	0	0	0	0	0
R0100 Non-avoidable preference shares at group level	0	0	0	0	0
R0110 Share premium account related to preference shares	0	0	0	0	0
R0120 Non-avoidable share premium account related to preference shares at group level	0	0	0	0	0
R0130 Reconciliation reserve	2,439,774,040	2,439,774,040	0	0	0
R0140 Subordinated liabilities	594,241,544	0	0	594,241,544	0
R0150 Non-avoidable subordinated liabilities at group level	0	0	0	0	0
R0160 An amount equal to the value of net deferred tax assets	0	0	0	0	0
R0170 The amount equal to the value of net deferred tax assets not available at the group level	0	0	0	0	0
R0180 Other items approved by supervisory authority as basic own funds not specified above	0	0	0	0	0
R0190 Non-avoidable own funds related to other own funds items approved by supervisory authority	0	0	0	0	0
R0200 Minority interests (if not reported as part of a specific own fund item)	0	0	0	0	0
R0210 Non-avoidable minority interests at group level	0	0	0	0	0
<b>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</b>					
R0220 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	3,153,980,725	2,559,739,181	0	594,241,544	0
<b>Deductions</b>					
R0230 Deductions for participations in other financial undertakings, including non-regulated undertakings carrying out financial activities	0	0	0	0	0
R0240 Deductions for participations in other financial undertakings according to art 228 of the Directive 2009/138/EC	0	0	0	0	0
R0250 Deductions for participations where there is non-availability of information (Article 229)	0	0	0	0	0
R0260 Deduction for participations included by using D&A when a combination of methods is used	0	0	0	0	0
R0270 Total of non-avoidable own fund items	0	0	0	0	0
R0280 Total deductions	0	0	0	0	0
<b>Total basic own funds after deductions</b>	<b>3,153,980,725</b>	<b>2,559,739,181</b>	<b>0</b>	<b>594,241,544</b>	<b>0</b>
<b>Ancillary own funds</b>					
R0300 Unpaid and uncalled ordinary share capital callable on demand	0	0	0	0	0
R0310 Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual-type undertakings, callable on demand	0	0	0	0	0
R0320 Unpaid and uncalled preference shares, callable on demand	0	0	0	0	0
R0330 A legally binding commitment to subscribe and pay for subordinated liabilities on demand	0	0	0	0	0
R0340 Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	0	0	0	0	0
R0350 Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	0	0	0	0	0
R0360 Supplementary members calls under subparagraph of Article 96(3) of the Directive 2009/138/EC	0	0	0	0	0
R0370 Supplementary members calls – other than under subparagraph of Article 96(3) of the Directive 2009/138/EC	0	0	0	0	0
R0380 Other ancillary own funds at group level	0	0	0	0	0
R0390 Other ancillary own funds	0	0	0	0	0
R0400 Total ancillary own funds	0	0	0	0	0
<b>Own funds of other financial sectors</b>					
R0410 Credit institutions, investment firms, financial institutions, alternative investment fund manager, financial institutions	0	0	0	0	0
R0420 Institutions for occupational retirement provision	0	0	0	0	0
R0430 Non-regulated entities carrying out financial activities	0	0	0	0	0
R0440 Total own funds of other financial sectors	0	0	0	0	0
<b>Own funds when using the D&amp;A, exclusively or in combination of method 1</b>					
R0450 Own funds aggregated when using the D&A and combination of method	0	0	0	0	0
R0460 Own funds aggregated when using the D&A and combination of method net of IGT	0	0	0	0	0
<b>Total available own funds to meet the consolidated group SCR (excluding own funds from other financial sector and from the undertakings included via D&amp;A)</b>	<b>3,153,980,725</b>	<b>2,559,739,181</b>	<b>0</b>	<b>594,241,544</b>	<b>0</b>
R0530 Total available own funds to meet the minimum consolidated group SCR	3,153,980,725	2,559,739,181	0	594,241,544	0
R0560 Total eligible own funds to meet the consolidated group SCR (excluding own funds from other financial sector and from the undertakings included via D&A)	3,153,980,725	2,559,739,181	0	594,241,544	0
R0570 Total eligible own funds to meet the minimum consolidated group SCR (group)	2,655,351,834	2,559,739,181	0	95,612,653	0
<b>Consolidated Group SCR</b>	1,912,253,055				
R0640 Minimum capital requirement for the consolidated Group SCR	476,633,944				
R0630 Ratio of Eligible own funds to the consolidated Group SCR (excluding other financial sectors and the undertakings included via D&A)	164.94%				
R0650 Ratio of Eligible own funds to Minimum Consolidated Group SCR	555.44%				
R0660 Total Eligible own funds to meet the group SCR (including own funds from other financial sector and from the undertakings included via D&A)	3,153,980,725	2,559,739,181	0	594,241,544	0
R0670 SCR for entities included with D&A method	1,912,253,055				
R0680 Group SCR	1,912,253,055				
R0690 Ratio of Eligible own funds to group SCR including other financial sectors and the undertakings included via D&A	164.94%				
<b>Reconciliation reserve</b>					
R0700 Excess of assets over liabilities	C0060				
R0710 Own shares (held directly and indirectly)	2,560,452,177				
R0720 Forfeitable dividends, distributions and charges	712,996				
R0730 Other basic own fund items	119,965,141				
R0740 Adjustment for netted own fund items in respect of matching adjustment portfolios and ring fenced funds	0				
R0750 Other eligible own funds	0				
R0760 Reconciliation reserve	2,439,774,040				
<b>Expected profits</b>					
R0770 Expected profits included in future premiums (EPFPF) – Life business	0				
R0780 Expected profits included in future premiums (EPFPF) – Non-life business	0				
R0790 Total Expected profits included in future premiums (EPFPF)	0				

