Solvency and Financial Condition Report as at 31 December 2016

Contents

Introduction

The new, harmonised EU-wide regulatory regime for insurance companies, known as Solvency II, came into force with effect from 1 January 2016. The regime requires new reporting and public disclosure arrangements to be put in place by insurers and some of that is required to be published on the Society's website. This Solvency and Financial Condition Report (SFCR) has been prepared to assist members to understand the capital position of the Society.

The contents of the SFCR are prescribed by EU regulation and must contain the following sections:

SFCR Section	Description of Contents
Business and Performance	Information about the Society and a summary of business and financial performance over the year.
System of governance	Information about the Society's organisational structure and system of governance, including risk management, internal control, internal audit and the actuarial function.
Risk Profile	Information about the key risks facing the Society and how these are managed.
Valuation for Solvency purposes	Valuation of the Society's assets and liabilities in accordance with accounting standards and solvency rules, including details on the assumptions used to calculate them and the differences between them.
Capital Management	Information on the capital requirements of the Society in line with Solvency II regulations.

Business and Performance

The Society enjoyed a good year in 2016, generating a transfer to Own Funds of £108,226. At 31 December 2016, there were unrealised gains of £1,516,225 in the value of investments held, in contrast to unrealised losses of £559,748 at 31 December 2015. There was also a significant increase in net operating expenses compared to prior years, largely due to the implementation of the succession plan for the Chief Executive position and general increases in regulatory costs. The reduction in risk-free rates contributed to an increase in the Society's technical provision and the fall in the value of sterling against the euro caused an increase in the Society's Minimum Capital Requirement.

System of Governance

The Society operates under the direction of the Management Committee, with day-to-day operational management delegated to the Chief Executive and other senior managers. The Society also has an Audit and Risk Management sub-Committee that deals with matters relating to financial and regulatory reporting, internal and external audit, internal control and risk management. During 2016, the Society set up its With-Profits Advisory Arrangement in order to protect the interests of With-Profits policyholders and ensure that the With-Profits Fund is managed in accordance with the Principles and Practices of Financial Management (PPFM).

The Society follows 'fit and proper person' principles in order to ensure that key functions are led by appropriately skilled people. The key functions include internal audit, risk management, actuarial and compliance. All outsourced services are reviewed periodically and, when considered appropriate, are re-tendered or renegotiated.

The Society has strong risk management arrangements, including an Own Risk and Solvency Assessment process. This is a rolling process, under the governance of the Management Committee, that provides a detailed analysis of the Society's capital adequacy, risk management and forward-looking perspective.

The adequacy and effectiveness of the Society's risk management, internal control and governance processes are subject to periodic review by Internal Audit, which reports its findings and recommendations independently to the Audit and Risk Management sub-Committee.

Risk Profile

The Society manages its risks to ensure that it can meet its obligations to policyholders as they fall due and provide them with a reasonable return on their investment. The principal risks faced by the Society are:

- Underwriting risk, which arises from the underwriting of the Society's policies and includes mortality, morbidity, lapse rates, expense levels etc.
- Market risk, which is the risk that a financial instrument will fluctuate in value because of the volatility of market prices.
- Counterparty default risk, which is the risk of potential losses due to unexpected default, or deterioration in the credit standing of counterparties and debtors.
- Liquidity risk, which is the risk that the Society, though solvent, does not have sufficient financial resources to meet its obligations as they fall due.
- Operational risk, which is the risk of loss arising from inadequate or failed internal processes, or from personnel and systems, or from external events.

For the key risks that the Society is exposed to, the sensitivity of the Society's surplus assets is investigated annually and the detailed results are contained in a Forward-Looking Assessment of Solvency report.

Valuation for Solvency Purposes

The table below summarises the Society's assets and liabilities valued in accordance with Financial Reporting Standards and Solvency II regulations.

£000	Solvency II	Financial Statements
Assets	33,597	33,597
Technical Provisions	27,895	27,895
Other Liabilities	262	262

Capital Management

The Society is a mutual organisation and so does not have any shareholders. The Society's own funds are the surplus accumulated that has not yet been allocated to policies. It forms part of the working capital of the Society and is available to meet risk and capital requirements, as well as any uncertain additional liabilities that may arise in the future.

The Solvency Capital Requirement (SCR) is capital that needs to be held in additional to the technical provisions. This is assessed based on the Society's risks as being sufficient to cover possible losses due to those risks. It considers four different risks: market, counterparty, life underwriting and operational. The Society is also subject to the Minimum Capital Requirement. The absolute floor of €3.7m converted into pounds using the official exchange rate at 31 December 2016 is £3,332k.

The table below summarises the Society's capital position as at 31 December 2016:

£000	31 December 2015	31 December 2016
Own Funds	5,331	5,440
Capital Requirement	2,657	3,332
Free Assets	2,674	2,108

The movement in the Capital Requirement between 31 December 2015 and 31 December 2016 is due entirely to the movement in the euro / sterling exchange rate. The small decrease in own funds was due to the liabilities increasing by more than the assets. The most significant reason for the change in both liabilities and assets was market movements. The Society had sufficient assets to cover the technical provisions and Minimum Capital Requirement at all times during 2016.

Approval by the Management Committee

The Management Committee is responsible for preparing the Solvency and Financial Condition Report in accordance with the Prudential Regulation Authority (PRA) rules and Solvency II Regulations.

The members of the Management Committee confirm that, to the best of their knowledge,

- Throughout the 2016 year, the Society has complied in all material respects with the requirements of the PRA rules and Solvency II Regulations as applicable; and
- It is reasonable to believe that, at the date of publication of the SFCR, the Society continues so to comply and will continue so to comply in the future.

By order of the Management Committee,

R G Frier, Deputy Chair

18 May 2017

M A Bicknell, Chief Executive

18 May 2017

A Business and performance

A1 Business

A1.1 Corporate structure

The Society, which was founded in 1865, is a mutual friendly society, incorporated under the Friendly Societies Act 1992. The registered number of the Society is 708F.

The Society is not part of a group and does not have any subsidiaries.

A1.2 Business objectives

The Society's principal activity is to provide savings plans with life assurance to employees within the railway industry through endowment policies, which, in the case of those with relevant certification, can include cover against permanent disablement.

A1.3 Registered office

The registered office of the Society is:

727 Washwood Heath Road
Birmingham
B8 2LE

A1.4 Regulators

The Society is authorised by the Prudential Regulation Authority. The Society is regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

Prudential Regulation Authority
Bank of England
20 Moorgate
London
EC2R 8AH

Financial Conduct Authority
25 The North Colonnade
London
E14 5HS

The Society, as a category 5 firm, has no named supervisor and is managed through the smaller insurer regime at the Prudential Regulation Authority.

A1.5 Auditors

The independent statutory auditor of the Society is RSM UK Audit LLP and can be contacted as follows:

RSM UK Audit LLP
Chartered Accountants
St Philips Point
Temple Row
Birmingham
B2 5AF

A1.6 Lines of business

All of the Society's business risks and returns are within one business segment i.e. long term with-profits regular savings plans with life and/or disablement cover. All of the Society's business is transacted in the United Kingdom, although members may move overseas subsequent to taking out a policy. The split of in force business by product and premium income is as follows:

£000	2016 (53 weeks)	2015 (52 weeks)
Saver and Disability Plan	2,695	2,671
Saver Plan	1,529	1,372
Children's Saver Plan	332	318
total gross premiums written	4,556	4,361

For Solvency II purposes, all the Society's activity is classed as 'Insurance with profit participation'.

A1.7 Significant business events during the year

A key priority for the Society during 2016 was the implementation of Solvency II. This was probably the most significant regulatory change that the Society has had to implement in its history. It has been a major focus for the Society's management team and professional advisors, including our actuary, fund manager and statutory auditor. It has unfortunately led to an increase in our regulatory compliance costs.

A significant impact on the Society's financial position during 2016 was the reduction in the risk-free rates provided by the European Insurance and Occupational Pensions Authority, which are used to calculate the investment returns within the actuarial valuation. The change in risk-free rates compared to 2015 caused an increase in the technical provisions of £1,538k as at 31 December 2016.

A further significant event during 2016 was the fall in the value of sterling against the euro. The euro-sterling exchange rate published by the European Union on 31 October 2016 showed that the euro had reached 90.05 pence. This had the effect of increasing the Society's Minimum Capital Requirement by £675k between 31 December 2015 and 31 December 2016.

2016 also saw significant fluctuations in the investment markets, which have impacted the Society's investment portfolio. The UK referendum on membership of the European Union in June followed by the US presidential election in November brought political uncertainties that concerned investors. However, by the end of the year there had been significant increases in both the equity and bond markets. The Bank of England base rate fell to a historic low of 0.25% on 4 August.

A2 Underwriting performance

A2.1 Premiums and Claims

The table below shows the Society's premiums and claims for the year:

£000	2016	2015
gross premiums	4,556	4,361
reinsurers' share of premiums	0	0
gross claims	4,048	3,966
reinsurers' share of claims	0	0

Underwriting and reserving risks arise within with-profits business due to fluctuations in persistency, expenses and claims rates relative to the actuarial assumptions made in the pricing process. These risks are managed by the Society through its Underwriting Arrangements Policy. The permitted classes and characteristics of business to be written are discussed by the Management Committee at least annually. The capacity to accept new business is determined by the Society's available capital resources, in accordance with the Own Risk and Solvency Assessment process. The pricing of the Society's products is reviewed on a periodic basis, taking account of underwriting data and experience and in accordance with the professional advice of the Chief Actuary. The Society has robust underwriting arrangements in place, which include prospective policyholders being required to declare any pre-existing conditions and, in relation to disability plan business, to provide evidence that they carry out safety critical functions on the railway. Due to the nature of business transacted, the Society does not use reinsurance arrangements. The Society's lack of reinsurance arrangements is consistent with its risk appetite. They are not required to mitigate the volatility of capital. There is therefore no allowance for reinsurance in the estimation of technical provisions. Exposure of the Society's portfolio to catastrophic claims experience is considered by the Management Committee as part of its annual reverse stress testing discussion.

