Zurich Assurance Ltd

Solvency and Financial Condition Report 2016

Zurich Assurance Ltd

Contents

All amounts in the Solvency and Financial Condition Report, unless otherwise stated, are shown in Great British Pounds Sterling (GBP) rounded to the nearest thousand. The rounded amounts may not add to the rounded total in all cases. All ratios and variances are calculated using the underlying amounts rather than the rounded amounts.

Overview

Business profile

Zurich Assurance Ltd is a provider of long term insurance in the UK and is part of the Zurich Insurance Group

Zurich Assurance Ltd (ZAL) is a limited company domiciled and incorporated in the United Kingdom. ZAL also has overseas branches in Hong Kong, Malta and the Isle of Man, which are no longer open to new business.

GBP 2,348 m
Gross Claims (2016)

GBP 50,170 m
Total Assets under Management (as of 31 December 2016)

System of governance

Zurich Assurance Ltd operates a mature and well established system of governance

The Board derives its collective authority by direct delegation from its shareholder, and is supported by its Risk, Audit and Investment Committees.

ZAL documents its system of governance within its governance map, which sets out the key functions in the firm and the relevant individuals in control of these functions, along with their lines of accountability and responsibility. Aside from changes to Directors there have been no material changes to ZAL's system of governance during the reporting period.

Risk profile

Zurich Assurance Ltd holds appropriate capital for the risks its business faces and has robust controls and mitigants in place

ZAL's business model results in it being subject to a range of risks associated with the activity of issuing insurance and investment contracts and the use of financial instruments. These include risks for which ZAL holds capital and risks for which other mitigation is applied.

Regulatory capital, assessed on the Solvency II standard formula basis, is held to cover the risks associated with ZAL's balance sheet position, specifically for underwriting, market, credit and operational risks. Capital is also held for staff pension scheme risk not covered by the standard formula.

Financial condition

With a SCR ratio of 173%, Zurich Assurance Ltd is strongly capitalised

As of 31 December 2016, ZAL had a SCR ratio of 173%, compared to a requirement of 100% and in excess of ZAL's target ratio.

173%
Solvency II SCR ratio (as of 31 December 2016)

GBP 1,994 m
Own funds under Solvency II (as of 31 December 2016)

Introduction

1 Executive summary

Zurich Assurance Ltd (ZAL or 'the Company') is a limited company domiciled and incorporated in the United Kingdom. The principal activity of the Company is the provision of long term insurance business carried out in the United Kingdom. ZAL has overseas branches in Hong Kong, Malta and the Isle of Man. The branches are no longer open to new business.

In 2016 there was a significant change in the regulatory regime applying to ZAL and other insurers across Europe. Known as 'Solvency II', this new regime is designed to provide high levels of policyholder protection through a combination of strong risk management disciplines and financial strength requirements together with close supervision from regulators. For ZAL this was an evolution from the previous standards which had been in force in the UK and which ZAL applied as a part of the Zurich Insurance Group.

This report satisfies the regulatory disclosure requirements under the Solvency II directive, including the delegated regulations of the European Parliament. The elements of the disclosure relate to the Company's business performance, governance, risk profile, solvency and capital management. ZAL continuously complied in all material respects with the applicable requirements of Solvency II regulations from 1 January 2016.

ZAL presents its results as a standalone entity and the report should be read in that context. ZAL is part of the Zurich Insurance Group ('the Group'). In addition to the capital and liquidity held by ZAL, the Group holds substantial capital and liquidity centrally. This centrally held capital and liquidity can be deployed into subsidiaries if needed, and thus provides further support for ZAL to absorb potential losses which could arise from the occurrence of extreme adverse events. The Group itself is regulated by the Swiss Financial Markets Supervisory Authority. As of 1 January 2017, the Group had a solvency ratio of 227% as measured by the Swiss Solvency Test, which has equivalence with the Solvency II regulatory regime applicable to ZAL. The Group manages its capital at an AA level according to its internal economic capital model. The financial strength of Zurich Insurance Company Ltd, which is the main insurance carrier of the Group, is rated AA- by Standard and Poor's. More information on the Group's risk and capital management is provided in its annual report, which is available at www.zurich.com.

At 31 December 2016 ZAL had in excess of £50.1bn total assets under management and 3.4m policyholders and scheme members. ZAL's UK GAAP profit for the year before taxation was £4m and total annual premium equivalent was £490m. In 2016 gross claims were £2.3bn, and ZAL paid over 90% of critical illness claims, over 98% of death claims and 85% of income protection claims. ZAL is committed to paying valid claims as they make a real difference to the lives of its customers at a time when they are most vulnerable.

ZAL operated effective and well-embedded corporate governance and risk management frameworks throughout 2016 which met Solvency II requirements. There have been no significant changes to the governance and risk frameworks during 2016. ZAL manages its risks in accordance with its risk appetite which is set by the ZAL Board and which supports risk-based decision making.

ZAL ensures it has excess money (known as own funds) so that it can withstand any uncertainties in future experience. Under Solvency II the Solvency Capital Requirement (SCR) is the capital required to ensure that ZAL will be able to meet its obligations over the next 12 months with a probability of at least 99.5%.

At 31 December 2016 ZAL had own funds of £1,994m and a Solvency Capital Requirement of £1,155m meaning that ZAL's solvency position at 31 December 2016 was strong with a solvency ratio of 173%.

The Zurich Insurance Group pools risk and capital as much as possible at group level realising diversification benefits for the Group. ZAL manages its capital in line with the Group's capital management policy and returns value to its shareholder whilst maintaining appropriate capital buffers to meet its Solvency II capital requirements at all times.

2 Statement of directors responsibility

The ZAL Board of Directors acknowledges its responsibility for preparing the Solvency and Financial Condition Report (SFCR) in all material respects in accordance with the rules issued by the Prudential Regulation Authority (PRA) and the Solvency II regulations.

The ZAL Board is satisfied:

a) Throughout the 2016 financial year, ZAL complied in all material respects with the applicable requirements of the PRA Rules and the Solvency II regulations; and

b) It is reasonable to believe ZAL has continued to comply subsequently and that it will continue to comply in future.

On behalf of the ZAL Board

Anne Torry

Chief Executive Officer

12 May 2017

Introduction *continued*

3 Independent auditors report

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

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

Opinion
We have audited the following documents prepared by the Company as at 31 December 2016:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Company 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 ' Executive Summary' 'Business and performance', 'System of governance' and 'Risk profile' elements of the Solvency and Financial Condition Report;
- Company templates S.05.01.02, S.05.02.01;
- The written acknowledgment 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 Company 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 supplemented by relevant supervisory 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, and applicable law. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report* section of our report.

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

Responsibilities of Directors for the Solvency and Financial Condition Report
The Directors are responsible for the preparation of the Solvency and Financial Condition Report in accordance with the financial reporting provisions of the PRA rules and Solvency II regulations which have been supplemented by the determination of a capital add-on made by the PRA under the PRA Rules and Solvency II regulations on which it is based.

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

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

It is our responsibility to form an independent opinion, in accordance with applicable law, ISAs (UK & I) and ISAs (UK) 800 and 805 as to whether the information subject to audit in the relevant elements of the Solvency and Financial Condition Report is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based. ISAs (UK & I) require us to comply with the Auditing Practices Board's Ethical Standard for Auditors.

An audit involves obtaining evidence about the amounts and disclosures in the relevant elements of the Solvency and Financial Condition Report sufficient to give reasonable assurance that the relevant elements of the Solvency and Financial Condition Report are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the relevant elements of the Solvency and Financial Condition Report. In addition, we read all the financial and non-financial information in the Solvency and Financial Condition Report to identify material inconsistencies with the audited relevant elements of the Solvency and Financial Condition Report. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

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

Report on Other Legal and Regulatory Requirements

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

PricewaterhouseCoopers LLP

Bristol

12th May 2017

- The maintenance and integrity of the information in respect of Zurich Assurance Ltd displayed on the Zurich Insurance Company Ltd website is the responsibility of the directors of Zurich Assurance Ltd; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Solvency and Financial Condition Report since it was initially presented on the website.
- Legislation in the United Kingdom governing the preparation and dissemination of Solvency and Financial Condition Reports may differ from legislation in other jurisdictions.

A. Business and performance

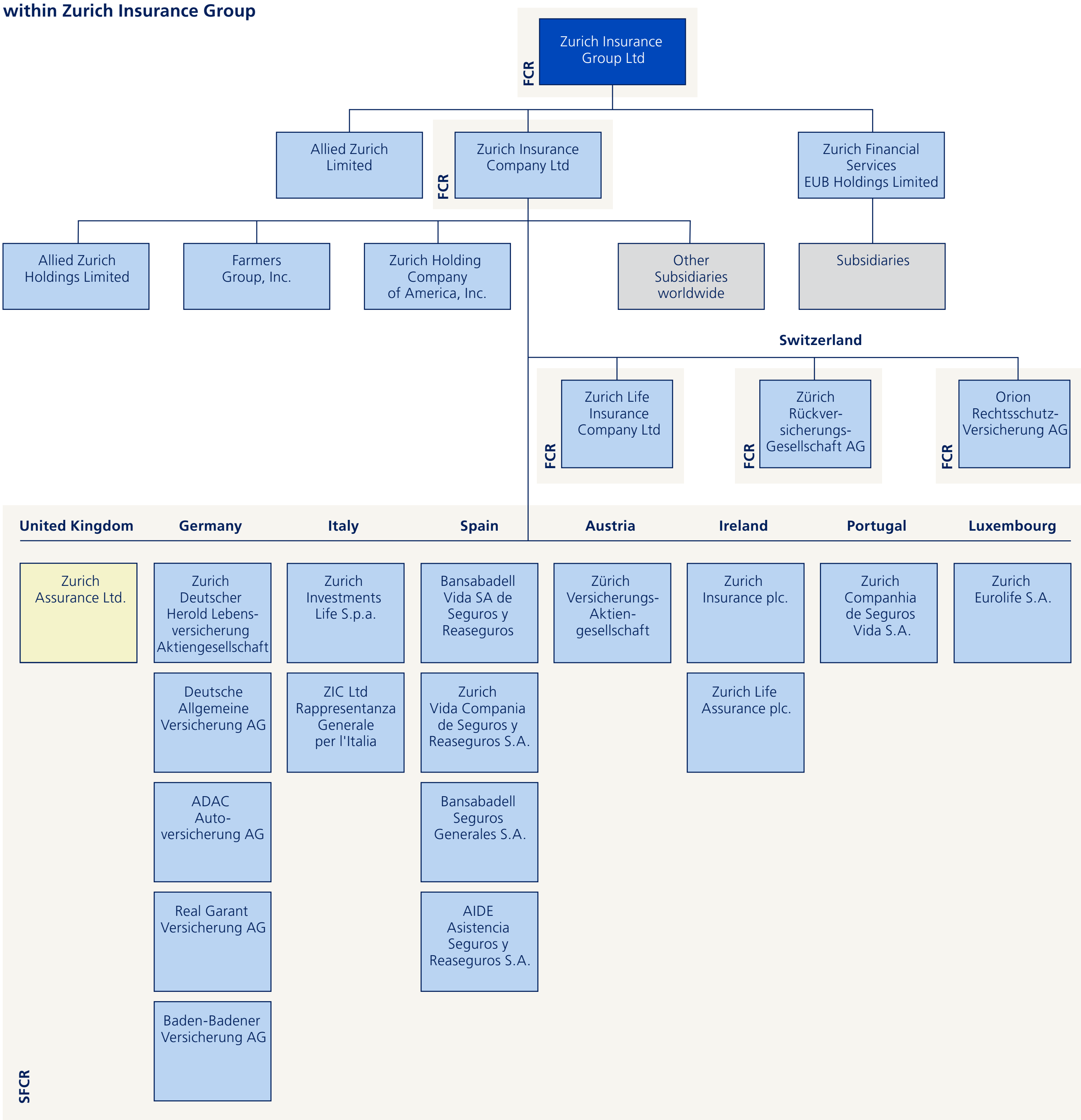
A.1 Business profile

Name, Location and legal form of the undertaking or the natural persons that are direct and indirect holders of qualifying holdings in the undertaking, with a description of all subsidiaries.	ZAL is a limited company domiciled and incorporated in the UK. The registered office is The Grange, Bishops Cleeve, Cheltenham, Gloucestershire, GL52 8XX. The principal activity of the Company is the provision of long term insurance business carried out in the United Kingdom and overseas. This includes its primary branch situated in Hong Kong, and two smaller branches in Malta and the Isle of Man. These overseas branches are no longer open to new business. ZAL is registered in England and Wales under company number 02456671 as a private company limited by shares.
Name and contact details of the supervisory authority responsible for financial supervision and, where applicable, name and contact details of the group supervisor	ZAL is authorised by the Prudential Regulation Authority (PRA) and regulated by the PRA and the Financial Conduct Authority (FCA). The PRA can be contacted at Threadneedle Street, London EC2R 8AH. The FCA can be contacted at 25 The North Colonnade, London E14 5HS. The Zurich Insurance Group is subject to insurance group supervision by the Swiss Financial Market Supervisory Authority (FINMA). FINMA can be contacted at Laupenstrasse 27, 3003 Bern.
Name and contact details of the external auditor of the undertaking	PricewaterhouseCoopers LLP 2 Glass Wharf, Bristol, BS2 0FR.
List of material related undertakings including the name, legal form, country, proportion of ownership interest held and, if different, proportion of voting rights held	A list of material related undertakings can be found in Appendix 1.
Description of the holders of qualifying holdings in the undertaking;	ZAL is a member of the Zurich Insurance Group. Zurich Insurance Group is a leading multi-line insurer that serves its customers in global and local markets. The Group is headquartered in Zurich, Switzerland. Zurich Insurance Group ('the Group') consists of Zurich Insurance Group Ltd (ZIG) holding entity and its subsidiaries. Zurich Insurance Company Ltd (ZIC) is the principal operating insurance company of ZIG. ZIC and its subsidiaries are collectively referred to as 'Zurich Insurance Company Group' or 'ZIC Group'. The main subsidiaries of ZIC include Allied Zurich Holdings Limited, Farmers Group, Inc, Zurich Life Insurance Company Ltd and Zurich Holding Company of America, Inc. The Company's immediate parent company is Eagle Star Holdings Limited.
Proportion of ownership interest held and, if different, the proportion of voting rights held.	ZIG has a 100% shareholding and voting power in ZIC. ZIC has a 100% shareholding and voting power in Allied Zurich Holdings Limited. Allied Zurich Holdings Limited has a 100% shareholding and voting power in Zurich Financial Services (UKISA) Limited. Zurich Financial Services (UKISA) Limited has a 100% shareholding and voting power in Eagle Star Holdings Limited. Eagle Star Holdings Limited has a 100% shareholding and voting power in ZAL.
Where the undertaking belongs to a group, details of the undertaking's position within the legal structure of the group	ZAL is a fully-owned subsidiary of ZIC, which is part of the Zurich Insurance Group. See description of ownership above. The Company operates in the UK business unit as part of the Group, and was part of the UK Life business unit (UK Life) during 2016.
Undertaking's material lines of business – **Health insurance**	Insurance contracts providing benefits in the event of illness, accident or disability.