<Note: this deduction is now included in R0290/C0020 as per 2.1.0 taxonomy

SOLVENCY AND FINANCIAL CONDITION REPORT  
**APPENDIX B**  
PENSION INSURANCE CORPORATION GROUP LIMITED  
CONTINUED

**S.25.03.22**

**Solvency Capital Requirement – for undertakings on Full Internal Models – 31 December 2016**

	Unique number of component <b>C0010</b>	Component description <b>C0020</b>	Calculation of the Solvency Capital Requirement <b>C0030</b>
1	10320I	Interest rate risk – interest rate up more onerous	698,767,996
2	10600I	Property Risk	4,406,772
3	10700I	Spread risk – if matching adjustment impact not identified	1,512,063,677
4	10900I	Currency risk	315,779,608
5	11010I	Other market risk – inflation risk	282,876,240
6	11020I	Other market risk – implied volatility risk	595,909,299
7	11030I	Other market risk – RPI/CPI basis risk	249,217,484
8	11090I	Other market risk – funds risk	132,626,163
9	19900I	Diversification within market risk	-2,267,353,690
10	20120I	Type 1 counterparty risk – external reinsurance	26,018,144
11	20190I	Type 1 counterparty risk – asset counterparty	37,570,899
12	30210I	Longevity risk – longevity mis-estimation	344,911,733
13	30220I	Longevity risk – longevity trend	1,163,861,504
14	30290I	Longevity risk – other longevity risks	249,953,930
15	30299I	Longevity risk – longevity diversification	-531,022,884
16	30600I	Expense risk	183,496,307
17	39900I	Life underwriting risk diversification	-68,466,481
18	70100I	Operational risk	170,827,000
19	80300I	Loss-absorbing capacity of deferred tax	-230,220,097
<b>Calculation of Solvency Capital Requirement</b>			<b>C0100</b>
R0110	Total undiversified components		<b>2,871,223,604</b>
R0060	Diversification		-958,970,549
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC		
R0200	<b>Solvency capital requirement excluding capital add-on</b>		<b>1,912,253,055</b>
R0210	Capital add-ons already set		
R0220	<b>Solvency capital requirement</b>		<b>1,912,253,055</b>
<b>Other information on SCR</b>			
R0300	Amount/estimate of the overall loss-absorbing capacity of technical provisions		
R0310	Amount/estimate of the overall loss-absorbing capacity of deferred taxes		-230,220,097
R0410	Total amount of Notional Solvency Capital Requirements for remaining part		-683,614,933
R0420	Total amount of Notional Solvency Capital Requirement for ring fenced funds		
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios		2,595,867,988
R0440	Diversification effects due to RFF nSCR aggregation for Article 304		
R0460	Net future discretionary benefits		
R0470	Minimum consolidated group solvency capital requirement		478,063,264

# APPENDIX B

## PENSION INSURANCE CORPORATION GROUP LIMITED CONTINUED

### S.32.01.22

#### Undertakings in the scope of the group – 31 December 2016

Country C0010	Identification code of the undertaking C0020	Type of code of the ID of the undertaking C0030	Legal Name of the undertaking C0040	Type of undertaking C0050	Legal form C0060	Category (Mutual/non-mutual) C0070	Supervisory Authority C00800	Criteria of influence					Inclusion in the scope of Group supervision	Date of decision if art. 214 is applied C0250	Method used and under treatment of the undertaking C0260
								% used for the establishment of consolidated accounts C0180	% capital share C0190	% voting rights C0200	Other criteria C0210	Level of influence C0220			
1 GB	549300UNZ1FOTWMZYC35	LEI	Pension Insurance Corporation Group Limited	5		2									Method 1-Full consolidation
2 GB	M31AVD1X8NY21MAUQF46	LEI	Pension Insurance Corporation PIC	1	Company limited by shares or guarantee	2	Prudential Regulation Authority	100.00%	100.00%	100.00%	Dominant	100.00%	Included in the scope		Method 1-Full consolidation
3 GB	549300Q8BH2WBUKFA06	LEI	PIC Holding Limited	5		2		100.00%	100.00%	100.00%	Dominant	100.00%	Included in the scope		Method 1-Full consolidation
4 GB	PSC	Specific code	Pension Service Corporation Limited	10		2		100.00%	100.00%	100.00%	Dominant	100.00%	Included in the scope		Method 1-Full consolidation

SOLVENCY AND FINANCIAL CONDITION REPORT  
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