A2.2 Operating Expenses

The other significant financial values are the Society's operating expenses; these are set out below:

£000	2016	2015
acquisition costs	199	223
administrative expenses	964	688
total operating expenses	1,163	911

There was a small reduction in acquisition costs. This was largely attributable to a decrease in payments made to Area Representatives and Depot Introducers in line with a reduction in new business in 2016 compared to 2015. There was a significant increase in administrative expenses. The principal reasons for this are as follows:

- There was a significant increase in actuarial and audit fees arising from the implementation of Solvency II.
- There were significant additional costs associated with the Chief Executive succession.
- Management Committee costs also increased due to a revised fee structure for Non-Executive Directors that came into force during the year.

The Society does not have any material leasing arrangements.

A3 Investment performance

Performance for the year ended 31 December 2016 and for the prior year is as follows:

£000	interest & dividends receivable 2016	realised gain/(losses) 2016	unrealised gains/(losses) 2016	total 2016	total 2015
government bonds	279	188	195	662	73
corporate bonds	341	117	343	801	93
equities	181	(87)	514	608	378
collectives	61	(45)	417	433	202
cash and cash equivalents	0	10	2	12	0
loans and mortgages	74	0	0	74	78
investment property	67	0	45	112	(17)
total	1,003	183	1,516	2,702	807

Investment costs for the various categories were as follows:

£000	investment costs	
	2016	2015
government bonds	91	85
corporate bonds		
equities		
collectives		
cash and deposits	0	0
loans and mortgages	0	0
investment property	6	3

A4 Performance of other activities

The Society does not carry out any other activities.

A5 Other material information

No other material information is necessary to give a full picture of the Society's business and performance.

B System of governance

B1 General information on the system of governance

The Society operates under the direction of the Management Committee, with day-to-day operational management delegated to the Chief Executive and other senior managers. The strategic direction of the Society, performance against annual and long-term plans and targets, monitoring of the business and reviewing the work of Sub-committees is within the remit of the Management Committee.

The core responsibilities of the Management Committee are to:

- ensure that the Society operates within the established framework of an effective system of internal control, risk management, governance and compliance;
- ensure that the solvency capital requirements and minimum capital requirements are maintained at all times;
- determine the strategy and approve the business plan;
- ensure that the business is conducted in an efficient and effective manner and that the interests of members are at the heart of everything the Society does; and
- assist approved persons (including those carrying out controlled functions and/or those subject to the Senior Insurance Managers Regime) to discharge their responsibilities in respect of the area of the business for which they are responsible.

There are certain decision-making powers that are reserved for the Management Committee. These include:

- declaration of bonus rates
- approval of the Annual Report and Accounts
- approval of the Own Risk and Solvency Assessment (ORSA)
- setting the remuneration of the Society's Chief Executive, other senior managers and staff
- appointment and dismissal of the Chief Executive
- approval of the Business Plan and budgets
- acquisition / disposal of significant assets

The Management Committee comprised seven members at 31 December 2016, all of whom were non-executive directors. The Annotated Corporate Governance Code for mutual insurers recommends that Boards should comprise a mix of executive and non-executive members. From February 2017, the incoming Chief Executive has taken on an executive director role as a member of the Management Committee. The Society also has an Audit and Risk Management sub-Committee and a With-Profits Advisory Arrangement. The Chief Executive is responsible for overseeing all activities of the Society and refers material matters to the Management Committee.

B1.1 Membership of the Management Committee

The following individuals were members of the Management Committee as at 31 December 2016:

J W Goolamier	Chair
R G Frier	Deputy Chair
A Edwards	Senior Independent Director
J McKenna	Chair of Audit and Risk Management sub-Committee
M A Casey	Chair of With-Profits Advisory Arrangement
L P Davies	
R T Brushfield-Hodges	

B1.2 Audit and Risk Management sub-Committee

The main responsibilities of the Audit & Risk Management sub-Committee are to:

- review the effectiveness of the Society's financial reporting;
- review the system of internal control;
- review the arrangements for identifying and evaluating risks in relation to the Society's current and future activity in accordance with the Business Plan;
- monitor the effectiveness of the external audit process including a review of the external auditors' appointment, fees and independence; and
- monitor the role and effectiveness of the internal audit function.

The Audit & Risk Management sub-Committee met five times during the year and senior management also attended those meetings. On two occasions, the external auditors were present and, on three occasions, representatives from the internal audit firm attended. The sub-Committee has unfettered access to both the internal and external auditors and, equally, the audit firms have right of access to the sub-Committee and to the Management Committee as deemed appropriate. In addition to monitoring the external audit from the outset of the planning stage, the sub-Committee also considers the significant findings and recommendations arising from the audit of the Society's annual report and accounts. The independence of the external audit function is monitored by the sub-Committee. The terms of reference of the Audit & Risk Management sub-Committee are available on the Society's website.

B1.3 Membership of the Audit and Risk Management sub-Committee

The following individuals were members of the Audit and Risk Management sub-Committee as at 31 December 2016:

J McKenna	Chair
M A Casey	
A Edwards	
R G Frier	

B1.4 With-Profits Advisory Arrangement

The purpose of the With-Profits Advisory Arrangement (WPAA) is to protect the interests of with-profits policyholders and ensure that the With-Profits Fund is managed in accordance with the Principles and Practices of Financial Management (PPFM). The WPAA is advisory in nature i.e. it is not a decision-making body; instead, its role is to inform the decision making of the Management Committee.

The main responsibilities of the With-Profits Advisory Arrangement are:

- to assess, report on and provide advice to the Management Committee on the manner in which the with-profits business is administered in accordance with the PPFM;
- to review the way in which the Management Committee exercises its discretion in the management of the With-Profits Fund including matters relating to the calculation and application of asset shares, smoothing and bonus calculations;
- to challenge any significant changes to the risk profile or investment strategy of the Society; and
- to assess the performance of the With-Profits Actuary.

B1.5 Membership of the With-Profits Advisory Arrangement

The following individuals were members of the With-Profits Advisory Arrangement as at 31 December 2016:

M A Casey	Chair
L P Davies	
R G Frier	

B1.6 Key functions

The Society follows 'fit and proper person' principles to ensure that key functions are led by appropriately skilled people. All outsourced services are reviewed periodically and, when considered appropriate, are re-tendered or re-negotiated.

Key Function	Provider	Key roles and responsibilities and how they report to the Management Committee
Internal Audit	outsourced – CK Chartered Accountants	The Internal Audit function is delivered through an outsourced arrangement by a regional firm of Chartered Accountants. The purpose of Internal Audit is to provide the Audit and Risk Management sub-Committee with assurance on whether the Society's risk management, internal control and governance processes are operating effectively to protect the assets, reputation and sustainability of the Society. Internal Audit is authorised to have full and complete access to any of the Society's records and personnel. It can decide which audits to perform, the scope, frequency and timing of its work, the procedures it follows and the content of its reports. The Chief Executive, as Head of Internal Audit (SIMF 5), has overall responsibility for ensuring that there is an adequate and effective internal audit function in place. Because internal audit is currently delivered under an outsourced arrangement, the people that carry out the audits are independent from the staff that work in the areas under review. The Chief Executive plays no part in managing or directing the Internal Audit staff. Further information regarding Internal Audit is contained in section B5.

Key Function	Provider	Key roles and responsibilities and how they report to the Management Committee
Risk Management	in-house	The Risk Management function is delivered in-house. The Finance Manager, as Chief Risk Officer (SIMF 4), has primary responsibility for the Society's overall risk management arrangements and reports to the Audit and Risk Management sub-Committee in this capacity. Within the limitations of a small society, the Society has adopted Three Lines of Defence principles in its risk management framework. The First Line of Defence is the day-to-day management activity, checking and validation carried out in accordance with policies and procedures. The Management Team, led by the Chief Executive, is responsible for the First Line of Defence. The Second Line of Defence is the Risk Management function, which seeks to ensure conformity with risk, actuarial and compliance policies and procedures. The Finance Manager, as Chief Risk Officer is responsible for the Second Line of Defence. The Third Line of Defence is the Internal Audit function, which provides an independent, objective and critical assessment of the design and effectiveness of the Society's internal control, risk management and governance arrangements. The Chief Executive, as Head of Internal Audit, is responsible for the Third Line of Defence. The Chief Executive plays no part in managing or directing the internal audit staff. Further information regarding Risk Management is contained in section B3.

<table>
<tr><th>Key Function</th><th>Provider</th><th>Key roles and responsibilities and how they report to the Management Committee</th></tr>
<tr><td>Actuarial</td><td>outsourced – Steve Dixon Associates LLP</td><td>The actuarial function is delivered through an outsourced arrangement. The roles of Chief Actuary (SIMF 20) and With-Profits Actuary (SIMF 21) are currently held by the same person. The Chief Actuary reports to the Management Committee and Audit and Risk Management sub-Committee. The With-Profits Actuary reports to the Management Committee and the With-Profits Advisory Arrangement.

The specific responsibilities of the Chief Actuary are to:
• calculate the Society's Technical Provisions and Solvency Capital Requirement;
• identify and carry out stress and scenario testing, including reverse stress testing, based on input from senior management and the Management Committee;
• assess the suitability of using standard formula methodology to calculate the Society's Solvency Capital Requirement;
• undertake the risk modelling underlying the calculation of the capital requirements of the Society;
• prepare the Society's Forward Looking Assessment of Solvency; and
• issue an opinion on the adequacy of the Society's underwriting policy and reinsurance arrangements.