Undertaking's material lines of business – **Insurance with-profit participation**	Contracts which are eligible to participate in discretionary distributions based on profits arising in part of the business. ZAL has two ring-fenced with-profits funds, the 90:10 With-Profits Fund and the 100:0 With-Profits Fund, where policyholders participate in the profits.
Undertaking's material lines of business – **Index-linked and unit-linked insurance**	Contracts where the benefits are wholly or partly determined by reference to a unit or index value. This excludes any linked contracts already classified under health.
Undertaking's material lines of business – **Other life insurance**	Any other directly written insurance contract not classified as health, with-profit or linked insurance.
Undertaking's material lines of business – **Non material Lines of Business (LoB)**	These represent the accepted reinsurance treaties. These lines of business are immaterial.
Undertaking's material geographical areas where it carries out business – **United Kingdom**	This is the primary geographical area. For presentation purposes this also includes the non branch business sold in the rest of Europe, which is not material.
Undertaking's material geographical areas where it carries out business – **Rest of Europe**	The business sold in Europe includes Jersey, Guernsey, Isle of Man and Malta. The Malta business and some of the Isle of Man business has been written through branches which are now closed to new business.
Undertaking's material geographical areas where it carries out business – **Asia**	The business carried out in Asia is through the Hong Kong branch, which is closed to new business.
Business planning period	For business planning purposes ZAL operates a three year planning period.

A. Business and performance *continued*

Chart 1: Public reporting on solvency and financial condition within Zurich Insurance Group



SFCR: Solvency and Financial Condition Report (Solvency II; from 2016) **FCR:** Financial Condition Report (Swiss regulation; from 2017)

Subsidiary/branch Group of subsidiaries/branches Current disclosure

Note: The purpose of the chart above is to provide a simplified overview of the Group's major subsidiaries and branches (as reported at December 31, 2016), with special focus on the public reporting of their solvency and financial condition. Please note that this is a simplified representation showing entities that must publish such a report and therefore it may not comprehensively reflect the detailed legal ownership structure of the entities included in the overview. The ordering of the legal entities under each country is not indicative of ownership; these are independent legal entities.

A.2 Underwriting performance

The Company prepares its statutory financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP), including Financial Reporting Standard (FRS) 101. Consequently, the information included in this section is presented on a UK GAAP basis.

The UK GAAP profit for the year before taxation was £4m. This includes a loss of £81m on derivative contracts held to mitigate equity risk on unit-linked business, as part of ZAL's capital management objectives, see section C.2 'Market risk'. From a solvency perspective the derivative loss is offset by higher future profits from policies, whereas in the profit before tax under UKGAAP there is no recognition of the higher future profits.

The significant lines of business contributing to the profit for the year were unit-linked insurance, health insurance and other life insurance. There was some with-profits business where the contribution to the result was the shareholder's share of any bonuses paid.

The table below shows the Company's premiums, claims and expenses split by Solvency II lines of business for the period ended 31 December 2016:

Premiums, Claims and Expenses by Line of Business

In £'000	Health insurance	Insurance with-profit participation	Index-linked and unit-linked insurance	Other life insurance	Non material LoBs	TOTAL
Gross Premiums	196,223	16,411	208,928	448,686	2,609	**872,857**
Reinsurers' share of premiums	81,109)	(444)	(40,415)	(356,902)	-	**(478,870)**
Gross Claims	(100,172)	(246,547)	(1,635,834)	(364,316)	(1,583)	**(2,348,452)**
Reinsurers' share of claims	34,477	325	43,421	310,249	-	**388,472**
Expenses	(49,200)	(10,378)	(289,835)	(111,338)	(4,065)	**(464,816)**

A large proportion of gross claims paid were due to surrenders on products which are closed to new business. There is a corresponding offset to this through the movements in technical provisions. Higher surrender volumes have been seen since the introduction of the Pension Freedom changes in 2015, which gave more flexibility to policyholders.

The figures above exclude unit-linked investment contracts which are accounted for using deposit accounting; income arising from these contracts is within 'Other technical income'.

The Company's primary market is the United Kingdom. The table below shows the Company's premiums, claims and expenses split by material geographical area:

Premiums, Claims and Expenses by Geographical Area

In £'000	United Kingdom	Asia	Other Europe	TOTAL
Gross Premiums	842,026	30,157	674	**872,857**
Reinsurers' share of premiums	(476,942)	(1,928)	-	**(478,870)**
Gross Claims	(2,300,534)	(38,687)	(9,231)	**(2,348,452)**
Reinsurers' share of claims	385,647	885	1,940	**388,472**
Expenses	(458,033)	(6,436)	(347)	**(464,816)**

A. Business and performance *continued*

The reconciliation from the Solvency II information reported in QRT S.05.01 in Appendix 2 to UK GAAP profit before taxation is as follows:

SII to UK GAAP reconciliation

In £'000	TOTAL
Gross Premiums (as per S.05)	872,857
Reinsurers' share of premiums (as per S.05)	(478,870)
Gross Claims (as per S.05)	(2,348,452)
Reinsurers' share of claims (as per S.05)	388,472
Expenses (as per S.05)	(464,816)
Changes in Other Technical Provisions (as per S.05)	(4,506,111)
Investment Performance	6,589,324
Other Technical Income	129,759
Tax change attributable to Long Term Business	(180,565)
Non-technical Income	4,637
Funds for Future Appropriation (FFA)	(2,115)
Other Activities	215
UK GAAP Profit before Taxation	4,335

The UK GAAP figures above use the Solvency II presentation. For certain headings the reported figures above may differ from the presentation in the financial statements.

The Company had 3.4 million policy holders or scheme members at 31 December 2016.

Gross premiums written during 2016 comprised regular premiums of £766m and single premiums of £107m. These figures exclude unit-linked investment contracts which are accounted for using deposit accounting; income arising from these contracts is shown within 'Other Technical Income'.

Total annual premium equivalent (APE) for the year was £490m. This remains a strong result in a challenging business environment, and reflects the strength of the Company's diversified distribution strategy.

The Company is committed to paying valid claims as they make a real difference to the lives of the Company's customers at a time when they are most vulnerable. During 2016 the Company's retail protection business paid out 90% of critical illness claims, over 98% of death claims and 85% of income protection claims. In the minority of claims not paid, reasons include non-disclosure of medical information on applications and instances of income protection customers having returned to work before the policy's payment period started.

Technical provisions increased in the year, mainly driven by a rise in the technical provision for unit-linked insurance. This was offset by an increase in investment performance on unit-linked assets over the year, primarily due to increases in market valuations in both equity and debt securities.

The FFA represents the amounts in the participating ring-fenced funds for which the allocation to participating policyholders and shareholders has not been determined at the balance sheet date.

Expenses in the year included acquisition costs and overhead expenses.

A.3 Investment performance

Net investment income represents income earned in the year, which is reported on an accruals basis and includes amortisation of premium (discount) on fixed interest securities. The investment result for the year was:

Investment Performance

In £'000	Net Investment Income	Net capital gains (losses)	Investment result
Cash and cash equivalents	898	(24)	874
Equity securities	9,442	34,424	43,866
Debt securities	84,952	212,817	297,769
Real estate held for investment	268	6,553	6,821
Mortgage loans	421	-	421
Other loans	2,395	-	2,395
Collective Investments Undertakings	439	1,628	2,067
Derivatives	-	(90,219)	(90,219)
Assets held for unit-linked contracts	825,074	5,395,882	6,220,956
Other investments	(505)	104,879	104,374
Investment result, gross	**923,384**	**5,665,940**	**6,589,324**
Investment expenses			(74,037)
Investment result, net			**6,515,287**

During 2016 there were strong capital gains in both equity and debt securities due to increases in market valuations. Real estate includes a large market value increase in one asset, revalued to reflect recent evidence of sales of similar assets in the vicinity.

The loss on derivatives of £90m included £81m on derivative contracts held to mitigate equity risk on unit-linked business, as part of ZAL's capital management objectives, see section A.2 'Underwriting performance' and C.2 'Market risk'. The remaining £9m loss on derivatives arose in the with-profits funds. The cost was met by the asset shares and estate and did not contribute to the underwriting result.

Included within the loss on 'Cash and cash equivalents' is £0.025m, which relates to a net foreign exchange loss on foreign cash and cash equivalents balances.

For unit-linked contracts, the net capital gains were due to strong valuation gains in equity and debt securities held.

Securitisation or repackaged loans

ZAL had exposure to securitisations and repackaged loan holdings of £165m at 31 December 2016. The net investment income is included in the 'debt securities' and 'assets held for unit-linked contracts' figures above. The risks associated with these holdings is covered in section C 'Risk profile'.

A. Business and performance *continued*

A.4 Performance of other activities

ZAL reported net income from Other income and expenses for the year 2016 of £4.6m, which consisted of the following:

Other income and expenses

In £'000	Income	Expenses
Investment result in non-technical account	4,500	(109)
Other income and expenses in non-technical account	1,038	(792)
Taxation	-	(49)
Total of other income/expenses	**5,538**	**(950)**

The 'Investment result in non-technical account' represents dividend income from subsidiary undertakings.

'Other income and expenses in non-technical account' captures income streams earned by the shareholder fund and other shareholder expenses, including depreciation.

'Taxation' represents the impact of both current and deferred tax on the 'Underwriting performance' and the 'Other incomes and expenses'. UK corporation tax has been calculated at rates between 17% and 20% in accordance with the rates applicable to the long term business of a life insurance company.

Leasing arrangements

ZAL was not party to any finance lease arrangements.

ZAL has previously entered into certain operating lease contracts in relation to land and buildings where ZAL is lessor and has also entered into operating lease contracts with tenants where ZAL is the lessee. These consist of eight agreements where ZAL is lessor and eleven separate agreements where ZAL is lessee. No one lease is material in nature or in size.

A.5 Any other information

There is no other information to report.

B. System of governance

B.1 General information on the system of governance

This section provides information on ZAL's system of governance. This includes roles and responsibilities of the ZAL Board and Executive Committees, and remuneration policies and transactions with members of the Board. Under Solvency II ZAL is required to maintain a comprehensive and up-to-date governance map. ZAL uses this to set out the key functions in the firm and the relevant individuals responsible for these functions, along with their lines of accountability and responsibility both within the firm and the wider group.

ZAL's system of governance is well established and aligned to the wider governance principles of ZIG or the 'Group', as well as the requirements of Solvency II. The system of governance ensures that there are clear roles and responsibilities throughout the governance structure including the role of the Board, its Committees and the use of non-executive directors, with the effectiveness of the Board being reviewed on an annual basis. The system of governance is considered appropriate for the nature and scale of ZAL's business.

Zurich Assurance Ltd Board overview and role

ZAL is a wholly-owned subsidiary of a global insurance group ZIG and is aligned to the Group's internal organisational structure. The Board derives its collective authority by direct delegation from its shareholder. Its key purpose is to ensure ZAL's prosperity by collectively directing company affairs whilst meeting the appropriate interests of its key stakeholders, including its customers, employees and the shareholder.

The ZAL Board has two overarching responsibilities:

- To ensure the Company remains compliant with local law and meets the expectations of its regulators, paying due regard to jurisdictional best practice; and
- To maintain ZAL's business as a going concern in line with its strategic aims and targets or, if it was ever to be required, manage its orderly closure. In either respect, the directors should ensure full regard is paid to the interests and expectations of all of the Company's customers and other stakeholders.