The specific responsibilities of the With-Profits Actuary are to:
• advise the Management Committee on key aspects of discretion to be exercised in the administration of the With-Profits Fund;
• advise the Management Committee as to whether the assumptions used to calculate the future discretionary benefits within the technical provisions are consistent with the Principles and Practices of Financial Management; and
• report to the Society's With-Profits policyholders as to whether the discretion exercised by the Society in respect of the period covered by the annual report may be regarded as taking the interests of the relevant classes of the Society's With-Profits policyholders into account in a reasonable and proportionate manner.

Further information regarding the Actuarial Function is contained in section B6</td></tr>
</table>

Key Function	Provider	Key roles and responsibilities and how they report to the Management Committee
Compliance	in-house with external support	The compliance function is delivered in-house with support from a risk management consultant. Regulatory responsibility for the Compliance Oversight Function (CF10) is shared between the Chief Executive and the General Manager. The compliance function helps to ensure that the Society manages its regulatory risk exposure effectively. The Society employs a retail compliance officer to undertake checks on new policies sold through the Area Representative / Depot Introducer network. The results of this activity are reported to the Management Committee periodically during the year. Training on compliance is provided to Management Committee members, senior managers, head office staff and Area Representatives, at least annually. The Society periodically commissions a review of its compliance arrangements by an external consultant. The results of this review are reported to the Management Committee. Further information regarding the compliance function is contained in section B4.

B1.7 Changes to system of governance during 2016

2016 saw the creation of the With-Profits Advisory Arrangement, the purpose of which is to protect the interests of with-profits policyholders and ensure that the With-Profits Fund is managed in accordance with the Principles and Practices of Financial Management (PPFM).

The Society also strengthened its Management Committee through the appointment of a qualified actuary.

There were no other material changes to the system of governance.

B1.8 Remuneration policy

The principles underlying the remuneration policy of the Society apply to all employees. These include the following:

- The total remuneration package needs to be sufficient to attract and retain high-calibre individuals, whilst demonstrating value for money to the Society.
- The remuneration package should be appropriately constructed so that it contributes to the retention and motivation of key individuals.
- Remunerations packages should reflect the individual's role, responsibilities and performance.

All employees receive a fixed salary that is appropriate to their role. The Society does not use annual bonuses, long-term incentive plans or any other form of variable pay structure. All employees are eligible to join the Society's Group Personal Pension Scheme. The Society does not operate supplementary pension or enhanced early retirement arrangements.

Non-Executive members of the Management Committee are remunerated by way of an annual fee and a meeting attendance allowance. In addition, reasonable expenses incurred in the course of Society business are reimbursed. Non-Executive members are not entitled to join the pension scheme.

B1.9 Transactions with Committee Members, Officers and their close family members

The following transactions have been undertaken as part of the normal business of the Society. These transactions were originally made on the same terms and conditions as applicable to other members of the Society, or on commercial terms.

life assurance policies	2016 persons	2016 amount £	2015 persons	2015 amount £
premiums paid during the year	12	18,626	11	14,374
total sum assured at 31 December	10	255,494	10	237,066

Payments of £1,679 (2015: £1,003) were made in 2016 to some Committee members in relation to their duties as Depot Introducers.

During the year, Mr Roger Frier had a mortgage with the Society. Interest of £13,036 (2015: £13,427) was charged. At 31 December 2016, £266,064 (2015: £259,984) was owed to the Society in respect of the mortgage.

During the year, Mr Terry Brushfield-Hodges was paid £12,193 (2015: £11,909) and Mr Roger Frier was paid £4,608 (2015: £5,562) for consultancy services provided to the Society.

B2 Fit and Proper requirements

B2.1 Skills, knowledge and expertise

The Society has arrangements in place to ensure that its Management Committee and Senior Managers collectively possess the skills, qualifications and experience to provide sound and prudent management of the Society. The key areas of knowledge are:

- insurance and financial services
- business strategy and business model
- solvency II requirements
- financial and actuarial analysis
- statutory and regulatory requirements

An independently facilitated Management Committee evaluation is carried out periodically to ensure that those charged with the Society's governance possess the attributes required in the regulated financial services industry. Skills gaps or areas for development that are identified through this process are addressed through the provision of training or, where appropriate, through the recruitment of additional Committee members.

B2.2 Fitness and propriety of persons

The Society has arrangements in place to ensure that its Management Committee and Senior Managers meet the regulatory 'fit and proper' requirements. The following factors are taken into account when deciding whether an individual is fit and proper:

- honesty, integrity and reputation;
- competence and capability;
- financial soundness

The Society employs the following procedures, as deemed appropriate, to the nature of the appointment to assess fitness and propriety:

- annual self-declaration
- annual credit reference agency checks
- professional qualifications check
- FCA Register search

B2.3 Controlled Function holders

The following persons were responsible as at 31 December 2016 for carrying out the key functions:

Controlled Function		name
SIMF 1	Chief Executive Officer	Robert Leddington
SIMF 2	Chief Finance Officer	Lynsey Inglis
SIMF 4	Chief Risk Officer	Lynsey Inglis
SIMF 5	Head of Internal Audit	Robert Leddington
SIMF 9	Chair	Joe Goolamier
SIMF 11	Chair of the Audit Committee	Joe McKenna
SIMF 14	Senior Independent Director	Alan Edwards
SIMF 20	Chief Actuary	Alison Carr
SIMF 21	With-Profits Actuary	Alison Carr
CF10	Compliance Oversight	Robert Leddington / Victoria Herbert
CF11	Money Laundering Reporting	Robert Leddington

B3 Risk management system including Own Risk and Solvency Assessment

B3.1 Risk management framework

Effective risk management is fundamental to the Society's strategy as it protects our members' funds, ensures the efficient use of capital and helps to deliver our Business Plan. Risk Management was further strengthened during 2016 through the embedding of our Own Risk and Solvency Assessment (ORSA) process. The Society manages its risks within a defined framework. The framework comprises the Risk Appetite Statement, the Capital Assessment of Risks and the Risk Register. Ultimate responsibility for identifying and managing the risks faced by the Society rests with the Management Committee whilst the Audit and Risk Management sub-Committee has responsibility for the detailed scrutiny of risk management issues.

B3.2 Risk identification

The Society assesses its risks on an ongoing basis throughout the financial year. Key risks, and the mitigating actions and controls in place to manage the risks, are recorded in the Risk Register, which is maintained by the Finance Manager, in her capacity as Chief Risk Officer.

B3.3 Risk appetite, tolerances and limits

The Society's Risk Appetite is determined by the Management Committee and is reviewed on a regular basis as new risks emerge, or at least annually. The Risk Appetite Statement is translated into risk thresholds and risk trigger points, which are used to manage the Society's solvency.

B3.4 Three Lines of Defence

Within the limitations of a small society, the Society has adopted Three Lines of Defence principles in its risk management framework. The First Line of Defence is the day-to-day management activity, checking and validation carried out in accordance with policies and procedures. The Management Team, led by the Chief Executive, is responsible for the First Line of Defence. The Second Line of Defence is the Risk Management function, which seeks to ensure conformity with risk, actuarial and compliance policies and procedures. The Finance Manager, as Chief Risk Officer is responsible for the Second Line of Defence. The Third Line of Defence is the Internal Audit function, which provides an independent, objective and critical assessment of the design and effectiveness of the Society's internal control, risk management and governance arrangements. The Chief Executive, as Head of Internal Audit, is responsible for the Third Line of Defence, but plays no part in managing or directing the internal audit staff, who have complete operational independence.

B3.5 Own Risk and Solvency Assessment (ORSA)

The Society's ORSA is a rolling process that provides a detailed analysis of the Society's capital adequacy, risk management and forward looking perspective. This is achieved using a combination of internal, actuarial and regulatory documents and information to report appropriately on the Society's financial position. The ORSA is carried out in accordance with the ORSA Policy agreed by the Management Committee. The intention of the Society's ORSA is to develop an understanding of the risks that the Society is exposed to and the associated capital requirements, thereby improving business decision-making processes.

B3.6 Capital requirements

A key element of the ORSA is an assessment of the Society's capital requirements. The Society uses the standard formula methodology as outlined in the Delegated Text and associated guidelines. Further information on this is provided in section E.

B3.7 Own Risk and Solvency Assessment programme of review

The ORSA is undertaken throughout the year in a way that is dovetailed with the business decision-making cycle, culminating in an annual ORSA submission to the Prudential Regulation Authority. The scheduled review programme for the various elements of the ORSA is as follows:

<table>
<tr><td>section of ORSA</td><td>frequency of review</td></tr>
<tr><td>Financial Performance</td><td>three times per year</td></tr>
<tr><td>Risk Appetite Statement</td><td>annually</td></tr>
<tr><td>Capital Assessment of Risks</td><td>annually</td></tr>
<tr><td>Risk Register</td><td>annually</td></tr>
<tr><td>Business Plan</td><td>annually</td></tr>
<tr><td>Actuarial Reporting:
Solvency II Technical Provisions and Capital Requirements
Suitability of Standard Formula Stresses to Measure Risk
Forward Looking Assessment of Solvency
Reverse Stress Testing</td><td>annually</td></tr>
<tr><td>Investment Policy</td><td>annually</td></tr>
<tr><td>Disaster Recovery Plan</td><td>annually</td></tr>
<tr><td>Corporate Control Manual</td><td>annually</td></tr>
</table>

In addition, the ORSA is reviewed if any significant events occur or risks emerge that could impact the ability of the Society to achieve its Business Plan. Examples of significant events or emerging risks include:

- significant falls in asset values
- significant reduction in the risk-free discount rate, potentially leading to increased technical provisions
- increase in the sterling value of the Minimum Capital Requirement
- mass surrenders of policies

At any point where a threshold in the Risk Appetite Statement is breached, an automatic review of the ORSA will be triggered. The most recent ORSA submission to the Prudential Regulation Authority was in December 2016.

B3.8 Governance of the ORSA

The Management Committee has ownership and ultimate responsibility for the ORSA, including the appropriateness and completeness of the processes and procedures and the approval of the disclosures and submissions to the Prudential Regulation Authority. The Management Committee is responsible for determining the Society's overall risk appetite. The Audit and Risk Management sub-Committee has a role in undertaking detailed scrutiny of the ORSA, including the Risk Appetite Statement, the Capital Assessment of Risks and the actuarial assumptions prior to submission for formal approval by the Management Committee. The Society's Finance Manager carries out the Senior Insurance Management Function of Chief Risk Officer and as such is responsible for the maintenance of the Society's risk management processes and procedures, for the accuracy of the financial data underlying the ORSA and for ensuring the continuous adequacy of the solvency of the Society through appropriate capital management. The Chief Actuary has a key role in the preparation of specific reports in the ORSA and for the provision of technical actuarial advice.

B4 Internal control and compliance arrangements

B4.1 Internal control system

The Society's internal control arrangements are designed to provide reasonable assurance as to the reliability of the Society's financial reporting, to ensure compliance with applicable statutory and regulatory requirements and to provide for the economic, efficient and effective management of the Society's business.

The Management Committee has ultimate responsibility for the maintenance of adequate and effective internal control, risk management and governance arrangements. It is supported in this by the Audit and Risk Management sub-Committee. Day-to-day responsibility for the design and maintenance of the internal control system rests with the Chief Executive and other senior managers.

The Society's internal control arrangements are subject to annual review by the Internal Audit function, the results of whose work is reported to the Audit and Risk Management sub-Committee.

The Society's financial statements are subject to strong internal controls in their preparation prior to audit by the Society's statutory auditor. They are also subject to detailed scrutiny by the Audit and Risk Management sub-Committee and formal approval by the Management Committee ahead of submission to the Regulator and publication to the membership. The technical provisions are derived by the Chief Actuary and are subject to scrutiny by a reviewing actuary, who is appointed by the statutory auditor.

Key elements of the Society's internal control system include:

Reconciliation procedures	These include the preparation and review of bank reconciliations and the reconciliation of the general ledger.
IT controls	These include processing controls, security of data and systems, authorisation and access controls, back up procedures, anti-virus, firewall protection, disaster recovery arrangements, control over systems developments and changes and business continuity planning.
Management information	This includes the monthly reports prepared for the Management Committee on investment performance, new business volumes, claims etc.
Segregation of duties	This includes the processes for the initiation and authorisation of payments.
Data controls	This includes the checking and reconciliation of policy data to ensure the completeness and accuracy of the data upon which the actuarial valuation is undertaken.
Physical security	This includes the access to the office premises and the locking away of cheque books and other sensitive documents.
Treating Customers Fairly	This is embedded and evidenced by a monthly report by the General Manager to the Management Committee.

Internal Audit, through its planned work, provides an opinion at least annually to the Audit and Risk Management sub-Committee on the adequacy of the Society's system of internal control.

B4.2 Implementation of the Compliance Function

The compliance function is delivered in-house with support from a risk management consultant. Regulatory responsibility for the Compliance Oversight Function (CF10) is shared between the Chief Executive and the General Manager.

The compliance function helps to ensure that the Society manages its regulatory risk exposure effectively.

The Society employs a retail compliance officer to undertake checks on new policies sold through the Area Representative / Depot Introducer network. The results of this activity are reported to the Management Committee periodically during the year. Training on compliance is provided to Management Committee members, senior managers and staff, at least annually. The Society periodically commissions a review of its compliance arrangements by an external consultant. The results of this review are reported to the Management Committee.

B5 Internal Audit Function

B5.1 Implementation of the Internal Audit Function

The purpose of the Society's Internal Audit function is to provide the Audit and Risk Management sub-Committee with assurance on whether the Society's risk management, internal control and governance processes are operating effectively to protect the assets, reputation and sustainability of the Society. Doing this helps to improve the effectiveness of these processes.

All of the Society's activities (including outsourced activities) are within the scope of Internal Audit. Internal Audit carries out an Audit Needs Assessment (ANA) to determine which areas of activity need to be subject to internal audit scrutiny and the frequency with which a review is carried out over the cycle of the Internal Audit strategy. The ANA is used to direct internal audit resources to those areas of the Society's operations that are assessed as generating the greatest risk to the achievement of its objectives. Internal Audit takes a risk based approach and does not necessarily have to cover all of the potential scope areas every year. Its focus may change in light of emerging risks and Internal Audit's ongoing assessment of risk. Internal Audit can also, where appropriate, undertake special investigations and consulting arrangements at the request of the Audit and Risk Management sub-Committee, Management Team or regulators. Internal Audit seeks to co-ordinate its activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimise duplication of efforts.

Internal Audit is currently delivered under an outsourced arrangement by a regional firm of Chartered Accountants. This means that the people that carry out the audits and report the findings to the Audit and Risk Management sub-Committee are independent from the staff that work in the areas under review. The Chief Executive as Head of Internal Audit (SIMF 5) is responsible for ensuring that there is an adequate and effective internal audit function in place. He is also the primary operational contact between Internal Audit and the Society on a day-to-day basis. However, in accordance with the principles of auditor independence, he plays no part in directing or managing the internal audit staff.

B5.2 Independence of the Internal Audit Function

The Internal Audit function derives its authority from the Management Committee through the Audit and Risk Management sub-Committee. The Internal Audit function is authorised by the Audit and Risk Management sub-Committee to have full and complete access to any of the Society's records and personnel. The Internal Audit function, under the governance of the Audit and Risk Management sub-Committee, is free to decide which audits to perform, the scope, frequency and timing of its work, the procedures it follows and the content of its reports. The Internal Audit function does not have any operational responsibility or authority over any of the activities audited. It is not responsible for the implementation of internal controls, the development of procedures, the installation of systems, the preparation of regulatory submissions or any other activity that may impair, or be perceived to impair, its objectivity.

B6 Actuarial Function

The Society has an Actuarial Function, which is wholly outsourced. The roles of Chief Actuary (SIMF 20) and With-Profits Actuary (SIMF 21) are held by Alison Carr of Steve Dixon Associates LLP, who is a Fellow of the Institute of Actuaries.

The Actuarial Function produces a range of written reports to the Management Committee annually. These include:

- summary of the data used for the annual valuation
- advice on the basis, assumptions and methodology used to calculate the technical provisions and solvency capital requirement of the Society
- results of the annual valuation
- With-Profits Actuary report setting out advice on the level of bonus that could be granted to members of the Society
- review of factors used to calculate surrender claim amounts
- Forward-Looking Assessment of Solvency
- Reverse Stress Testing
- opinion on underwriting policy and reinsurance arrangements
- review of Investment Policy

B7 Outsourcing

The policy of the Society is that its core policy administration, information systems and finance functions are managed in-house. Outsourcing is generally restricted to key areas where either professional expertise is not available from within the Society's own resources or where third-party provision of a service or function is preferable, for example to help demonstrate independence.

The key areas where functions are currently outsourced are:

- Internal Audit
- Actuarial function
- Fund Management
- Investment Property Management

All outsourced providers are based in the United Kingdom.

In the case of actuarial services, the outsourcing relationship is such that an external third-party undertakes the regulatory SIMF roles of Chief Actuary and With-Profits Actuary. For all other outsourced services where there is an associated SIMF or CF role, a member of the Society's senior management holds the regulatory position.

In determining the award of an outsourced contract the Society undertakes due diligence to establish a provider's financial stability and track record in providing similar services. In this regard, background endorsements are sought from amongst the Society's friendly society peer group.

When the Society enters into outsourced arrangements, contracts for services, except in exceptional circumstances, do not extend beyond one year. Notice periods are normally one year or less, depending on the nature of the services. All outsourced services are reviewed periodically and, when considered appropriate, are re-tendered or re-negotiated.

In recent years, the Society has changed the outsourced provider of the fund management function.

B8 Assessment of system of governance

The Management Committee has performed a self-assessment of its system of governance against the requirements of the Annotated Corporate Governance Code issued by the Association of Financial Mutuals. The outcome of this self-assessment is contained in the Corporate Governance Report within the Society's published Annual Report and Accounts.

B9 Other material information

No other material information is necessary to give a full picture of the Society's system of governance.

C Risk Profile

C1 Risk management framework

The Society manages its risks within a defined framework. The framework comprises the Risk Appetite Statement, the Capital Assessment of Risks and the Risk Register. Ultimate responsibility for identifying and managing the risks faced by the Society rests with the Management Committee whilst the Audit and Risk Management sub-Committee has responsibility for the detailed scrutiny of risk management issues. The Finance Manager, as Chief Risk Officer (SIMF 4), has primary responsibility for the Society's overall risk management arrangements, including the maintenance of adequacy levels of solvency.

C2 Prudent Person Principle

The Society invests its assets in accordance with the 'prudent person principle' as set out in Article 132 of the Directive 2009/138/EC. The fund manager operates in accordance with the Investment Policy, which specifies the type of investments that they are allowed to invest in, the minimum and maximum proportions allowable, the maximum exposure to overseas holdings, the required modified duration of bonds and their levels of credit rating. The Society's Management Committee undertakes regular reviews of the performance of the fund manager and reviews the Investment Strategy at least annually. The Society's Principles and Practices of Financial Management (PPFM) document sets out how the Society conducts its With-Profits business. The PPFM makes reference to the Investment Strategy of the Society, the purpose of which is to maximise the overall return of the investments of the Society subject to ensuring that guarantees are met through maintaining adequate solvency and liquidity.

C3 Risk sensitivity

For the key risks that the Society is exposed to, the sensitivity of the Society's surplus assets is investigated annually and the detailed results are contained in a Forward-Looking Assessment of Solvency report. The sensitivities that are examined include changes in new business levels, higher lapses, higher mortality and morbidity, higher expenses and changes in the value of assets and bond yields.