The remit of the ZAL Board comprises:

- **Values and standards –** The Board sets the values and standards for ZAL. This is achieved by adopting and adapting the Group code of conduct and other applicable group policies;
- **Strategy –** Executive management proposes its strategy for ZAL to the ZAL Board, to consider and adopt it as appropriate. As a part of its considerations, the Board takes into account the appropriateness of this strategy, ensuring it can be executed in a compliant manner. The Board ensures the strategy is within its stated risk appetite, and considers the extent to which it will enable ZAL to meet the interests and expectations of its stakeholders;
- **Risk management –** The Board has responsibility for setting ZAL's risk appetite and must ensure risks are appropriately identified and managed. Capital policy and plans (over the short, medium and long term) including capital buffers are reviewed by management and approvals are sought from the Board as and when appropriate;
- **Systems and controls –** The Board has responsibility for the effectiveness of an appropriate system of internal controls to ensure the ongoing compliance of the Company with all applicable regulation and legislation, to protect the interests of customers and to ensure that risks are mitigated to within the stated risk appetite. The control framework ensures that, where regulation or legislation requires Board notification or decision, matters are brought to the attention of the Board in a timely manner and the Board has accountability for ensuring the completion of remedial actions;
- **Resources –** The Board retains responsibility for ensuring the ongoing adequacy and efficient usage of the resource available to the Company to deliver its strategy and operational plan. Examples of resource-types include human, financial, physical or technological; and
- **Audit, Risk and Investment Committees –** The Board is responsible for the operation of the committees to assist the Board in meeting the expectations of the regulators or other sources of jurisdictional best practice that may be applicable. The Board is responsible for approving the terms of reference for each of the committees.

ZAL's Board is composed of executive directors and independent non-executive directors. There is no formal limit to the number of directors that can sit on the Board, however, appointment is subject to group governance principles for subsidiaries. The table below shows the composition of the ZAL Board during 2016:

B. System of governance *continued*

Zurich Assurance Ltd Board of Directors

Individual	Role	Comments
N.A. Burnet	Executive Director	Resigned 25 February 2016
J.T.G. Butler	Independent Non-executive Director	Chair of Audit Committee
C.S. Fairclough	Independent Non-executive Director	Chair of Risk Committee
G.P.J. Shaughnessy	Executive Director	Resigned as CEO 1 January 2016, retained Directorship
J.B. Quin	Executive Director	Appointed 17 June 2016
I.C.R. Stuart	Independent Non-executive Director	Chair of Board and Investment Committee
J.R. Sykes	Executive Director	Appointed as CEO ad interim 1 January 2016, resigned as CEO ad interim 1 July 2016, retained Directorship
A Torry	Executive Director, CEO	Appointed as CEO 1 July 2016

Committees of the Board of Directors

The ZAL Board has three standing committees, which regularly report to the Board and submit proposals for resolution by the Board:

Risk Committee

The Risk Committee is authorised to assist the Board in carrying out its responsibilities in relation to the oversight of risk management in accordance with law and regulations by:

- Providing oversight and guidance to the Company and its management in relation to risk management and assisting in identifying issues requiring management's attention;
- Acting as a focal point for discussion and communication on matters regarding the oversight of risk management including monitoring adherence to the Board's defined risk appetite; and
- Giving sufficient attention to presented issues and information to determine which areas might require further review, additional attention and escalation.

Audit Committee

The Audit Committee is authorised to assist the Board in carrying out its responsibilities relating to financial reporting, internal control and governance, in accordance with regulation, legislation and acceptable ethical standards by:

- Providing oversight and guidance to the Company and its management with regard to the above matters and to assist in identifying issues requiring management's attention;
- Acting as a focal point for discussion and communication of matters regarding the oversight of financial reporting, internal control, compliance (including financial crime) and governance; and
- Giving sufficient attention to presented issues and information to determine areas for further review, additional attention and escalation.

The Audit Committee is also responsible for the oversight of the Company's external auditor, PwC.

Investment Committee

The Investment Committee is authorised to assist the Board in carrying out its responsibilities in relation to the oversight of investment management in accordance with law and regulations by:

- Providing oversight and guidance to the Company and its management in relation to investment management and assisting in identifying issues requiring management's attention;
- Acting as a focal point for discussion and communication of matters regarding the oversight of investment management; and
- Giving sufficient attention to presented issues and information to determine which areas might require further review, additional attention and escalation.

Executive Committee

The role of the Executive Committee is to support management and advise the Chief Executive Officer (CEO) on the day to day management of the business, ensuring executive alignment on courses of action for the business through robust challenge and decision-making and identifying any decisions that may need to be taken to the ZAL Board.

The following figure sets out the composition of the Executive Committee as of 31st December 2016:

Executive Committee

Name	Position held
Anne Torry	Chief Executive Officer, Chair
Helen Pickford	Chief Financial Officer
Shaun Hicks	Chief Risk Officer
Richard Peden	Head of Compliance and Market Insight
David White	Managing Director Retail
Jim Sykes	Chief Operating Officer, Managing Director InForce, Managing Director Corporate (ad interim)
Richard Pash	Director of Marketing
Emma Huntington	Managing Director FutureYou
Jeanette Harris	Human Resources Business Partner
Neil Hodges	UK General Counsel
Carol Canton	Head of Communications, UK

Key functions within ZAL

The key functions relating to corporate governance and risk management identified by ZAL are shown in the table below. Each key function holder is either a standing ex officio attendee of, or has a right of access to, the ZAL Board outside of their own management reporting line. This gives the individual the operational independence to carry out their tasks and advise and inform the Board of any issues or concerns.

Key function holders

PRA Definition	ZAL Role Title	Individual in Role
The Risk Management Function	Chief Risk Officer	Shaun Hicks
The Compliance Function	Head of Compliance and Market Insight	Richard Peden
The Internal Audit Function	Internal Audit Director	Helen Wroe
The Actuarial Function	Chief Life Actuary	Simon Johnson

Remuneration policy and guiding principles

ZAL is a subsidiary of ZIG and applies the Group's remuneration philosophy and agreed remuneration rules. The remuneration rules serve as a framework for the governance, design, implementation and monitoring of the Group's remuneration architecture globally. They are designed to support the business strategy, risk management framework and operational and financial plans for ZIG and its subsidiaries. Employees working on behalf of ZAL are predominantly employed by Zurich Employment Services Limited with the costs subsequently being recharged to ZAL. ZAL applies a remuneration policy in respect of these employees.

The ZIG Board is responsible for the design, implementation and monitoring of the Group's overall remuneration architecture. The ZIG Board has established a Remuneration Committee to oversee the design of the Group's remuneration architecture, the implementation of the remuneration rules and the respective monitoring process on behalf of the ZIG Board. The ZIG Board reviews the remuneration rules regularly, at least once a year. The rules are amended by the ZIG Board as necessary.

B. System of governance *continued*

The ZAL Board is responsible for its own remuneration arrangements and has developed its own remuneration policy statement in the context of the Group remuneration rules. The ZAL Board has delegated responsibility for reviewing and monitoring implementation of this policy to its Risk Committee. The Risk Committee meets on at least an annual basis to review the remuneration policy statement and its implementation.

ZAL operates a balanced and effectively managed remuneration system providing competitive total remuneration opportunities designed to attract, retain, motivate and reward employees to deliver high performance. The link between pay and performance is supported by fixed pay (i.e. base salary and benefits) and performance-related pay (short and long term bonus schemes as applicable).

The remuneration system is an important element of the Group's risk management framework and is designed to discourage inappropriate risk taking through effective governance and a clearly defined performance management process which supports the Group's overall strategy, values and long term interests. Performance-related pay is designed to promote sound risk management and does so by ensuring an appropriate balance between fixed and performance based elements.

Total remuneration and its composition may be influenced by factors such as scope and complexity of the role, level of responsibility, risk exposure, business performance, individual performance, internal equity, and legal requirements.

The key design principles of ZAL's remuneration arrangements include:

- Aligning remuneration structures to the delivery of good customer outcomes and adherence to corporate values;
- Being simple, transparent and implementable;
- Oriented towards the long term for those individuals who might have a material impact on the Company's risk profile;
- Ensuring the structure and level of total remuneration are aligned with risk policies and risk-taking capacity;
- Promoting a high performance culture by differentiating total remuneration based on the relative performance of businesses and individuals;
- Defining the expected performance through a structured system of performance management and using this as the basis for remuneration decisions; and
- Linking variable remuneration awards to key performance factors which include the performance aspects of the wider Group's business and the Company as well as individual achievements.

Total remuneration for employees of the Company can include the following elements:

Base salary
Base salary is the fixed pay for the role performed, determined by the scope and complexity of the role and is reviewed regularly. Overall base salary structures are positioned to manage salaries around the relevant market medians and take into account the individual's overall experience and performance. Employees may also participate in a defined contribution pension scheme.

Board members and key function holders are, where relevant, members of their respective country pension schemes and all arrangements are subject to the standard rules of those schemes.

Variable remuneration
ZAL operates variable short term and long term incentive plans aligned to the achievement of key financial objectives and the execution of the business strategy, risk management framework and operational plans.

Variable remuneration is structured such that typically there is a higher weighting towards the longer term sustainable performance for the most senior employees of the Group, including the individuals with the most impact on the Group's risk profile. This ensures that a significant portion of the variable pay for the senior group is deferred. Variable remuneration includes both short term incentive plans for which all employees are eligible to join and long term incentives for selected employees.

In alignment with the Group's risk profile and business strategy, long term incentives are provided with deferred effect taking into account material risks and the associated time horizon. Deferred bonuses vest after three to five years and the amount due is dependent on the ZIG share price at the date of vesting. In addition there are restrictions in place preventing the sales of half of the vested shares for a further three years.

Material transactions during the reporting period

There were no material transactions between ZAL and the members of its Board during the reporting period.

Material changes to the system of governance during the reporting period

Aside from the changes to ZAL's directors shown in this section there have been no material changes to ZAL's system of governance throughout the period.

B.2 Fit and proper requirements

ZAL applies fit and proper requirements to its approved persons, senior insurance managers (SIMF) and key function holders. Fitness means the knowledge, professional qualifications and relevant experience are adequate to enable sound and prudent management, control and oversight of ZAL. The concept of fitness also extends to the assessment of (collective fitness) – the collective diversity of qualifications of the senior managers of ZAL. Propriety is the evidence of good reputation and integrity (honesty and individual soundness).

ZAL operates a process for assessing the fitness and propriety of its SIMF and key function holders via background screening and pre-employment or pre-appointment checking carried out internally and through an external screening partner. To ensure that these individuals remain fit and proper an annual self-certification exercise takes place, and furthermore each year the fitness and propriety of a third of all such employees is checked by a third party. This means that all in-scope employees are independently verified every three years.

The collective fitness of the senior managers of ZAL refers to the qualifications and experience with respect to:

- Insurance and financial markets – awareness and understanding of the wider business, economic and market environment in which ZAL operates;
- Business strategy and business model – appropriate detailed understanding of these aspects with regard to ZAL;
- System of governance – awareness of the risks ZAL is facing and capability to manage them and to assess the effectiveness of the measures to deliver effective governance, oversight and controls and changes;
- Financial and actuarial analysis – ability to interpret ZAL's financial and actuarial information, identify key issues and put in place appropriate controls and take necessary measures; and
- Regulatory framework and requirements – awareness and understanding of the regulatory framework in which ZAL operates, awareness and understanding of requirements and expectations and adaptation of changes without delay.

B.3 Risk management system including the Own Risk and Solvency Assessment (ORSA)

Risk management framework

Risk management is integral to ZAL's strategy and operations. ZAL operates a rigorous risk management framework designed to promptly identify, measure, manage, report and monitor all risk types and associated risks that affect the achievement of strategic, operational and financial objectives. This includes reviewing the Company's risk profile and monitoring risk exposures against ZAL's risk appetite as defined by the Board, so that ZAL is able to respond to new risks and opportunities and to support risk-based decision making.

The Board defines ZAL's risk strategy and appetite and oversight of the risk management framework is provided by the Risk Committee which is authorised by the Board and its purpose is to assist the Board by:

- Providing oversight and guidance to the Company and its management in relation to risk management and assisting in identifying matters requiring management's attention;
- Acting as a focal point for discussion and communication of matters regarding risk management; and
- Giving sufficient attention to presented issues and information to determine which areas might require further review, additional attention and escalation.

B. System of governance *continued*

ZAL manages and mitigates the risks identified within the risk assessment process through specifically identified executive management actions which are tracked and reported.

Three lines of defence model

A 'three lines of defence' model is adopted and applied through the Group's risk governance structure to deliver integrated assurance and ensure risks are clearly identified, owned and managed so that:

- Business management takes risks and is responsible for day-to-day risk management;
- The risk management function oversees the overall risk management framework, and helps the business manage its risks. Other governance and key functions, such as compliance, legal, actuarial and finance help the business manage and control specific types of risks; and
- The audit function provides independent assurance regarding the effectiveness of the risk management framework and risk controls.

Risk management organisation

The Group Chief Risk Officer (CRO) leads the Group risk management function, which develops methods and processes for identifying, measuring, managing, monitoring and reporting risks throughout the Group. The Group sets out its risk management requirements through the 'Zurich Risk Policy' which specifies the Group's risk tolerance, risk limits and authorities, reporting requirements, procedures to approve any exceptions and procedures for referring risk issues to senior management and the Board of Directors.

The ZAL CRO reports to the Group CRO and has confidential access to the Chairperson of the ZAL Board Risk Committee to maintain organisational independence. ZAL's CRO organises the risk function along five main areas of responsibility:

- Risk assurance and oversight – responsible for processes and procedures required for the development of all the Risk Assurance activities;
- Strategy and insights – responsible for the oversight of commercial risk exposures within the business as well as providing model design;
- Regulatory oversight and actuarial assurance – responsible for providing oversight on all regulatory activities as well as assurance of capital management projections;
- Model validation – responsible for validation of capital management models; and
- Change – responsible for the delivery of regulatory and business framework projects.

The Own Risk and Solvency Assessment (ORSA)

The ORSA is the assessment of the current and future risk profile of ZAL as well as an assessment of regulatory capital requirements, including:

- The nature, scale and complexity of the current and likely future risks inherent to the business
- ZAL's solvency position under current and stressed conditions
- A forward-looking assessment of the solvency position over the planning horizon

The ORSA process addresses all material risk types that ZAL's business is exposed to and considers these over the short, medium and long term. The ORSA process is a continuous process made up of a combination of periodic and ongoing activities. It culminates in a formal ORSA report which is compiled on an annual basis as a minimum.

The ORSA is a key component of ZAL's risk framework with supporting processes integrated into the risk management system. The ORSA supports business planning and strategic decision making. Its risk governance principles are based on cooperation, participation and mitigation in achieving effective risk management. These principles are based on the 'three lines of defence' model and applied, as appropriate, to the ORSA process in ensuring the management and assurance over ZAL's risk exposures.

ZAL's ORSA process is composed of a number of individual processes and sub-processes which ultimately lead to the development of the ORSA report. The nature of the interaction between these supporting processes involves a mixture of direct and indirect relationships with key decision points and feedback loops. It is the fundamental aim of the ORSA process to demonstrate ZAL's understanding of the relationship between risk taking, its solvency position and its capital base.

Risk reporting

The CRO presents a comprehensive risk and capital report to ZAL's Board Risk Committee quarterly and provides more frequent information on ZAL's risk and capital position as deemed appropriate. The Chairperson of the Risk Committee provides appropriate risk and capital updates to the full Board. In addition to the Board and its committees risk reporting is presented to executive and non-executive management through a number of channels.

B.4 Internal control system

Internal control framework

The ZAL Board has overall responsibility for risk management and internal controls. Primary risk management and internal control systems are established at a group level and applied, where appropriate, by ZAL, with additional controls applied to meet ZAL's specific control requirements.

ZAL's management is responsible for identifying, evaluating and addressing significant risks, and designing and maintaining internal controls. The internal control framework is reviewed and updated on a regular basis in response to business change to ensure controls are appropriate and proportionate to the risk exposure.

The internal control framework increases the reliability of ZAL's financial reporting and its operational effectiveness, and ensures legal and regulatory compliance is maintained.

Internal and external auditors regularly report conclusions, observations and recommendations that arise as a result of their independent reviews and testing of internal controls over financial reporting and operations.

Compliance function

ZAL's compliance function provides policies and guidance, business advice, training and assurance over compliance controls. The compliance function also supports ZAL's management in maintaining and promoting a culture of compliance and ethics consistent with Zurich Basics, the Group's code of conduct.

The compliance framework relies on an ongoing compliance risk assessment to support a risk-based monitoring regime. The results of this assessment underpin the compliance function's strategic planning which is conducted in consultation with management. The compliance monitoring plan is presented annually to the Audit Committee and approved on behalf of the Board. Through this comprehensive monitoring program, the compliance function implements, embeds and monitors compliance with external regulation and internal policies and guidance.

ZAL operates a Model Governance Committee (MGC) to support the CRO in performing effective model governance, by overseeing the design and development of capital models and ensuring that they continue to be fit for purpose and operating as intended. The key components and responsibilities of model governance which are overseen by the committee are:

- Model development;
- Model change;
- Data quality; and
- Model validation

B. System of governance *continued*

B.5 Internal audit function

The internal audit function of the Group (Group Audit) reports to the Chair of the ZAL Audit Committee and is tasked with providing independent and objective assurance to the ZAL Board, Audit Committee, CEO and management. This is accomplished by developing a risk-based audit plan which is updated in response to changes in ZAL's risk profile. The plan is based on the full spectrum of business risks as well as concerns and issues raised by the Audit Committee, management and other stakeholders. Group Audit executes the plan in accordance with defined operating standards, which incorporate and comply with the International Standards for the Professional Practice of Internal Auditing, issued by the Institute of Internal Auditors (IIA). Key issues raised by Group Audit are communicated to the responsible management function, the CEO and the Audit Committee using a suite of reporting tools.

The ZAL Audit Committee approves the audit plan annually, and reviews reports from the Internal Audit Director on significant risk, control and governance issues every quarter as a minimum. The Internal Audit Director reports functionally to the Audit Committee and administratively to the CEO, and meets regularly with the Chairperson of the Audit Committee. Group Audit has no operational responsibilities over the areas it reviews. To ensure independence, all Group Audit employees globally report through to the Head of Group Audit.

Important audit findings, including ineffective opinions, mitigation actions and management responses are reported to the ZAL Audit Committee, Board and CEO. The ZAL Internal Audit Director is responsible for ensuring issues which could have an impact on ZAL's operations are brought to the attention of the Audit Committee and appropriate levels of management ensuring timely follow-up action occurs. This is supported by attendance at each meeting of the Audit Committee.

The Internal Audit Director is authorised to review all areas of ZAL and has unrestricted access to all of its activities, accounts, records, property and personnel necessary to fulfill its duties. In the course of its work, Group Audit takes into consideration the work of other assurance functions. In particular, Group Audit coordinates its activities with the external auditors, sharing risk assessments, work plans, audit reports and updates on audit actions.

The ZAL Audit Committee assesses the independence of Group Audit and reviews its activities, plans and organisation, the quality of its work and its cooperation with the external auditors. As required the Internal Audit function is quality-reviewed periodically, at least every five years, by an independent qualified body. This review was conducted most recently in 2016 and the results confirmed that Group Audit's practices conform with IIA standards.

B.6 Actuarial function

The UK Chief Life Actuary (CLA) heads ZAL's Actuarial function which is responsible for:

- Coordinating the calculation of the technical provisions;
- Ensuring appropriateness of methodologies, models and assumptions used in the calculation of the technical provisions;
- Assessing sufficiency and quality of data used in the calculation of technical provisions;
- Comparing best estimate against experience;
- Reporting to the ZAL Board on the adequacy of technical provisions;
- Expressing an opinion on the underwriting policy and adequacy of reinsurance arrangements;
- Contributing to the effective implementation of ZAL's risk management system; and
- Ensuring the Group's reporting and governance standards are adhered to.

The UK Life Actuarial function is made up of people within the Finance and Risk functions with sufficient knowledge of actuarial and financial mathematics to carry out the work of the actuarial function. The Risk team is fully independent from the team calculating the technical provisions and from the underwriting and reinsurance area. As a result the Risk team are able to provide an independent viewpoint to the ZAL Board.

The UK CLA reports into the UK Life Chief Financial Officer (CFO), with direct access to the ZAL Board. The UK CLA is an approved person under the PRA's SIMF regime (SIMF 20).

B.7 Outsourcing

Outsourcing is an arrangement by which a business capability is performed by a service provider instead of being performed by ZAL . This enables ZAL to focus on its core business capabilities. Outsourcing poses risks, particularly operational, reputation and credit risks, which must be managed.

A service provider may be either a third party external to ZAL, or another Zurich unit or function other than ZAL (also called intra-group sourcing). ZAL makes use of service providers covering a range of services and has a comprehensive policy to manage the associated outsourcing risks. It is ZAL's policy to manage the risks in outsourcing by:

- Only outsourcing work such that ZAL retains effective control over its business;
- Assessing and mitigating potential risks before making the decision to outsource and during the life of the outsourcing arrangement;
- Standardising the selection and management of outsourcing arrangements in order to manage exposure to third parties;
- Making use of globally selected suppliers to more effectively oversee and manage risk in outsourcing, taking into account potential effects of concentration risk;
- Maintaining an inventory of service providers and outsourced work to detect potential areas of concentration;
- Establishing internal controls and monitoring them through the life of the outsourcing arrangement; and
- Developing and maintaining strategies to exit from outsourcing arrangements.

Applicable standards for managing outsourcing are set out in ZAL's risk policy supplemented by the Zurich Group's sourcing policy. These documents address key processes including: fair and unbiased supplier selection, due diligence requirements, contracting, managing service delivery, risk and issues management and exiting outsourcing arrangements.

These standards and processes are applicable to both external suppliers and intra-group arrangements and are applied on a risk-based and proportionate basis depending upon the materiality of the relationship. This is assessed using factors including the financial value and financial liability associated with the arrangement, the extent to which customer data is shared and the degree to which Zurich's business and reputation may be affected by a failure of that relationship.

Some activities have a higher level of oversight and set requirements for how they are managed in an outsourcing arrangement. The critical activities are:

- Compliance with Zurich's policies and legal and regulatory requirements;
- Ongoing risk management;
- Internal audit, accounting and finance operations;
- Actuarial activities;
- Storing, retaining and transferring confidential and highly confidential data; and
- Maintaining and supporting IT systems.

Third party oversight is achieved through a framework of regular cross-business forums which cover: service delivery (against agreed service levels), financial management (against agreed forecasts), assurance and transformation.

All outsourcing activity within ZAL is overseen by the Chief Operating Officer who is the key function holder responsible for outsourcing.

A list of ZAL's critical and important outsourcing arrangements is provided in the table below.

B. System of governance *continued*

Outsourcers

Operational function	Outsourcer	Location
Investment Funds	Mercer Global Investments	UK
Operational Administration	Capita Life & Pensions	UK
Investment Funds	Nikko Asset Management	UK
Investment Funds	Schroder Investment Management	UK
Investment Funds	Threadneedle Asset Management	UK
IT Support & Delivery	CSC	UK
Document Logistics	RR Donnelly	UK
Document Logistics	Swiss Post	UK

B.8 Any other information

With-profits business

ZAL operates two ring-fenced with-profits funds and has appointed a With-Profits Actuary who reports to the CRO. The role of the With-Profits Actuary is to provide ZAL management and the ZAL Board with actuarial advice for the with-profits funds. The With-Profits Actuary supports ZAL in maintaining compliance with regulatory requirements and ensuring an appropriate balance between fairness to policyholders and the mitigation of risks to the shareholder including the risk that with-profits funds may not be able to meet liabilities to policyholders as they fall due.

C. Risk profile

Introduction

This section sets out and describes;
- The material risks in ZAL's risk profile;
- The processes used to identify and monitor these risks; and
- The mitigation techniques used to reduce risk exposures to within ZAL's risk tolerance and appetite.

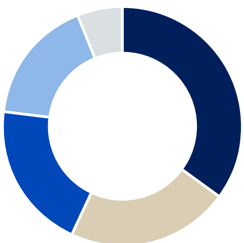
ZAL's business model results in it being subject to a range of risks associated with the activity of issuing insurance and investment contracts and the use of financial instruments.

These include risks for which ZAL holds capital - underwriting risk, market risk, credit risk, operational risk and pension scheme risk - and also risks for which other mitigation techniques are applied such as liquidity risk.

Regulatory capital, assessed on the Solvency II standard formula basis, is held to cover the risks associated with ZAL's balance sheet position where the value depends on financial markets, best estimate assumptions being different to expected, operational risks and failures of counterparties. Capital is held for staff pension scheme risk not covered by the standard formula where the scheme is not directly held on the balance sheet, as is the case for ZAL. More detail of the pension scheme risk is provided in section C.6 'Other material risks'.

The capital held by ZAL is broken down in the figure below:

ZAL Solvency II Capital by Risk (Undiversified)
%, as of December 31, 2016



Underwriting	35%
Pension Scheme	22%
Market	20%
Credit	17%
Operational	6%

Further information on each risk is provided in the sections below including sensitivity analysis where appropriate. To measure ZAL's sensitivity to its material risks stresses are performed on each of the risk types and the impact on own funds calculated. Material risks are identified by analysing ZAL's Solvency II standard formula SCR as at December 31, 2016. The stresses performed are the Solvency II standard formula stresses calibrated to the equivalent of a 1 in 20 year event. In performing the sensitivity analysis, ZAL has used assumptions consistent with the Solvency II standard formula. The impact of own funds presented allows for movements in asset values, best estimate liabilities and risk margin.

ZAL mitigates its risks so that they are kept within the Board's stated risk appetite. Throughout 2016 ZAL remained within this appetite in all material regards. A wide range of mitigation techniques are available to ZAL, and these are discussed below. At a high level the key mitigation techniques are:

- Reinsurance;
- Outsourcing;
- Robust system of governance and oversight arrangements; and
- Derivatives used for hedging purposes.

C. Risk profile *continued*

C.1 Underwriting risk

Underwriting risk is the inherent uncertainty regarding the occurrence, amount or timing of insurance liabilities. The specific risks ZAL is exposed to associated with underwriting include:

- Mortality – actual policyholder death experience is higher than expected.
- Longevity – annuitants live longer than expected.
- Morbidity / disability – policyholder health-related claims are higher than expected.
- Lapse – policyholder behaviour in discontinuing or reducing contributions or withdrawing benefits prior to the maturity of contracts is different to that expected.
- Expense – expenses incurred in acquiring and administering policies are higher than expected.
- Catastrophe – policyholder health and death related claims from a large scale event.