C4 Overview of key risks

An overview of the principal risks associated with the business including an outline of how they are each managed is provided below.

C4.1 Underwriting risk

Life underwriting risk considers the risks arising from the underwriting of the Society's policies. The Solvency Capital Requirement for underwriting risk is quantified in section E2.2.

C4.1.1 Mortality

This stress covers the loss or change in technical provisions following a permanent 15% increase in the expected mortality.

C4.1.2 Longevity

This stress covers the loss or change in technical provisions following a permanent 20% decrease in the expected mortality. As the effect for the Society is to reduce liabilities and have no effect on assets, the stress is therefore assumed to be nil.

C4.1.3 Morbidity

This stress covers the loss or change in technical provisions following a permanent increase in expected morbidity. The disability inception stress is based on 35% increase in disability claims in the first 12 months from the valuation date and then 25% thereafter.

C4.1.4 Lapse

This stress covers the change in technical provisions as a result of the unexpected change in policyholder surrenders and lapses.

The lapse stress is based on three scenarios, with the scenario having the greatest impact on total liabilities being used to calculate the additional capital to cover lapse risk:

- future lapses 50% higher than expected
- future lapses 50% lower than expected
- mass lapse of 40% of in-force business, a one-off event

C4.1.5 Expense

This stress covers the risk of expense levels of administering the in-force policies being higher than assumed. This can arise from an increase in expenses through inflation or unexpected costs. The expense stress is a permanent 10% increase in administration expenses plus a 1% increase per annum in expense inflation.

C4.1.6 Life Catastrophe

This stress relates to the risk of loss or change in the technical provisions relating to the outbreak of major epidemics as well as the unusual accumulation of risks under extreme circumstances. The life catastrophe stress is a 0.15% increase in mortality rates for each policy where the payment of benefits is dependent on the policyholders' death.

C4.1.7 Underwriting risk mitigation

This Society's approach to underwriting aims to protect members from external anti-selection factors and means that if a policyholder has a pre-existing condition, they would not be able to claim for death or disablement due to that condition.

C4.2 Market risk

Market risk is the risk that the value of a financial instrument will fluctuate because of the volatility of market prices.

The market risk module considered for the Society's asset portfolio consists of the asset stresses discussed below, with the Solvency Capital Requirement for market risk quantified in section E2.3.

C4.2.1 Interest rate

This stress allows for movements in the risk-free rates, used in the valuation of the technical provision. The impact of the change in risk-free rates is measured against both the assets and liabilities.

C4.2.2 Equity

The Solvency II Delegated Act requires an immediate fall of 39% plus a symmetric adjustment for equities listed on regulatory markets in countries that are members of the EEA or OECD (and 49% for other equities), although the Society has taken advantage of the ability to assume a lower stress for purchases made prior to 1 January 2016.

C4.2.3 Property

The asset stress allows for an instantaneous fall of 25% in the value of property, including property held via collective investment schemes.

C4.2.4 Currency

The currency risk takes into account the impact of a sharp rise or fall in the currency exchange rates. The currency stress allows for an instantaneous fall of 25% in the sterling market value of non-sterling assets.

C4.2.5 Spread

The spread is an additional return over the risk-free rate earned on bonds and is representation of the riskiness of bond returns.

C4.2.6 Concentration

Concentration risk considers the impact of a large exposure with a particular counterparty.

C4.2.7 Correlation

The Implementing Rules take into account the diversification within the asset portfolios by using a correlation matrix. This is because it is unlikely that all these risks (major and individual) will occur simultaneously.

C4.2.8 Market risk mitigation

The Society calculates its solvency position at least monthly and if the free assets figure falls below its trigger point for action then the solvency position is calculated daily. If the position worsens then the fund manager would be consulted with a view to realigning the investment portfolio so that the Society's risk threshold is not breached.

C4.3 Counterparty default risk

The counterparty default risk module considers the risk of potential losses due to unexpected default, or deterioration in the credit standing of counterparties and debtors over the ensuing year. The method given within the Implementing Rules assesses the probabilities of default and losses given default based on current credit ratings. The Solvency Capital Requirement for counterparty default risk is quantified in section E2.4.

C4.3.1 Counterparty default risk mitigation

Credit risk in relation to financial investments is managed by ensuring that the fund manager avoids excessive exposure to any one single counterparty. Additionally, the maximum exposure to fixed income holdings of different ratings is specified to ensure that the Society is not exposed to undue risk.

C4.4 Liquidity risk

Liquidity risk is the risk that the Society, though solvent, does not have sufficient financial resources to enable it to meet its obligations as they fall due. The Society's exposure to liquidity risk is considered to be low, since it maintains a high level of liquid assets to meet its liabilities. As at 31 December 2016, the Society had cash holdings of £742,806. In addition, £29,453,153 or 92% of the Society's total investments of £31,968,373 were held in a form that could easily be made liquid. The only significant investments that are considered illiquid are the investment properties, policy loans and mortgages.

The Solvency Capital Requirement does not include any allowance for liquidity risk.

C4.5 Operational Risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, or from personnel and systems, or from external events. The capital requirement for operational risk uses a formulaic approach based on either office premiums or technical provisions, which is quantified in section E2.6.

The significant operational risk issues faced by the Society are summarised below.

C4.5.1 Regulatory Compliance

Failure to comply with regulatory requirements would have a significant impact on the Society, including the prospect of regulatory intervention, increased expense and reputational damage. This risk is mitigated by having robust governance processes and internal controls and a strong compliance culture. Internal controls are subject to regular checking by internal audit. Regulatory compliance is also reviewed periodically and reported to the Management Committee. The Society continues to respond positively to increased regulatory requirements, in particular those emanating from the Solvency II Directive and Senior Insurance Managers Regime. During 2016, the Society made substantial progress by embedding its Own Risk and Solvency Assessment into its business decision making and governance processes. Non-executive challenge and support was strengthened through the appointed of a qualified actuary to the Management Committee.

C4.5.2 Inability to adapt to potential changes to legislation surrounding with-profits business

Potential changes to legislation surrounding with-profits business could have an adverse impact on the Society's new business levels. The Society is starting to prepare for the changes to regulations surrounding Packaged Retail and Insurance Based Investment Products (PRIIPS). The Society's membership of the Association of Financial Mutuals means that it is kept up to date on the development of government policy in this area.

C5 Other material risks

No further material risks have been identified.

C6 Other material information

No other material information is necessary to give a full picture of the Society's risk profile.

D Valuation for solvency purposes

D1 Valuation of assets

The table below details the basis for the Society's Solvency II asset valuation for each material class of assets. Assets are measured on a market value basis as at 31 December 2016.

	Solvency II £'000	Financial Statements £'000
Investment Property	1,604	942
Office Property, Plant and Equipment	322	322
Financial Investments	29,241	29,453
Loans and Mortgages	1,273	1,273
Cash and cash equivalents	522	743
Insurance receivables	404	404
Any other assets, not elsewhere shown	231	460
Total assets	33,597	33,597

D1.1 Investment Property

For Solvency II purposes the investment properties have been valued at fair value, this is the same basis as the financial statements, which follow UK GAAP. Full valuations are made by an independent, professionally qualified surveyor, on an annual basis.

For Solvency II purposes, any Real Estate Investment Trusts (REITs) held directly have also been included in the investment property asset category. The REIT value is taken at market value as at 31 December 2016 and then increased by the loan to value ratio. The increased value is assumed to be supplemented by cash deposits.

D1.2 Office Property, Plant and Equipment

The office property is valued at fair value. This is the same basis for Solvency II purposes as the financial statements, which follow UK GAAP. A full valuation is made on an annual basis by an independent, professionally qualified surveyor.

Plant and equipment is stated at cost less accumulated depreciation.

D1.3 Financial Investments

The Society's investments are valued at fair value. Fair value is the quoted mid-market value as at 31 December 2016.

The separate financial investment categories have been analysed in the following table.

	Solvency II £'000	Financial Statements £'000
Government bonds	10,927	8,240
Fixed interest securities	9,126	11,586
Directly held equities	5,826	6,324
Collectives	3,362	3,303
Total financial investments	29,241	29,453

The differences between Solvency II and the financial statements can by analysed as follows:

- The Government bonds figure includes accrued interest for Solvency II purposes, whereas this is shown as part of the 'other assets' figure in the financial statement asset categories. The financial statements also include only UK government bonds whereas for Solvency II purposes any European approved government bonds are also shown in this asset category.
- Fixed interest securities also include accrued interest for Solvency II purposes. As noted the difference between the financial statement value and the Solvency II value is due to the European approved government bonds being reclassified as government bonds for Solvency II purposes.
- One holding which is classed as a direct equity has been reclassified as a collective for Solvency II purposes. All REITs have been classed as investment property for Solvency II purposes.
- The difference between the total financial investments relate to the transfer of the REIT investments from equities to investment property for Solvency II purposes and the accrued interest that has been added to the government bonds and fixed interest securities.

The financial investments are managed by LGT Vestra. The fund aims to generate returns whilst ensuring the long-term liabilities of the Society are sufficiently covered by the asset mix and duration of the portfolio.

D1.4 Loans and Mortgages

Loans and mortgages are valued on the same basis for Solvency II purposes as they are in the financial statements. This is the total balance due less a provision for any bad debts.

D1.5 Cash and Cash Equivalents

Cash and cash equivalents are valued at carrying value on 31 December 2016. A reduction has been applied to the cash and cash equivalents under Solvency II for the gearing of REITs. It is assumed that the difference between market value and the underlying Solvency II value would be financed by a reduction in cash.

D1.6 Other Assets

All other assets are valued for Solvency II purposes on the same basis as the financial statements, at fair value or settlement value.

D1.7 Recognition and Valuation Basis

This is the first year the Society has reported under Solvency II and there has been no change to the recognition or valuation basis of assets for Solvency II purposes during the reporting period.