ZAL quantifies underwriting risk as part of its Solvency Capital Requirements. As well as holding capital, ZAL uses a variety of risk mitigation techniques which help it manage and reduce its exposure to underwriting risks.

ZAL has a system of regular monitoring which reports on the mortality, longevity, morbidity, lapse and expense experience of the business. This is used to help determine the rates at which new business is accepted and the value of ZAL's technical provisions. In addition to monitoring business experience ZAL regularly assesses whether its underwriting risk exposures are in line with its expectations and its risk appetite.

Risk mitigation techniques and their effectiveness

ZAL uses a number of techniques to mitigate underwriting risk as set out below:

Reinsurance
ZAL's principal mitigation technique for underwriting risk is reinsurance. ZAL effectively mitigates its morbidity, mortality, longevity and catastrophe risks by reinsuring a significant proportion of its underwriting risk both with other entities within the Zurich Group and with external reinsurers. The use of reinsurance reduces financial volatility in ZAL and the capital requirement for underwriting risk. ZAL retains risks in line with its risk appetite. ZAL's actuarial function and regular governance meetings oversee the use and effectiveness of its reinsurance arrangements and review arrangements on a regular basis.

Underwriting discipline, product design and expense management
Alongside reinsurance, a number of other techniques are used to mitigate underwriting risk. Underwriting discipline is a fundamental part of managing underwriting risk and applies to product design and approval and the underwriting process. When designing certain products ZAL makes use of product features such as reviewable charges which enable ZAL to charge an appropriate rate for the risks associated with these policies.
ZAL further mitigates underwriting risk by underwriting individual protection business at the point of application and claim. The process involves reviewing appropriate policyholder medical information and if required seeking additional information to support the underwriting decision.

ZAL mitigates underwriting risk for group protection policies by both underwriting the scheme risk for cover below the automatic acceptance limit and underwriting individual benefit exposures that exceed this at the point of application and claim.

The continued suitability and the potential risks of existing life products are regularly reviewed.

The risk that administration expenses increase is mitigated through robust budgeting and expense management processes, by use of outsourcing where appropriate – including for policy administration on a fixed per policy basis, in real terms – and the application of efficiency methodologies within ZAL's business.

Analysis of sensitivities for underwriting risk

ZAL's sensitivities to underwriting risks are shown in the table below. ZAL has used assumptions consistent with the Solvency II standard formula.

Sensitivities are not shown for catastrophe and mortality risks as these are not a material component of ZAL's Solvency II standard formula SCR due to the risk mitigation techniques that ZAL uses. ZAL's greatest sensitivity is to lapse risk where it is sensitive to a reduction in expected future profits from unit-linked business, and expense risk where higher than expected expenses could reduce expected future profits.

Impact of life insurance risk scenarios on basic own funds

Life insurance risk scenario results	Impact on Basic Own Funds (in £'000)
Lapse	(123,323)
Expenses	(102,885)
Longevity	(34,887)
Morbidity	(27,009)

The impacts have been calculated using the following 1 in 20 year stresses:

- Lapse: a mass lapse event of 25.5% on individual business and 44.7% on group business
- Expenses: a 6.4% increase in renewal expenses and a 0.6% increase in expense inflation
- Longevity: a 12.8% reduction in the number of deaths experienced at each age
- Morbidity: claim incidences increase by 22.4% in year 1 and 16.0% thereafter, with a 12% reduction in recovery rates

C.2 Market risk

Market risk is the risk associated with ZAL's assets and liabilities where their value or cash flow depends on financial markets; this includes the market value of ZAL's balance sheet positions and future earnings on contracts linked to the value of unit-linked assets.

The risks associated with market risk include:

- Equity price risk – risk of loss resulting from changes in equity prices;
- Property price risk – risk of loss resulting from changes in property prices;
- Interest rate risk – risk of loss resulting from changes in interest rates, including changes in the shape of yield curves;
- Credit spread risk – risk of loss resulting from widening of credit spreads; and
- Currency exchange rate risk – risk of loss resulting from currency exchange rate movements.

ZAL quantifies market risk as part of its Solvency Capital Requirements, ZAL uses a variety of risk mitigation techniques which helps it manage and reduce its exposure to market risks. ZAL monitors and controls exposures to market risk by aligning its strategic asset allocation to its risk appetite. Consideration is given to regulatory requirements, liability profiles and capital impacts. ZAL operates an Investment Committee which has responsibility for the implementation, monitoring and evaluation of this process and approves any changes to the strategic asset allocation, including within with-profits funds.

ZAL's Investment Committee sets, reviews and monitors ZAL's strategic asset allocation and boundaries and monitors ZAL's asset/liability exposure. Risk assessments include quantification of the contributions to financial market risk from major risk drivers. The economic effect of potential extreme market moves is regularly examined and considered when setting the asset allocation.

Through the implementation of the risk management techniques and processes detailed in this section, ZAL also ensures that the management of assets is in line with that which would be expected of a prudent person managing such assets.

Risk mitigation techniques and their effectiveness

ZAL uses a variety of risk mitigation techniques to effectively manage market risks. The specific risk mitigation technique depends on the risk. For ZAL's material market risks the mitigation techniques used are outlined below.

C. Risk profile *continued*

Equity risk
ZAL uses a derivative strategy to mitigate equity risk within its unit-linked business. Derivatives are used to protect the value of expected future management charges less investment expenses against movements in equity prices, maintaining the economic value of the Company to the shareholder. ZAL is exposed to a low level of equity risk as the equity derivative strategy does not cover all of the equity exposure within the with-profits funds or the equity exposure within ZAL's Hong Kong branch.

Credit spread risk
Spread risk is mitigated by limiting ZAL's investment exposure to lower credit quality assets.

Interest rate risk
ZAL mitigates its interest rate risk by specifying fixed interest portfolio mandates which include target asset durations and range limits. Matching target asset durations consistent with the liability durations further reduces this risk.

Analysis of market risk sensitivities

ZAL's sensitivities to market risk are shown in the table below. ZAL has used assumptions consistent with the Solvency II standard formula.

Consistent with ZAL's Solvency II standard formula SCR, credit spread is the market risk that ZAL is most sensitive to. This is driven by ZAL's holdings of corporate bonds which are used to back policyholder liabilities.

Currency risk is primarily driven by policyholders choosing assets in foreign denominations, which exposes ZAL to the fluctuations in future annual management charges on these assets. Due to the effectiveness of mitigation techniques equity risk is not a material component of ZAL's Solvency II standard formula SCR, therefore no sensitivities are shown.

Analysis of economic sensitivities on market risk exposure

Sensitivity Scenarios	Impact on Basic Own Funds (in £'000)
Interest rate up	(14,000)
Interest rate down	2,000
Credit spread	(80,000)
Currency	(58,000)

The impacts have been calculated using the following 1 in 20 year events:

- Interest rate up: a 0.64% increase in the risk free interest rate
- Interest rate down: a 0.22% reduction in the risk free interest rate
- Currency: a 16% strengthening of sterling relative to other currencies

For the credit spread sensitivity spreads have been assumed to widen with the change, varying by the credit rating and duration of the asset held to give an overall 1 in 20 year event.

C.3 Credit risk

Counterparty credit risk is the risk associated with a loss or potential loss from counterparties failing to fulfil their financial obligations. ZAL's exposure to counterparty credit risk is derived from the following main asset categories:

- Cash and cash equivalents
- Reinsurance assets
- Receivables
- Derivatives

ZAL is also exposed to credit risk by the use of fund reinsurance to access external funds provided by other life insurers. Here the legal form is a reinsurance arrangement but in practice the fund operates in the same way as a collective investment arrangement. ZAL considers its exposure to the risks associated with these funds to be very low however it does hold capital for these arrangements under its Solvency II standard formula SCR, which requires the same treatment as for other reinsurances.

ZAL quantifies credit risk as part of its Solvency Capital Requirements. ZAL implements credit exposure limits and regularly monitors credit exposures to individual counterparty and related counterparties by aggregating exposures across various types of credit risk. The limits vary based on the underlying counterparty rating and appropriate benchmarks.

Risk mitigation techniques and their effectiveness

ZAL's credit risk exposures are monitored by its Investment Committee. ZAL controls credit risk primarily through implementation and adherence to policies for credit risk concentration and average credit rating target, as well as through regular routine monitoring through its liquidity and reinsurance forums.

Cash and cash equivalents
In order to mitigate concentration, settlement and operational risks related to cash and cash equivalents, ZAL limits the maximum cash amount that can be deposited with a single counterparty and maintains an authorised list of acceptable cash counterparties based on current ratings and outlook.

Reinsurance Assets
ZAL typically cedes new business, both internally and externally, to authorised reinsurers with a minimum credit rating of 'A-'. ZAL maintains a list of authorised acceptable reinsurance counterparties based on current ratings and outlook, taking the analysis of fundamentals and market indicators into account. Credit risk is also mitigated by the reinsurers placing collateral of acceptable quality.

Receivables
ZAL reports internally on past due receivable balances and aims to keep the balance of past due positions as low as possible. ZAL has a small amount of exposure to intermediaries where commission is paid on policies which are later cancelled; this is managed via the commission claw-back process to further limit the size and duration of any exposure.

Derivatives
To limit credit risk, derivative financial instruments are typically executed with counterparties rated "A–" or better by an external rating agency. ZAL only transacts derivatives with counterparties where a credit support agreement is in place – this mitigates credit exposures from over-the-counter transactions due to close-out netting and requires the counterparty to post collateral when the derivative position is beyond an agreed threshold. Derivative valuation reconciliation and collateral assessments take place on a daily basis to ensure credit risk is appropriately mitigated.

Analysis of credit risk sensitivities

ZAL's sensitivity to counterparty credit risk is primarily driven by its exposure to fund and risk reinsurers. As the exposure to reinsurers is significantly mitigated through the use of collateral arrangements ZAL's most material sensitivity is to fund reinsurers. ZAL is sensitive to both increases in the probability of default and the loss given default and increases in these will reduce own funds. In a 1 in 20 year stress calculation the probability of default is expected to be very small and as a result any impact on own funds would be immaterial.

C. Risk profile *continued*

C.4 Liquidity risk

Liquidity risk is the risk that ZAL may not have sufficient liquid financial resources to meet its obligations when they fall due, or would have to incur excessive costs to do so.

ZAL monitors liquidity risk by projecting expected future payments and buys and sells investments, including cash and cash equivalents, with the objective of having sufficient cash to meet payments as they fall due. The amount of cash is managed separately for each unit-linked fund and set at a level which aims to reflect the liquidity of the other investments in the fund.

ZAL monitors the impact of financial market volatility on the level of policy surrenders, funds withdrawals and fund switches. In response ZAL holds appropriate levels of unencumbered liquidity to meet any potential increases in withdrawals, including those from unit-linked funds.

A liquidity governance framework is in place to monitor liquidity in the short, medium and long term. This ensures there are appropriate liquidity levels at all times. This framework monitors liquidity risk by taking into account the amount, availability and speed at which assets can be accessed and includes daily liquidity monitoring.

Disclosure of expected profit included in future premiums

As at December 31, 2016 ZAL's expected profit included in future premiums (EPIFP) was £285 million. Whilst this contributed to ZAL's own funds, it is not liquid and not taken into account when assessing ZAL's liquidity position.

Risk mitigation techniques and their effectiveness

Whilst operational liquidity risk is inherent to the nature of the business that ZAL operates, it is also in the nature of long term insurance that ZAL has large volumes of assets which are either liquid or generate steady liquidity. While small amounts of liquidity risk are unavoidable, the Board's requirement is for ZAL to ensure sufficient liquidity to meet all forecast cash outflows in the short and medium term.

Analysis of liquidity sensitivities

ZAL mitigates liquidity risk by ensuring it holds enough liquid assets under a range of scenarios. Given this approach the impact on ZAL's own funds from a liquidity sensitivity would be zero and a sensitivity analysis is not applicable.

C.5 Operational risk

Operational risk is 'the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events such as outsourcing, catastrophes, legislation, external fraud including cyber risk'. This definition includes legal, compliance and customer conduct risks. ZAL quantifies its exposure to operational risk as part of its Solvency Capital Requirement.

Risk mitigation techniques and their effectiveness

Operational risk mitigation enables ZAL to manage the likelihood of operational risks occurring and to reduce the impact should they occur. To achieve this ZAL implements a robust and comprehensive framework for identifying, assessing, managing and reporting operational risk.

This framework ensures that material operational risks are fully understood and appropriately managed to within ZAL's risk appetite. ZAL makes use of a number of processes and tools to understand and manage its operational risk profile including risk and control assessments, loss event management, scenario analysis and reverse stress testing.

As part of the operational risk framework, ZAL operates a robust conduct risk framework in order to manage the risks to the delivery of customer outcomes in all its businesses. This approach allows ZAL to adequately identify, analyse and prioritise conduct risk exposures from within its business models and strategies and equally evaluate the resultant impact on its conduct risk appetite.

ZAL's exposure to operational risk is mitigated by a system of internal controls, capital, corporate internal insurance programmes and its business continuity planning process.

Analysis of operational risk sensitivities

ZAL uses the Solvency II standard formula to calculate its capital requirement for operational risk. As a result its sensitivity to operational risk is based on the factors affecting this calculation which are primarily expenses on unit-linked business. Due to the formulaic nature of the calculation no quantitative analysis is provided. However, ZAL further seeks to understand operational risk sensitivities through the use of specific operational risk scenario analysis.

C.6 Other material risks

Off balance sheet risks

As ZAL does not transfer any risk to special purpose vehicles, it is not exposed to any risks arising from their use.

ZAL may be exposed to pension scheme risk. This is the risk that ZAL may need to support its parent company UKISA in securing funding for the defined benefit staff pension scheme, following changes in the assets or liabilities of the scheme.

Employees in the UK working on behalf of ZAL are predominantly employed by Zurich Employment Services Limited (ZES), a wholly owned subsidiary of UKISA. The employees of ZES mainly participate in a pension scheme which contains both defined benefit and defined contribution sections. The defined benefit sections of the scheme were closed to new entrants in March 2007 and to further accruals from 1 January 2016. The financial position of the pension scheme is recognised in the ZES balance sheet. UKISA, as the pension scheme sponsoring company, is obliged under the scheme rules to procure payment of contributions that the participating employers, including ZES, are required to make into the scheme.

Although ZAL is not bound by any legal obligation to support the pension scheme, under extreme circumstances there remains a risk that ZAL may be required to assist its parent UKISA in securing the funding ZES may be required to make to the pension scheme. The Solvency II standard formula does not cover this off balance sheet pension scheme risk. To reflect this specific limitation of the standard formula when applied to ZAL's business, ZAL has agreed a capital add-on with the PRA. ZAL is in the process of developing a partial internal model to capture the pension scheme risk and replace the capital add-on in due course.

Other risks for which ZAL does not hold capital

In addition to the risks identified above ZAL is also exposed to a number of other risks for which ZAL does not hold capital as it is not the most appropriate mitigant. The most material of these risks are strategic risk, reputational risk and group risk. These risks are detailed below.

Strategic risk
Strategic risk is the unintended risk that can result as a by-product of planning or executing the strategy. Strategic risks can arise from:

- Inadequate assessment of strategic plans;
- Ineffective implementation of strategic plans; and
- Unexpected changes to assumptions underlying strategic plans.

ZAL works to reduce unintended risks of strategic business decisions through its risk assessment processes and tools, including its strategic level risk assessment process. As part of this regular process, ZAL's Executive Management identifies both current and future key strategic risks. The material strategic risks are mitigated through robust and diligent Board and Executive Management governance processes. These provide the means through which strategic plans are reviewed, challenged and refined. Through this comprehensive and iterative process strategic risk is mitigated.

C. Risk profile *continued*

Reputational risk

Reputational risk is the risk that an act or omission by ZAL, or the Group to which the Company belongs, or any of its employees results in a loss of reputation or trust in the Company among any of its stakeholders. ZAL accepts that exposure to these risks cannot be completely avoided and continues to take risk on a well informed and conscious basis.

Reputational risk is primarily a consequence of the crystallisation of other risks, most notably operational risk. Reputational risk is effectively managed through business controls, including but not restricted to appropriate recruitment and vetting procedures and a suitable business culture and ethos, supplemented by effective media relations and communications activity.

Group risk

Group risk is the risk of loss resulting from the failure of a group company as a going concern, or from the failure of a group company to provide key outsourced services as required by ZAL.

These can be broadly categorised as;

- Operational outsourcing risk – these are the risks associated with the failure of shared services or functions outsourced to other parts of the Group;
- Brand and reputational risk – this is the risk that a event occurs elsewhere in the group which generates negative publicity which adversely impacts ZAL's business; and
- Risks relating to intra-group reinsurance.

ZAL has intra-group agreements in place for all outsourcing placed with group companies that is categorised as critical or important. Monitoring of all outsourcing arrangements is undertaken by the designated outsourcing contract owners. The Board receive an annual update on the current list of critical and important outsourcing arrangements.

The Board recognises that there are significant advantages to being part of a well-capitalised international group and that these outweigh potential group risks.

Given ZAL's business model, potential group risk exposures are largely unavoidable and the purchase of financial mitigation for this risk is not commercially realistic. In accordance with the Board's risk strategy, group risk will continue to be taken on a well informed and conscious basis. The Board recognises that the consequential risks arising from the failure of a Zurich Group entity to provide services are identified and considered both within Executive Management's functional oversight processes and within ZAL's approaches for operational risk, credit risk and stress testing.

C.7 Any other information

There is no other material information to report

D. Valuation for solvency purposes

D.1 Assets

This section sets out the principles of valuation that ZAL uses to calculate its assets for solvency reporting and explains the differences compared to the valuation used in ZAL's financial statements which are prepared using UK GAAP.

Recognition of Assets

All regular way purchases and sales of financial investments are recognised on the trade date i.e. the date the Company commits to purchase or sell the investments. Such purchases or sales of financial investments are those under a contract whose terms require the delivery of assets within the time frame established by regulation or market convention.

Asset valuation methodologies for Solvency II

The Solvency II balance sheet is presented in the 'Valuation of asset types for financial reporting and solvency purposes' table below. The asset valuation methodologies used to calculate this balance sheet are set out below.

Assets valued using mark to market methods
The significant majority of ZAL's assets are unit-linked assets, which are valued using mark to market methods as described below.

The fair value of instruments traded in active markets is based on quoted bid prices provided by third party data providers as at the valuation date. In certain cases prices are provided using other valuation techniques, but where all significant valuation inputs are based on observable market data (e.g. broker quotes) these assets are considered as mark to market.

These assets are reported in the 'Investments (other than assets held for index-linked and unit-linked contracts)' and 'Assets held for index-linked and unit-linked contracts' asset classes.

Assets valued using mark to model methods
The mark to model valuation approach relates to pricing techniques where at least one of the significant inputs is not based on observable market data and applies to the valuation of the following assets of ZAL:

Derivatives
ZAL has holdings of over-the-counter (OTC) options. OTC options use a valuation model based on a number of parameters, including market value of the underlying interest rate curve, volatility surfaces and dividend yields.

ZAL also permits holdings of derivatives including OTC foreign exchange (FX) forwards within unit-linked funds, where appropriate and relevant to the investment objective, for the purposes of efficient portfolio management. In these cases, the value of the FX forward is an exposure within the specific unit-linked fund and is valued using discounted interest rate curves and FX spot rates.

Holdings in related undertakings, including participations
All assets and liabilities of subsidiaries are valued in line with Solvency II valuation rules using the adjusted equity method. Therefore a subsidiary's own funds value is market consistent. Participations represent the value of ZAL's subsidiary companies.

Assets held for index-linked and unit-linked contracts
The fair value of these assets is principally determined using external pricing services. Liquidity and market activity levels are used to determine fair value where the pricing of these assets is not based on fully observable inputs.

Reinsurance recoverables
The calculation of the Solvency II reinsurance recoverables is the same as for the Best Estimate Liability, see section D.2 – 'Calculation of the Best Estimate Liabilities' for further details.

D. Valuation for solvency purposes *continued*

Private loans secured on real estate
Private loans secured on real estate are included within the 'Investments (other than assets held for unit-linked contracts)' asset class at fair value. Fair value is arrived at by discounting the known cashflows by an appropriate discount rate, which gives consideration to prevailing market rate plus an idiosyncratic spread relating to the risk of the investment.

Other valuation methods
This refers to assets that are mainly recorded at fair value, which is their nominal amount adjusted for the probability of default of the counterparty.

This also includes the valuation of the following assets:

Intangible Assets
The economic value of deferred acquisition costs (DAC) is nil for solvency purposes, as required by Solvency II regulations.

Deferred tax assets
Provision is made for deferred tax assets, using the liability method, on all material timing differences including revaluation gains and losses on investments recognised in the profit and loss account. Deferred tax is calculated at the rates at which it is expected that the tax will arise. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

The deferred tax asset is in respect of certain investment losses which can be utilised against certain future investment gains and has no maturity date.

Property, plant and equipment held for own use
Property, plant and equipment are included at fair value.

Property (other than for own use)
The Fair value model is used for the valuation of investment property. The investment method of valuation determines the fair and best value of a freehold or leasehold interest in commercial property reflecting the risk, return and expectation of growth through the application of yields and assessment of current rental value, assessed by the analysis of comparable investment or rental transactions.

Properties are valued on a monthly basis by Jones Lang LaSalle Limited and CBRE Limited, with the exception of the agricultural portfolio that is valued on an annual basis by Bidwells and Savills (UK) Limited. The valuations are undertaken in accordance with the RICS Valuation - Professional Standards 6 January 2014 (the 'Red Book'), by independent valuers who have the relevant qualifications and experience. The date of the last valuation for all land and buildings was 31 December 2016.

Loans and Mortgages
Loans and Mortgages have been valued in accordance with IAS 39. They are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These investments are initially recognised at cost, being the fair value of the consideration paid for the acquisition of the investments, and are subsequently valued at fair value. All transaction costs directly attributable to the acquisition are also included in the cost of the investments.

ZAL is not party to any finance lease arrangements.

ZAL has no material operating lease arrangements as described in section A.4.

There have been no material changes made to the recognition and valuation basis during the period.

There are no future management actions that would impact on the above.

No assets are deemed to be long term in nature, therefore no adjustments have been made in respect of uncertain future events.

Sensitivities

Fair values for assets valued using mark to model methods are sensitive to changes in key assumptions, within the following categories:

Holdings in related undertakings including participations
There is no material sensitivity around the fair value of each of ZAL's interests in subsidiary undertakings.

Assets held for index-linked and unit-linked contracts
This asset category includes investments in property partnerships and other securities, which are quoted on an exchange.

Debt securities and other fixed income securities
This asset category includes asset-backed securities.

The key assumptions driving the valuation of these investments include equity levels, discount rates, credit spreads rates and prepayment rates. The effect on reported fair values of using alternative values for each of these assumptions, while the other key assumptions remain unchanged, is disclosed in the table below.

Sensitivity analysis

£'000	Less favourable values (relative change)	Decrease in reported fair value	More favourable values (relative change)	Increase in reported fair value
Key assumptions				
Equity levels	(20%)	(1,877)	20%	1,877
Discount rates	20%	(3,975)	(20%)	3,975
Spread rates	20%	(3,729)	(20%)	3,729
Prepayment rates	(20%)	(52)	20%	52

The sensitivity analysis is intended to reflect the uncertainty inherent in the valuation of these investments under current market conditions, and its results cannot be extrapolated due to non-linear effects that changes in valuation assumptions may have on the fair value of these investments. Furthermore, the analysis does not indicate a probability of such changes occurring and it does not necessarily represent ZAL's view of expected future changes in the fair value of these investments. Any management actions that may be taken to mitigate the inherent risks are not reflected in this analysis.

The table above gives the impact on fair value of the assets. Any change in the fair value of the assets does not correlate directly to the movement in the value of basic own funds and the excess of assets over liabilities, due to an offset within technical provisions. Any direct impacts are deemed to be immaterial.

Differences between Solvency II valuation and UK GAAP (FRS 101 'Reduced disclosure framework')

The table below sets out the differences between the valuation of assets under Solvency II and UK GAAP.

D. Valuation for solvency purposes *continued*

Valuation of asset types for financial reporting and solvency purposes

in £'000 Total Assets split by material classes of assets	Solvency II	Financial Statements (UK GAAP)	Difference
Deferred acquisition costs	–	274,198	(274,198)
Deferred tax assets	626	–	626
Property, plant & equipment held for own use	2,396	2,396	–
Investments (other than assets held for index-linked and unit-linked contracts)	3,895,828	3,894,285	1,543
Assets held for index-linked and unit-linked contracts	32,168,371	46,026,902	(13,858,531)
Loans and mortgages	62,280	62,280	-
Reinsurance recoverables	16,314,425	2,991,223	13,323,202
Insurance and intermediaries receivables	83,700	83,763	(63)
Reinsurance receivables	180,789	180,447	342
Receivables (trade, not insurance)	62,153	29,871	32,282
Cash and cash equivalents	184,924	184,924	-
Any other assets, not elsewhere shown	20,813	33,836	(13,023)
Total assets	**52,976,305**	**53,764,125**	**(787,820)**

The UK GAAP figures above use the Solvency II balance sheet presentation. For certain balance sheet headings the reported figures above may differ from the presentation in the financial statements.

The main valuation differences between Solvency II and UK GAAP are explained below.

Deferred acquisition costs

Under UK GAAP the costs of acquiring new business, other than for with-profits business, are deferred to the extent that they are recoverable. DAC is included in the UK GAAP Balance Sheet as an asset.

Under Solvency II the economic value of the DAC asset is nil, as required by the regulations.

Assets held for index-linked and unit-linked contracts

Under UK GAAP unit-linked funds reinsurance contracts are treated as investment contracts as required by IFRS 4 and are therefore disclosed in 'Assets held for index-linked and unit-linked contracts'. Solvency II requires the legal form to be followed and they are presented as reinsurance recoverables.

Reinsurance recoverables

The different presentation of the unit-linked fund reinsurance is explained under the 'Assets held for index-linked and unit-linked contracts' section above.

The valuation of the reinsurance recoverable asset differs between Solvency II and UK GAAP due to the difference in the valuation of the underlying liabilities. The explanation of the difference in the valuation of the liabilities is included in section D.2 – 'Technical provisions reconciliation to financial statements'.

D.2 Technical provisions

Technical provisions overview

The technical provisions are prepared in accordance to Solvency II requirements. The value of the technical provisions is the sum of the Best Estimate Liabilities (BEL) plus a risk margin.