D2 Valuation of technical provisions

D2.1 Results

All of the Society's business is classified as one line of business. The total technical provisions are shown below:

£000	31 December 2016
best estimate	25,931
risk margin	1,965
technical provisions	**27,895**

D2.2 Method of valuation

The Society has adopted the standard formula methodology approach. The methodology for the calculation of technical provisions and capital requirements is outlined in the Delegated Act and associated guidelines. In broad terms, the gross technical provisions can be defined as the sum of the best estimate and risk margin. The total of best estimate and risk margin must correspond to the amount that an undertaking would expect to pay if they were to transfer their insurance obligations to another undertaking.

D2.2.1 Calculation of best estimate

The best estimate is the total of the discounted policy cash-flows. The policy cash-flows allowed for within the cash-flow projection are:

income	premiums
expenditure	expenses plus surrender, death, disability and maturity benefits (including future bonus declarations where applicable) and tax (if applicable)

The expected cash-flows are generated using product details, individual policy data and assumptions on future expenses and mortality, morbidity and surrender rates.

The surrender values are based on the surrender value factors in place at 31 December 2016.

The cash-flows should also allow for a 'cost of guarantee' to allow for part of the members' benefit accrued to the valuation date assumed to be backed by equity assets rather than bonds. However, the Society holds sufficient bonds and deposits to cover the accrued benefits, so the cost of guarantees is zero.

D2.2.2 Calculation of risk margin

The risk margin is a part of the technical provisions required to ensure that the value of technical provisions is equivalent to the amount that an insurance undertaking would expect to require in order to take over and meet the insurance obligations.

The risk margin is calculated as the cost of providing an amount necessary to support the insurance obligations up until their maturity or final claim date. Under the Delegated Act, the amount required is equal to the Solvency Capital Requirement ("SCR") for the insurance obligations. The cost of providing this amount is calculated as the cost of capital rate multiplied by the SCR at each time interval in the future up until the policy end date and discounted back to the valuation date. The cost of capital rate within the Delegated Act is 6%.

Sources of capital risk for the Society come from market risk, life underwriting risk, counterparty risk and operational risk. Each individual capital risk (except operational risk) is stressed by a factor given within the Delegated Act. An individual SCR for each capital risk is calculated and then all individual SCRs are correlated within their own risk modules to derive an overall SCR for that module. These overall module SCRs are then correlated further to calculate a gross base SCR ("BSCR").

The Society is allowed, under the Delegated Act, to change the future discretionary benefits in each capital risk stress scenario when calculating the risk margin. For example, under the market risk module, there is an equity risk of an instantaneous fall in market values of equities. In this scenario, the Society can consider whether the impact of the fall in equities would change the future discretionary benefits to be declared.

For the Society, the only possible discretionary benefits are future bonuses and surrender values. Any reduction in the discounted value of future discretionary benefits is used to offset the impact of the capital risk stress. This is the "loss absorbency of technical provisions".

D2.2.3 Unbundling

Unbundling refers to the requirements to separate, where possible, different lines of business that are included within one contract. The Society's death and disability policies include elements of health insurance (with profit participation) and life insurance with profit participation, but it is not possible to define obligations and premiums attributable to each part, so the two lines of business have not been separated and all business is assumed to be life insurance with profit participation.

D2.2.4 Contract Boundaries

Article 18 of the Delegated Act provides principles to follow when determining the contract boundary of a policy type i.e. the future point at which the calculation of future net cash-flows should cease. As the Society has fixed premium rates throughout the term of its policies, the contract boundary is the maturity date for all the Society's policies.

D2.3 Assumptions

The assumptions used are supposed to reflect a reasonable best estimate of the likely experience, with no prudence margins.

D2.3.1 Expenses

We have assumed an expense allowance of 18% of premiums. This is consistent with the Society's expected future expenses over the next ten years.

D2.3.2 Mortality and morbidity

We have projected the policies using mortality and morbidity assumptions equal to the actual mortality and morbidity, as a proportion of the relevant table, experienced during 2012-2016, rounded to the nearest 5%. The table below summarises the mortality and morbidity assumptions.

	mortality	morbidity
under 17	40% ELT15	
17 or over	65% AMC00/AFC00	35% of the Society's own table of disablement rates

D2.3.3 Future bonuses

We have assumed that future bonus rates will be set to ensure that they are sustainable with regard to the current risk-free rates. As is the current practice, we have assumed that the last few remaining pre-1984 policyholders will receive bonuses of twice those given to post-1984 policyholders.

D2.3.4 Surrenders

We assume that lapses occur at 6.5% pa, which is consistent with the Society's experience during the period 2012-16. The surrender value is calculated as the claim amount multiplied by the current surrender factor.

D2.3.5 Cost of guarantees

As there are sufficient deposits and bonds to cover the guaranteed benefits, no cost of guarantees needs to be calculated and hence no assumptions are required.

D2.4 Level of uncertainty

There are no material deficiencies in the data used for the calculation of the technical provisions.

By definition, the models used in the calculation of the technical provisions are a simplified version of real life but are designed to capture the key features of the cashflows being modelled. The Society is not aware of any material features that have been excluded from the calculations and the methodology employed is proportionate to the nature, scale and complexity of the risk accepted by the Society.

The cashflows projected in determining the technical provisions are best estimates. However, there is always uncertainty in projecting those cashflows, including uncertainty of timing, frequency of and severity of claim events, uncertainty in claim amounts, uncertainty in expenses and uncertainty in policyholder behaviour.

A robust assumption setting process is followed to ensure that uncertainties are well understood. Historical experience is used to guide the assumption setting, but past experience is no guarantee of future experience. Analysis of how the model results compare to past experience can be used as a guide and is part of the assumption setting process. The sensitivity of the results is also central to the assumption setting process. The technical provisions are most sensitive to discount rate, lapse and expense assumptions.

D2.5 Explanation of material differences between financial statements and Solvency II

The technical provisions shown in the Society's financial statements are equal to the Solvency II technical provisions, therefore there are no differences in the bases, methods and assumptions used.

D2.6 Transitional adjustments

The regulations allow insurers, in some circumstances, to use transitional adjustments to smooth the change between the Solvency I and Solvency II regimes. The Society has not used any of the following:

- the matching adjustment referred to in Article 77b of the Directive
- the volatility adjustment referred to in Article 77d of the Directive
- the transitional risk-free interest rate-term structure referred to Article 308c of the Directive
- the transitional deduction referred to in Article 308d of the Directive.

The Society has used the equity transitional measure referred to in Article 308b(12) of the Directive.

D2.7 Recoverables from reinsurance and Special Purpose Vehicles

The Society does not have any reinsurance or use any Special Purpose Vehicles.

D2.8 Material changes in assumptions and methods from previous reporting period

The material changes in assumptions between 31 December 2015 and 31 December 2016 were:

- significant reductions in the discount rates (which are set by the regulator)
- reductions in assumed future bonus rates to ensure consistency with the lower discount rates
- higher assumed expenses to be consistent with the Society's business plans

D3 Valuation of other liabilities

The table below details the valuation of other liabilities for Solvency II purposes and as per the financial statements, which follow UK GAAP.

£000	Solvency II	Financial Statements
claims outstanding	57	57
other creditors	205	205
total other liabilities	262	262

D3.1 Recognition and Valuation Basis

This is the first year the Society has reported under Solvency II and there has been no change to the recognition or valuation basis of other liabilities for Solvency II purposes during the reporting period.

D4 Other material information

No other material information is necessary to give a full picture of the Society's valuation for solvency purposes.

E Capital Management

E1 Own funds

The Society is a mutual organisation and so does not have any shareholders. The Society's own funds are essentially the surplus accumulated that has not yet been allocated to policies. It forms the working capital of the Society and is available to meet risk and capital requirements, as well as any uncertain additional liabilities that may arise in the future.

£000	31 December 2016	31 December 2015
total basic own funds	5,440	5,331

The small increase in own funds was due to the assets increasing by more than the liabilities. The most significant reason for the change in both liabilities and assets was market movements (associated with a reduction in discount rates). Further explanation of the movement in own funds is contained in the Society's Annual Report and Accounts.

All the own funds are eligible to cover the SCR and MCR.

E1.1 Objectives, policies and processes for managing own funds

The Society has a risk and capital management policy, which includes a minimum level of free assets (i.e. own funds less capital requirement) that the Society aims to maintain. This is set with the aim of ensuring that the Society can still meets its liabilities and capital requirements in a wide range of future circumstances. The policy also states potential actions to be taken if the free assets reach a specified "trigger point" which is higher than the minimum level, such as realignment of investment portfolios. The policy was updated during 2016 to ensure it remained suitable under Solvency II.

The Society's solvency position is monitored regularly:

- Liabilities are revalued at least quarterly, with revaluation more regularly if conditions suggest its free assets may be approaching the trigger point.
- Daily calculations are normally carried out using the most recently calculated liabilities and estimated assets, based on market movements.
- The solvency position is provided to the Management Committee each month.

The Society also carried out annual projections of its business, focussed on its business planning period of four years, but projecting for at least ten years, and including projections under a variety of scenarios. If there were significant changes to the Society's business, or to outside influences such as investment markets or a significant change in regulation, the Society would update its projections.

E1.2 Comparison of own funds under Solvency II and in financial statements

The own funds shown in the Society's financial statements are equal to the Solvency II own funds.

E1.3 Other issues

- None of the basic own funds are subject to the transitional arrangements referred to in Articles 308b(9) and 308b(10) of the Directive.
- There are no ancillary own funds.
- No deductions are made from own funds as there are no significant restrictions affecting the availability and transferability of own funds within the Society.