ZAL's approach to the valuation of BEL and risk margin is described in more detail below.

Technical provisions by line of business

in £'000	Best Estimate	Risk Margin	Technical Provisions (total)
Insurance with-profits participation	1,644,981	73,721	1,718,702
Other life (excluding health and index-linked and unit-linked)	2,770,177	19,024	2,789,201
Index-linked and unit-linked	44,962,793	309,059	45,271,852
Health insurance (direct business)	226,578	47,607	274,185
Health reinsurance (reinsurance accepted)	2,004	-	2,004
Total	**49,606,533**	**449,411**	**50,055,944**

Calculation of the Best Estimate Liabilities

Insurance with-profits participation (with-profits business)

The BEL is calculated as the present value of the expected future cash flows in respect of the policies (for example premiums, investment returns, claims and cost of administrations) projected using a stochastic valuation. A wide range of economic outcomes are considered in the valuation of any options and guarantees. The BEL also includes provision for vested and future bonuses at rates consistent with the Company's Principles and Practices of Financial Management.

Index-linked and unit-linked insurance, other life insurance, and health (direct and reinsurance accepted) insurance

The BEL is calculated as the present value of the expected future cash flows on the policies, projected using a single set of best estimate assumptions.

Where products have material options and guarantees, the BEL includes an extra allowance for the potential changes in the financial market to increase or decrease the value of the options and guarantees before their expiry.

Main assumptions

Discount rate

The risk-free interest rate used for discounting and projecting cash flows in the technical provision calculations is the 'GBP risk-free term structure' as published by the European Insurance and Occupational Pensions Authority (EIOPA).

Mortality and morbidity

To set the best estimate mortality and morbidity assumptions, ZAL management annually investigates its mortality and critical illness experience over the previous four calendar years. Allowance is made for expected future mortality improvements on annuity business and conventional protection business, and for any other factors ZAL considers relevant to future experience. The assumptions are changed to reflect the more recent investigation unless the difference in experience is deemed to be statistically insignificant, in which case the assumptions are left unchanged.

The assumptions are set with reference to relevant industry and reinsurance information - in particular mortality assumptions are set with reference to the standard tables provided by the Continuous Mortality Investigation (CMI) Bureau and a CMI projections model. These tables are based on industry-wide experience and wider population experience. ZAL management sets the percentage assumption based on its own studies.

If lower mortality rates were assumed to apply, the technical provisions would increase in respect of annuity products and decrease in respect of protection products. If lower morbidity rates were assumed to apply, the technical provisions would decrease. The effects on the value of the technical provisions from changes in the assumptions are shown in the 'Indication of the level of uncertainty in the technical provisions' section.

Expenses

ZAL's best estimate expense assumption includes allowance for all expenses associated with servicing its ongoing insurance obligations. This includes:

- Internal servicing and claims costs - both those directly attributable to the policies plus an allocation of overhead costs
- Outsourced administration costs
- Investment management expenses

D. Valuation for solvency purposes *continued*

Per policy expense assumptions are set based on an annual expense analysis.

If lower expenses were assumed to apply, the technical provisions would decrease. The effects on the value of the technical provisions from changes in the assumptions are shown in the 'Indication of the level of uncertainty in the technical provisions' section

Withdrawal rate and lapse rate
ZAL's best estimate withdrawal or lapse rate assumptions are reviewed annually. They are based on the average rates experienced over the previous two calendar years. In setting the rates the experience data is grouped by similar product types to ensure it is sufficiently credible.

If lower withdrawal or lapse rates were assumed to apply, the technical provisions would increase for some policies and decrease for others. Overall, higher withdrawal/ lapse rates would reduce technical provisions as shown in the 'Indication of the level of uncertainty in the technical provisions' section.

Material changes over the year
During 2016 the technical provisions increased as a result of a fall in the discount rate specified by EIOPA, in line with market movements. The only other material assumption change was to morbidity as part of the annual update which led to an increase in technical provision and an increase in reinsurance recoverables, with no overall material impact on own funds.

Risk margin

The risk margin is an addition to the BEL to ensure that the value of the technical provisions is equivalent to the amount that companies would be expected to require in order to take over and meet the insurance obligations. It represents the theoretical compensation for the risk of future experience being worse than that assumed in the BEL and for the cost of holding regulatory capital against this. See section E.2 'Solvency Capital Requirement and Minimum Capital Requirement' for more details on the capital requirements. The risk margin is calculated using the cost of capital approach.

The cost of capital rate is specified by the regulation, and is currently 6%. The risk margin is calculated as the present value of the cost of holding the SCR.

Separate calculations are carried out for each of the two ring-fenced with-profits funds and the remaining fund. The relevant risk types for risk margin are:

- Underwriting risk;
- Counterparty default risk; and
- Operational risk.

Simplifications used in the calculation of the risk margin
ZAL makes use of a simplified method when calculating the SCR for each of the future years that is used to determine the risk margin.

ZAL employs the proxy approach, where each of the relevant risk types within the SCR are projected using their expected run-off pattern. These risks are then aggregated to determine the overall projected SCR for each of the future years.

Indication of the level of uncertainty in the technical provisions

The uncertainty in the technical provisions primarily relates to how actual experience will differ from the best estimate. However, the assumption setting process is robust and well controlled to ensure any limitations are understood and documented.

The following table shows the percentage change in the technical provisions for changes in the key assumptions.

Sensitivity analysis of the technical provisions for life business

	Interest Rate		Expenses	Mortality Rates		Withdrawal Rates	
	+1.00%	-1.00%	+10.00%	+10.00% on assurance only	-10.00% on annuity only	+10.00%	-10.00%
Technical provisions	-2.24%	2.43%	0.23%	0.25%	0.32%	-0.16%	0.16%

Whilst the interest rate curve used in the calculation of technical provisions is not an assumption, ZAL is exposed to the mismatch risks between assets and liabilities. The movement in technical provisions is partly offset by the movement in assets.

Reinsurance is used to mitigate some of the mortality risk and after allowing for reinsurance recoverable the mortality sensitivity changes to 0.05% for +10% on assurances and 0.09% for -10% on annuities, where the change is the percentage change in technical provisions less reinsurance recoverables.

Technical provisions – reconciliation to financial statements

The following table sets out the differences between the valuation of technical provisions under Solvency II and UK GAAP.

Valuation of technical provisions for Solvency II and financial reporting purposes

in £'000	Solvency II	Financial Statements (UK GAAP)	Difference
Insurance with-profits participation	1,718,701	1,841,854	(123,153)
Other life (excluding health and index-linked and unit-linked)	2,789,202	3,652,125	(862,923)
Index-linked and unit-linked	45,271,852	45,563,458	(291,606)
Health insurance (direct business)	274,185	468,625	(194,440)
Health reinsurance (reinsurance accepted)	2,004	1,370	634
Total	**50,055,944**	**51,527,432**	**(1,471,488)**

The UK GAAP reserves are shown in the financial statements as technical provisions for long term business provision and technical provisions for linked liabilities. The table above shows these reserves presented differently by the Solvency II lines of business.

Insurance with-profits participation
The UK GAAP reserves for with-profits business is calculated as the Solvency II BEL plus an adjustment for the policyholders' share of any excess assets over BEL. The risk margin is not explicitly included, but forms part of the excess assets over BEL, most of which is included in UK GAAP reserves through the policyholders' share of this.

Index-linked and unit-linked Insurance, other life Insurance , and health (direct and reinsurance accepted) insurance
The main differences between the UK GAAP reserves and the Solvency II technical provisions for the index-linked and unit-linked insurance, other life insurance and health insurance lines of business are set out below:

- Under UK GAAP the contracts are classified as either insurance or investment contracts. All investment contracts are unit-linked and the reserve held is the unit reserve. Under Solvency II the corresponding BEL allows for expected future cash flows in addition to the unit reserve;
- For insurance contracts the UK GAAP assumptions include a margin for prudence while Solvency II assumptions use best estimate in the BEL with a separate risk margin;
- The UK GAAP reserve calculation uses a flat discount rate, derived from the assets ZAL holds, whilst the Solvency II BEL uses a discount rate specified by EIOPA; and
- Under UK GAAP a minimum reserve of zero is held for each contract whereas negative BELs are included for Solvency II.

D. Valuation for solvency purposes *continued*

Overall the reserves held for UK GAAP are higher than the Solvency II technical provisions reflecting the additional prudence in the UK GAAP reserve calculation. This difference is slightly reduced when considering the deferred acquisition cost asset and deferred fees liability held on the UK GAAP balance sheet, which is an overall net asset of £158m. No corresponding asset is held under Solvency II.

Matching adjustment

ZAL does not apply a matching adjustment to the technical provisions.

Volatility adjustment

ZAL does not apply a volatility adjustment to the technical provisions.

Transitional risk-free interest rate term structure

ZAL does not apply a transitional risk-free interest rate.

Transitional deduction

ZAL does not apply a transitional deduction to the technical provisions.

Recoverables from reinsurance contracts and special purpose vehicles

The reinsurance recoverables in respect of the majority of the reinsurance arrangements in place within ZAL are calculated on an individual policy basis using the same valuation approach and best estimate assumptions that are used to calculate the gross BEL.

ZAL does not make use of special purpose vehicles (SPVs). Consequently, there will be no recoverables from SPVs.

Other material information

Assumptions about future management actions
The cash flow projections used in the calculation of the BEL should reflect the actions that management would reasonably expect to carry out over the duration of the projections, and the time taken to implement those future management actions.

The following assumptions about future management actions have been made within the calculation of the BEL:

Asset mix
For with-profits business, the cash flow projection starts with the actual mix of assets and, at the end of each year, adjusts the holdings in accordance with the current long term investment strategy for the relevant part of the fund.

Bonus rates, future enhancements and market value reductions
Annual and regular bonus rates are assumed to remain unchanged from the valuation date, with final bonus rates adjusted to target a payout of 100% of asset share for each policy grouping, subject to:
- a minimum bonus rate of zero;
- smoothing of maturity payouts in certain market conditions, as set out in ZAL's published Principles and Practices of Financial Management (PPFM) for the with-profits funds; and
- a market value reduction cannot be applied on certain dates chosen in advance by policyholders, for example the maturity date for endowments, or on death.

D.3 Other liabilities

This section sets out the principles of valuation that ZAL has used to calculate other liabilities for solvency reporting.

Other liability valuation methodologies for Solvency II

Contingent liabilities
Valuation is based on the probability-weighted average of future cash flows required to settle the contingent liability over its lifetime, discounted at the relevant risk-free interest rate.

Provisions other than technical provisions
Valuation of provisions is in accordance with IAS 37. IAS 37 is used as a reasonable approximation for fair value as these provisions are materially short term in nature. Key assumptions are noted below.

Remediation and complaints
Estimated redress costs are included in technical provisions. The key assumption is the expected volume of future complaints. Whilst this provision has been based on recent actual experience, uncertainty regarding the ultimate cost remains. This provision relates to the cost of investigating and resolving current and future complaints in excess of the levels assumed in expense loadings within technical provisions. It is expected that the provision will be substantially utilised within the next two years.

Onerous property obligations
The provision takes into account assumptions as to the period the property will remain vacant or, where applicable, the period for which the property expense exceeds rent receivable. The position is regularly reviewed and any changes in circumstances are reflected in the calculation of the provision. It is expected that the provision will be utilised over the period of the leases of one to eleven years.

Deferred tax liabilities
Provision is made for deferred tax liabilities, using the liability method, on all material timing differences including revaluation gains and losses on investments recognised in the profit and loss account. Deferred tax is calculated at the rates at which it is expected that the tax will arise.

The deferred tax liability is primarily in respect of the long term business of the Company, and mainly relates to unrealised gains on investments, deferred expenses and deferred origination fees. Tax losses carried forward are expected to be recovered out of future profits arising in respect of policies inforce, future investment income and gains.

Derivatives
Measured at fair value.

Insurance & intermediaries payables
Measured at fair value.

Reinsurance payables
Measured at fair value.

Payables
Measured at fair value.

Any other liabilities, not elsewhere shown
Under UK GAAP Deferred Origination Fees (DOF) are included in the balance sheet as a liability. Under Solvency II the economic value of the DOF liability is nil, as required by the regulations.

All other liabilities are measured at fair value.

There are no material liabilities arising as a result of lease arrangements.

There are no future management actions that would impact on the above.

D. Valuation for solvency purposes *continued*

No liabilities are deemed to be significantly long term in nature or have significant assumptions or judgments where uncertain future events would need to be reflected in the valuation.

There have been no material changes made to the recognition and valuation basis during the period.

The table below sets out the differences between the valuation of liabilities under Solvency II and UK GAAP:

Valuation of other liabilities for Solvency II and financial reporting purposes

in £'000 **Material classes of other liabilities**	**Solvency II**	**Financial Statements (UK GAAP)**	**Difference**
Provisions other than technical provisions	31,351	31,351	-
Deferred tax liabilities	181,183	206,759	(25,576)
Derivatives	25,475	25,475	–
Insurance & intermediaries payables	301,995	303,506	(1,511)
Reinsurance payables	185,875	185,875	-
Payables (trade, not insurance)	102,275	42,126	60,149
Any other liabilities, not elsewhere shown	72,603	275,616	(203,013)
Total liabilities	**900,757**	**1,070,708**	**(169,951)**

The UK GAAP figures above use the Solvency II balance sheet presentation. For certain balance sheet headings the reported figures above may differ from the presentation in the financial statements.