E2 SCR and MCR

E2.1 Overall method for calculating SCR

The SCR is capital that needs to be held in addition to the technical provisions (best estimate plus risk margin). There is no capital add on. The Society does not use any of the standard formula simplifications set out in the Delegated Act for the SCR calculation, nor any undertaking-specific parameters. The SCR is assessed based on the Society's risks as being sufficient to cover possible losses due to those risks. It considers four different risks: market, counterparty, life underwriting and operational.

The capital requirements under each risk module (apart from operational risk) are calculated and then correlated together to form the Basic Solvency Capital Requirement ("BSCR"). The capital requirements are calculated both before and after the loss absorbency of technical provisions so that an adjustment to the BSCR can be made to allow for the fact that capital requirements will change if future discretionary benefits can be changed. The capital requirement for operational risk is then added on as an additional requirement at the end of the calculation.

In summary the SCR formula is:

- BSCR + Adjustment for Loss Absorbency of Technical Provisions + Operational Risk

The resulting SCR by risk module is shown below. The SCR is still subject to supervisory assessment, but we have not had any queries from the PRA on previous submissions.

E2.2 Life underwriting risk

£000	before loss absorbency	after loss absorbency
mortality	89	0
longevity	0	0
morbidity	98	0
lapse	4,697	27
expense	411	0
CAT	42	42
total before correlation	**5,338**	**70**
total after correlation	**4,935**	**56**

E2.3 Market risk

£000	before loss absorbency	after loss absorbency
interest rate	277	0
equity	2,548	1,509
property	476	127
currency	1,119	556
spread	1,644	906
concentration	24	0
total before correlation	**6,088**	**3,098**
total after correlation	**4,868**	**2,566**

The Society does not use the duration-based equity risk sub-module option set out in Article 304 of the Directive.

E2.4 Counterparty risk

£000	before loss absorbency	after loss absorbency
counterparty	275	0

E2.5 BSCR

	£000
BSCR before loss absorbency	7,841
BSCR after loss absorbency	2,580
Y = BSCR before loss absorbency less BSCR after loss absorbency	5,260
Z = total value of technical provisions in relation to future discretionary benefits	11,985
loss absorbency of technical provisions = maximum(minimum(Y, Z), 0)	5,260

E2.6 Operational risk

	£000
premiums earned in prior year	4,361
premiums earned in this year	4,556
technical provisions (without risk margin)	25,931
OP (premiums)	182
OP (technical provisions)	117
SCR operational risk	**182**

E2.7 Overall SCR

£000	31 December 2016	31 December 2015
BSCR	7,841	6,515
less loss absorbency of technical provisions	5,260	6,473
plus SCR operational risk	182	174
overall SCR	**2,763**	**217**

The most significant reasons for the increase in BSCR are:

- an increase in the lapse risk, due to use of a higher lapse assumption (and therefore a proportionate stress having a greater effect); and
- an increase in the equity risk, due to the unwinding of the equity transitional measure.

The loss absorbency has reduced due to lower future discretionary benefits being available to offset the effect of the stresses. Therefore, overall there has been a significant increase in the SCR.

The ratio of eligible own funds to the SCR is 197%.

E2.8 Minimum Capital Requirement

The Minimum Capital Requirement ("MCR") is calculated as MCR_{linear} (see below), subject to a floor of 25% net SCR and ceiling of 45% of net SCR, but with an overall minimum of €3.7m, i.e.: maximum (€3.7m, minimum (45% net SCR, maximum (25% net SCR, MCR_{linear})))

For the Society, MCR_{linear} is defined as 3.7% of technical provisions for guaranteed benefits less 5.2% of technical provisions for discretionary benefits. The absolute floor of €3.7m converted into pounds using the official exchange rate at 31 December 2016 is £3,332k.

The calculation below shows that the €3.7m absolute floor bites, so the minimum capital requirement is £3,332k at 31 December 2016. Changes in the MCR from 31 December 2015 to 31 December 2016 are therefore due purely to changes in the exchange rate.

The ratio of eligible own funds to the MCR is 163%.

£000	31 December 2016	31 December 2015
Solvency Capital Requirement	2,763	216
technical provisions - guaranteed benefits	13,946	11,884
technical provisions - discretionary benefits	11,985	12,964
MCR_{linear}	(88)	(234)
SCR-related floor (25% SCR)	691	54
SCR-related ceiling (45% SCR)	1,243	97
absolute floor	3,332	2,657
Minimum Capital Requirement	3,332	2,657

E3 Non-compliance

The Society has had sufficient assets to cover the technical provisions and MCR (and therefore the SCR) at all times during 2016.

E4 Other material information

There is no other material information to disclose regarding the capital management of the Society.

Railway Enginemen's Assurance Society

Solvency and Financial Condition Report

Disclosures

31 December

2016

(Monetary amounts in GBP thousands)

General information

Undertaking name	Railway Enginemen's Assurance Society
Undertaking identification code	213800RM1N52XCQ96840
Type of code of undertaking	LEI
Type of undertaking	Life undertakings
Country of authorisation	GB
Language of reporting	en
Reporting reference date	31 December 2016
Currency used for reporting	GBP
Accounting standards	The undertaking is using local GAAP (other than IFRS)
Method of Calculation of the SCR	Standard formula
Matching adjustment	No use of matching adjustment
Volatility adjustment	No use of volatility adjustment
Transitional measure on the risk-free interest rate	No use of transitional measure on the risk-free interest rate
Transitional measure on technical provisions	No use of transitional measure on technical provisions

List of reported templates

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.23.01.01 - Own Funds
S.25.01.21 - Solvency Capital Requirement - for undertakings on Standard Formula
S.28.01.01 - Minimum Capital Requirement - Only life or only non-life insurance or reinsurance activity

S.02.01.02

Balance sheet

		Solvency II value
	Assets	C0010
R0030	Intangible assets	
R0040	Deferred tax assets	
R0050	Pension benefit surplus	
R0060	Property, plant & equipment held for own use	322
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	30,845
R0080	*Property (other than for own use)*	1,604
R0090	*Holdings in related undertakings, including participations*	0
R0100	*Equities*	5,826
R0110	*Equities - listed*	5,826
R0120	*Equities - unlisted*	0
R0130	*Bonds*	20,053
R0140	*Government Bonds*	10,927
R0150	*Corporate Bonds*	9,126
R0160	*Structured notes*	0
R0170	*Collateralised securities*	0
R0180	*Collective Investments Undertakings*	3,362
R0190	*Derivatives*	
R0200	*Deposits other than cash equivalents*	0
R0210	*Other investments*	0
R0220	Assets held for index-linked and unit-linked contracts	
R0230	Loans and mortgages	1,273
R0240	*Loans on policies*	995
R0250	*Loans and mortgages to individuals*	278
R0260	*Other loans and mortgages*	
R0270	Reinsurance recoverables from:	0
R0280	*Non-life and health similar to non-life*	0
R0290	*Non-life excluding health*	
R0300	*Health similar to non-life*	
R0310	*Life and health similar to life, excluding index-linked and unit-linked*	0
R0320	*Health similar to life*	0
R0330	*Life excluding health and index-linked and unit-linked*	0
R0340	*Life index-linked and unit-linked*	0
R0350	Deposits to cedants	0
R0360	Insurance and intermediaries receivables	404
R0370	Reinsurance receivables	
R0380	Receivables (trade, not insurance)	
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	522
R0420	Any other assets, not elsewhere shown	231
R0500	Total assets	33,597

S.02.01.02

Balance sheet

		Solvency II value
	Liabilities	C0010
R0510	Technical provisions - non-life	0
R0520	*Technical provisions - non-life (excluding health)*	0
R0530	*TP calculated as a whole*	
R0540	*Best Estimate*	
R0550	*Risk margin*	
R0560	*Technical provisions - health (similar to non-life)*	0
R0570	*TP calculated as a whole*	
R0580	*Best Estimate*	
R0590	*Risk margin*	
R0600	Technical provisions - life (excluding index-linked and unit-linked)	27,895
R0610	*Technical provisions - health (similar to life)*	0
R0620	*TP calculated as a whole*	0
R0630	*Best Estimate*	0
R0640	*Risk margin*	0
R0650	*Technical provisions - life (excluding health and index-linked and unit-linked)*	27,895
R0660	*TP calculated as a whole*	0
R0670	*Best Estimate*	25,931
R0680	*Risk margin*	1,965
R0690	Technical provisions - index-linked and unit-linked	0
R0700	*TP calculated as a whole*	0
R0710	*Best Estimate*	0
R0720	*Risk margin*	0
R0740	Contingent liabilities	
R0750	Provisions other than technical provisions	
R0760	Pension benefit obligations	
R0770	Deposits from reinsurers	
R0780	Deferred tax liabilities	
R0790	Derivatives	
R0800	Debts owed to credit institutions	
R0810	Financial liabilities other than debts owed to credit institutions	149
R0820	Insurance & intermediaries payables	57
R0830	Reinsurance payables	
R0840	Payables (trade, not insurance)	
R0850	Subordinated liabilities	0
R0860	*Subordinated liabilities not in BOF*	
R0870	*Subordinated liabilities in BOF*	0
R0880	Any other liabilities, not elsewhere shown	56
R0900	Total liabilities	28,157
R1000	Excess of assets over liabilities	5,440

S.05.01.02

Premiums, claims and expenses by line of business

Life

		Line of Business for: life insurance obligations						Life reinsurance obligations		Total
		Health insurance	Insurance with profit participation	Index-linked and unit-linked insurance	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	Health reinsurance	Life reinsurance	
		C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0300
	Premiums written									
R1410	Gross		4,556							4,556
R1420	Reinsurers' share									0
R1500	Net		4,556							4,556
	Premiums earned									
R1510	Gross		4,556							4,556
R1520	Reinsurers' share									0
R1600	Net		4,556							4,556
	Claims incurred									
R1610	Gross		4,048							4,048
R1620	Reinsurers' share									0
R1700	Net		4,048							4,048
	Changes in other technical provisions									
R1710	Gross		1,889							1,889
R1720	Reinsurers' share									0
R1800	Net		1,889							1,889
R1900	Expenses incurred		1,163							1,163
R2500	Other expenses									
R2600	Total expenses									1,163

S.05.02.01

Premiums, claims and expenses by country

Life

		C0150	C0160	C0170	C0180	C0190	C0200	C0210
		Home Country	Top 5 countries (by amount of gross premiums written) - life obligations			Top 5 countries (by amount of gross premiums written) - life obligations		Total Top 5 and home country
R1400								
		C0220	C0230	C0240	C0250	C0260	C0270	C0280
	Premiums written							
R1410	Gross	4,556						4,556
R1420	Reinsurers' share							0
R1500	Net	4,556	0	0	0	0	0	4,556
	Premiums earned							
R1510	Gross	4,556						4,556
R1520	Reinsurers' share							0
R1600	Net	4,556	0	0	0	0	0	4,556
	Claims incurred							
R1610	Gross	4,048						4,048
R1620	Reinsurers' share							0
R1700	Net	4,048	0	0	0	0	0	4,048
	Changes in other technical provisions							
R1710	Gross	1,889						1,889
R1720	Reinsurers' share							0
R1800	Net	1,889	0	0	0	0	0	1,889
R1900	Expenses incurred	1,163						1,163
R2500	Other expenses							
R2600	Total expenses							1,163

S.12.01.02

Life and Health SLT Technical Provisions

		Insurance with profit participation	Index-linked and unit-linked insurance			Other life insurance			Annuities stemming from non-life insurance contracts and relating to insurance obligation other than health insurance obligations	Accepted reinsurance	Total (Life other than health insurance, including Unit-Linked)	Health insurance (direct business)			Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Health reinsurance (reinsurance accepted)	Total (Health similar to life insurance)
				Contracts without options and guarantees	Contracts with options or guarantees		Contracts without options and guarantees	Contracts with options or guarantees					Contracts without options and guarantees	Contracts with options or guarantees			
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0150	C0160	C0170	C0180	C0190	C0200	C0210
R0010	Technical provisions calculated as a whole										0						
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						
	Technical provisions calculated as a sum of BE and RM																
	Best estimate																
R0030	Gross Best Estimate	25,931									25,931						
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default										0						
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re	25,931									25,931						
R0100	Risk margin	1,965									1,965						
	Amount of the transitional on Technical Provisions																
R0110	Technical Provisions calculated as a whole										0						
R0120	Best estimate										0						
R0130	Risk margin										0						
R0200	Technical provisions - total	27,895									27,895						

S.23.01.01

Own Funds

	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
R0010	Ordinary share capital (gross of own shares)	0	0		0	
R0030	Share premium account related to ordinary share capital	0	0		0	
R0040	Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings	0	0		0	
R0050	Subordinated mutual member accounts	0		0	0	0
R0070	Surplus funds	0	0			
R0090	Preference shares	0		0	0	0
R0110	Share premium account related to preference shares	0		0	0	0
R0130	Reconciliation reserve	5,440	5,440			
R0140	Subordinated liabilities	0		0	0	0
R0160	An amount equal to the value of net deferred tax assets	0				0
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	0	0	0	0	0
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				
R0230	Deductions for participations in financial and credit institutions	0				
R0290	Total basic own funds after deductions	5,440	5,440	0	0	0
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	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				
R0320	Unpaid and uncalled preference shares callable on demand	0				
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	0				
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	0				
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	0				
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0				
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0				
R0390	Other ancillary own funds	0				
R0400	Total ancillary own funds	0			0	0
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	5,440	5,440	0	0	0
R0510	Total available own funds to meet the MCR	5,440	5,440	0	0	
R0540	Total eligible own funds to meet the SCR	5,440	5,440	0	0	0
R0550	Total eligible own funds to meet the MCR	5,440	5,440	0	0	
R0580	SCR	2,763				
R0600	MCR	3,332				
R0620	Ratio of Eligible own funds to SCR	196.90%				
R0640	Ratio of Eligible own funds to MCR	163.26%				

	Reconcilliation reserve	C0060
R0700	Excess of assets over liabilities	5,440
R0710	Own shares (held directly and indirectly)	0
R0720	Foreseeable dividends, distributions and charges	
R0730	Other basic own fund items	0
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	0
R0760	Reconciliation reserve	5,440
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) - Life business	7,542
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	
R0790	Total Expected profits included in future premiums (EPIFP)	7,542

S.25.01.21

Solvency Capital Requirement - for undertakings on Standard Formula

		Gross solvency capital requirement	USP	Simplifications
		C0110	C0080	C0090
R0010	Market risk	4,868		
R0020	Counterparty default risk	275		
R0030	Life underwriting risk	4,935		
R0040	Health underwriting risk	0		
R0050	Non-life underwriting risk	0		
R0060	Diversification	-2,236		
R0070	Intangible asset risk	0		
R0100	Basic Solvency Capital Requirement	7,841		

	Calculation of Solvency Capital Requirement	C0100
R0130	Operational risk	182
R0140	Loss-absorbing capacity of technical provisions	-5,260
R0150	Loss-absorbing capacity of deferred taxes	0
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	0
R0200	Solvency Capital Requirement excluding capital add-on	2,763
R0210	Capital add-ons already set	0
R0220	Solvency capital requirement	2,763
	Other information on SCR	
R0400	Capital requirement for duration-based equity risk sub-module	0
R0410	Total amount of Notional Solvency Capital Requirements for remaining part	0
R0420	Total amount of Notional Solvency Capital Requirements for ring fenced funds	0
R0430	Total amount of Notional Solvency Capital Requirements for matching adjustment portfolios	0
R0440	Diversification effects due to RFF nSCR aggregation for article 304	0

S.28.01.01

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

Linear formula component for non-life insurance and reinsurance obligations

		C0010
R0010	MCR_{NL} Result	0

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0020	C0030
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_L Result	-88

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
		C0050	C0060
R0210	Obligations with profit participation - guaranteed benefits	13,946	
R0220	Obligations with profit participation - future discretionary benefits	11,985	
R0230	Index-linked and unit-linked insurance obligations		
R0240	Other life (re)insurance and health (re)insurance obligations		
R0250	Total capital at risk for all life (re)insurance obligations		27,927

Overall MCR calculation

		C0070
R0300	Linear MCR	-88
R0310	SCR	2,763
R0320	MCR cap	1,243
R0330	MCR floor	691
R0340	Combined MCR	691
R0350	Absolute floor of the MCR	3,332
R0400	Minimum Capital Requirement	3,332

REPORT OF THE EXTERNAL INDEPENDENT AUDITOR TO THE MANAGEMENT COMMITTEE OF RAILWAY ENGINEMEN'S ASSURANCE SOCIETY LIMITED ('THE SOCIETY) PURSUANT TO RULE 4.1 (2) OF THE EXTERNAL AUDIT CHAPTER OF THE PRA RULEBOOK APPLICABLE TO SOLVENCY II FIRMS

REPORT ON THE AUDIT OF THE RELEVANT ELEMENTS OF THE SOLVENCY AND FINANCIAL CONDITION REPORT

Opinion

Except as stated below, we have audited the following documents prepared by the Society as at 31 December 2016:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Society as at 31 December 2016, (**'the Narrative Disclosures subject to audit'**); and
- Company templates S.02.01.02, S.12.01.02, S.23.01.01, S.25.01.21 and S.28.01.01 ('**the Templates subject to audit**').

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

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

- The 'Business and performance', 'System of governance' and 'Risk profile' elements of the Solvency and Financial Condition Report;
- Company templates S.05.01.02, S.05.02.01;
- The written acknowledgement by management of their responsibilities, including for the preparation of the Solvency and Financial Condition Report (**'the Responsibility Statement'**).

In our opinion, the information subject to audit in the relevant elements of the Solvency and Financial Condition Report of the Society 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.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & I)), International Standard on Auditing (UK) 800 and International Standard on Auditing (UK) 805. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report* section of our report. We are independent of the Society in accordance with the ethical requirements that are relevant to our audit of the Solvency and Financial Condition Report in the UK, including the APB Ethical Standard, and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of Matter – Basis of Accounting

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

Other Information

The Management Committee is responsible for the Other Information.

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

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

Responsibilities of the Management Committee for the Solvency and Financial Condition Report

The Management Committee is responsible for the preparation of the Solvency and Financial Condition Report in accordance with financial reporting provisions of the PRA rules and Solvency II regulations.

The Management Committee is also responsible for such internal control as it determines is necessary to enable the preparation of a Solvency and Financial Condition Report that is free from misstatement, whether due to fraud or error.

Auditor's Responsibilities for the Audit of the Relevant Elements of the Solvency and Financial Condition Report

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

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

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at http://www.frc.org.uk/auditscopeukprivate

This report is made solely to the Management Committee to comply with their obligations under Rule 2.1 of the External Audit Chapter of the PRA Rulebook for Solvency II firms. Our audit work has been undertaken so that we might state to the Management Committee those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Management Committee, the Society and the Society's members, for our audit work, for this report, or for the opinions we have formed.

Report on Other Legal and Regulatory Requirements

In accordance with Rule 4.1 (3) of the External Audit Chapter of the PRA Rulebook for Solvency II firms we are required to consider whether the Other Information is materially inconsistent with our knowledge obtained in the audit of the Society'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.

RSM UK Audit LLP

CHARLES FRAY (Senior Statutory Auditor)

For and on behalf of RSM UK Audit LLP, Statutory Auditor
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Date 19 May 2017

Appendix – relevant elements of the Solvency and Financial Condition Report that are not subject to audit

The relevant elements of the Solvency and Financial Condition Report that are not subject to audit comprise:

- The following elements of template S.12.01.02
    - Rows R0110 to R0130 – Amount of transitional measure on technical provisions
- Elements of the Narrative Disclosures subject to audit identified as 'unaudited'.