Differences between Solvency II valuation and UK GAAP (FRS 101 'Reduced disclosure framework')

The main valuation differences between Solvency II and UK GAAP are explained below:

Payables (trade, not insurance)
This reflects the differences in the presentation of the 'Participations' offset by the presentation of the 'Receivables (trade, not insurance)' as noted in 'The differences between SII Valuation and UK GAAP' section in D.1 'Assets' above.

ZAL has some ring-fenced funds, and therefore at the total Solvency II balance sheet level certain balances between these ring-fenced funds and the remaining funds are presented gross. However for the UK GAAP presentation, there is no requirement to show ring-fenced funds, therefore where there is a right of offset these balances are shown net. Therefore, there is an offsetting difference in the 'Receivables (trade, not insurance)' in D.1 'Assets' above.

Any other liabilities, not elsewhere shown
Deferred origination fees are valued at nil for Solvency II reporting.

There have been no material changes made to the estimations, recognition and valuation basis during the period.

Alternative methods for valuation

There are no alternative methods used - the 'Asset valuation methodologies for Solvency II' section under D.1 'Assets' outlines the standard methods currently used.

Guarantees and contingent liabilities

The Company has indemnified Zurich Advice Network Limited (ZAN) from any liability, arising from any claim or complaint relating to any products previously marketed, advised upon or sold (whether directly or indirectly) by ZAN or its predecessor or any of their advisers at any time from 5 June 1997.

The fair value is considered negligible as the Company assumes any liability in respect of its own products and therefore the probability of economic transfer being required as a result of this indemnity is considered to be remote.

The Company has indemnified Zurich Independent Wealth Management Limited (ZIWM) against any liability arising from any claim or complaint relating to any products previously marketed, advised upon or sold by ZIWM or any adviser connected to ZIWM.

The Company has provided a deed of indemnity to a group company, Zurich Legacy Solutions Services (UK) Limited, in relation to the assignment to the Company of the lease for premises at The Grange, Bishops Cleeve, Cheltenham. The term of the lease is for twenty years from and including 19 December 2001. The maximum liability arising under this deed of indemnity per annum is estimated at £3m.

The Company has indemnified Eagle Star (Malta) Limited (ESML) from any claim arising from negligence which would otherwise fail to be indemnified by the required Professional Indemnity insurance policy. The value of the indemnity will be up to £750,000 for each and every claim or series of claims arising out of the same occurrence; for the purposes of this undertaking "a series of claims arising out of the same occurrence" shall not be deemed to constitute one claim.

For the above indemnities, the directors do not consider it necessary to provide for any amounts in respect of these indemnities.

D.4 Alternative methods for valuation

Alternative methods of valuation have been reported in sections D.1 'Assets' under the mark to model and other valuation methods sections, D.2 'Technical provisions' and D.3 'Other liabilities'. There are no other alternative methods to report other than those already reported in these sections.

D.5 Any other information

There is no other material information to report.

E. Capital management

E.1 Own funds

Objectives of capital management in the context of the Zurich Group

The Zurich Group's capital management strategy is to maximise long term shareholder value by optimising capital allocation while managing the balance sheet at a level consistent with an 'AA' credit rating and in accordance with regulatory, solvency and rating agency requirements. In particular, the Zurich Group endeavors to manage its capital so that it and all of its regulated entities are adequately capitalised in compliance with the relevant regulatory capital adequacy requirements. The Group seeks to minimise constraints to capital fungibility by pooling risk, capital and liquidity centrally as much as possible.

ZAL's capital management and business planning framework

ZAL endeavours to manage its capital so that it meets regulatory Minimum Capital Requirements at all times. In addition, ZAL's capital management policy is consistent with the Zurich Group's capital management policy as set out above. The key elements of ZAL's capital management and business planning framework are set out below.

- The ZAL Board is responsible for ensuring that regulatory solvency is managed in line with regulatory and business requirements. The CFO is responsible for managing regulatory solvency within a range in order to avoid unnecessarily frequent capital movements to and from its shareholder. This range reflects legal, regulatory and business considerations. ZAL's solvency ratio is currently above the upper boundary and it is anticipated that ZAL will take actions over time to manage the ratio to within the target range, such as remitting excess capital to the shareholder;
- The lower solvency boundary of this range reflects a safety buffer above the minimum regulatory requirements. In the case of a deficiency against the lower solvency boundary, the CFO proposes corrective actions to the ZAL Board and Group Treasury and Capital Management. Corrective actions include requesting capital support from the shareholder if deemed appropriate;
- The upper boundary includes an adequate buffer in order to absorb solvency volatility under normal economic conditions. In case of excess capital above the upper solvency boundary, the CFO proposes to the ZAL Board and Group Treasury and Capital Management to remit the excess to the shareholder as soon as permissible from a legal, regulatory and business perspective;
- Regulatory solvency is monitored on a regular basis and reported to the regulator as requested; and
- ZAL operates a three year business planning period.

Structure of the own funds
The own funds are derived from the excess of assets over liabilities shown on the balance sheet, see sections D.1 'Assets', D.2 'Technical provisions' and D.3 'Other liabilities' for valuations of those items. There is a deduction for restricted own funds items in respect of ring-fenced funds as required by Article 70 1 (e) (i) of The Delegated Level 2 Regulations.

All own funds items are in tier one with the exception of the deferred tax asset which is classed as tier three as required by Article 76 (a) (iii) of The Delegated Level 2 Regulations. All own funds are available:

i) to meet the Solvency Capital Requirement (SCR).
ii) to meet the Minimum Capital Requirement (MCR) with the exception of the tier three own funds.

The composition of own funds is set out in the table below:

Composition of own funds

in £'000	31 Dec 2016
Assets	52,976,305
Other liabilities	(900,757)
Technical provisions	(50,055,944)
Excess of assets over liabilities	**2,019,604**
Adjustment for restricted own funds items in respect of ring-fenced funds	(25,880)
Total basic own funds after deductions	**1,993,724**
Total available and eligible own funds to meet the SCR	**1,993,724**
SCR	(1,155,390)
Excess available funds for SCR over SCR	**838,334**
Ratio of eligible own funds to SCR	**173%**
Total available and eligible own funds to meet the MCR	**1,993,098**
MCR	(292,356)
Excess available funds for MCR over MCR	**1,700,742**
Ratio of eligible own funds to MCR	**682%**

It is anticipated that ZAL will take actions over time to manage the ratio to within its target range, such as remitting excess capital to the shareholder.

The 'adjustment for restricted own funds items in respect of ring-fenced funds' above removes from own funds the contribution from each with-profits fund that is due to policyholders after allowing for the notional SCR of the fund.

The own funds split by tier are set out in the table below:

Segmentation of own funds by tier of capital

in £'000

Own funds	Tier 1	Tier 2	Tier 3	Total
Covering the SCR	1,993,098	–	626	1,993,724
Covering the MCR	1,993,098	–	–	1,993,098

Reconciliation to financial statements

The difference between the Solvency II 'Excess of assets over liabilities' and the 'Financial statements equity including fund for future appropriations' is explained in the table below.

Differences in excess of assets over liabilities for Solvency II and equity financial reporting purposes

in £'000	
Solvency II excess of assets over liabilities	2,019,604
Financial statements equity including fund for future appropriations	1,205,982
Difference	813,622

E. Capital management *continued*

The difference above is explained by:

Explanation of difference	in £'000
Difference in total assets (see section D.1)	(787,820)
Difference in gross technical provisions (see section D.2)	1,471,488
Difference in other liabilities (see section D.3)	169,951
Fund for future appropriations	(39,997)
Difference explained	813,622

- The fund for future appropriations represents the amounts in the participating ring-fenced funds for which the allocation to participating policyholders and the shareholder has not been determined at the balance sheet date.

Own funds consists of the following items:

Composition and description of own funds

In £'000

Basic Own Funds Items	Amount	Description
Ordinary share capital (net of own shares)	236,132	Relates to allotted, issued and fully paid ordinary share capital and capital contributions. The share capital and the capital contributions are not subordinated and have no restricted duration.
Surplus funds	197,934	Surplus funds that are not considered as insurance and reinsurance liabilities as noted in Article 69 1 (iv) of The Delegated Level 2 Regulations.
Reconciliation reserve	1,559,032	Reconciliation reserve as noted in Article 70 of The Delegated Level 2 Regulations. The Reconciliation reserve consists of the excess of assets over liabilities as reported in the Balance Sheet less the Ring-fenced Fund Restriction less Basic Own Funds items. The restriction is that which is applied to the with-profits funds, removing all excess applicable to policyholders. The Basic Own Funds is made up of Surplus, Deferred Tax assets (as reported in the Balance Sheet) and the Ordinary Share Capital held by ZAL.
Total Tier 1 Capital	**1,993,098**	
An amount equal to the value of net deferred tax assets	626	An amount equal to the value of net deferred tax assets as noted in Article 76 of The Delegated Level 2 Regulations.
Total Tier 3 Capital	**626**	
Total Basic Own Funds	**1,993,724**	

There were no significant changes to the material classes in own funds during the year.

E.2 Solvency Capital Requirement and Minimum Capital Requirement

SCR and MCR

The SCR and MCR both represent capital requirements that must be held in addition to the technical provisions. These have both been calculated in accordance with Directive 2009/138/EC and Commission Delegated Regulation (EU) 2015/35 (amended), with the SCR being calculated using the standard formula approach. Both these values are subject to final supervisory assessment.

The SCR is the capital required to ensure that ZAL will be able to meet its obligations over the next 12 months with a probability of at least 99.5%. In addition to the SCR capital a MCR is calculated which represents the threshold below which the regulator would intervene. The MCR is intended to correspond to an 85% probability of adequacy over a one year period and is bounded between 25% and 45% of the SCR.

The following table shows the total SCR and MCR at 31 December 2016.

SCR and MCR calculated using the Standard Formula

in £'000

	31 Dec 2016
SCR	1,155,390
MCR	292,356

SCR split by risk module or category

The SCR is held to cover the relevant risks described in section C, and can be broken down by the different types of risk as shown in the following table. The capital requirement is initially calculated for each risk in isolation with an allowance then made for any diversification benefits between the different risks. Operational risk is not assumed to diversify with other risk types. Further adjustments are made for the loss absorbing capacity of deferred tax and technical provisions, and for any capital add-on to determine the SCR.

SCR charges by risk module or risk category

in £'000

	31 Dec 2016
Market risk	363,431
Counterparty default risk	261,003
Life underwriting risk	474,972
Health underwriting risk	52,462
Total undiversified risk	**1,151,868**
Diversification effect	(343,712)
Basic Solvency Capital Requirement	**808,156**
Adjustment for the loss absorbing capacity of deferred taxes	(24,036)
Adjustment for the loss absorbing capacity of technical provisions	(63,082)
Operational risk	90,711
Adjustment due to ring fenced funds	23,641
Capital add-on (pension scheme risk)	320,000
SCR	**1,155,390**

The table above shows the adjustment due to ring-fenced funds explicitly. The QRT S.25.01.21 in the appendix has implicitly allowed for the same adjustment in each risk type and diversification.

Market risk covers interest rate, equity, property, spread, concentration and currency risks which are described further in section C.2. 'Market risk'

Life underwriting risk covers mortality, longevity, disability/morbidity, expense, lapse and life catastrophe risks. Health underwriting risk covers mortality, longevity, disability/morbidity, expense and lapse risks for health business and health catastrophe risks. These are described further in section C.1. 'Underwriting risk'

A capital add-on is held in respect of the pension scheme risk which is not covered by the standard formula calculation. ZAL is currently developing a partial internal model to model this risk, which will replace the capital add-on in due course, subject to regulatory approval. This is described further in section C.6 'Other material risks',

Material changes over the year

During 2016 the SCR reduced slightly. The increase in SCR from higher assets under management, mainly due to market movements, was more than offset by a reduction in credit risk following a reassessment of the risk on the fund reinsurance.

E. Capital management *continued*

Inputs used to calculate the MCR

The following table shows the inputs used to calculate the MCR.

Inputs used to calculate the MCR

in £'000	31 Dec 2016
Linear MCR	292,356
SCR	1,155,390
MCR Cap (45% of SCR)	519,926
MCR Floor (25% of SCR)	288,848
MCR	292,356

The MCR is calculated as the linear MCR subject to a floor of 25% of the SCR and a cap of 45% of the SCR. The linear MCR is a linear function of a set of the following variables: ZAL's technical provisions (net of reinsurance), written premiums, capital-at-risk and administrative expenses. values for which can be found on QRT S.28 in the appendix.

Any other information

Use of simplified calculations in the SCR
The following simplifications have been used in the SCR calculation in the counterparty default risk module:

- The risk-mitigating impact of reinsurance has been calculated for each reinsurance arrangement using the simplification as set out in Article 107 of the Delegated Regulation. This means the total risk mitigating impact from all reinsurance is allocated to individual reinsurers in proportion to the reinsurance recoverable for that reinsurer.
- Where collateral is provided under a reinsurance treaty, the risk adjusted value of this has been taken as 85% of the asset value held at end 2016, in accordance with Article 112 of the Delegated Regulation.

Use of undertaking specific parameters
- No undertaking specific parameters have been used.

Throughout 2016, ZAL was compliant with the applicable Solvency Capital Requirements.

E.3 Use of the duration-based equity risk sub-module in the calculation of the Solvency Capital Requirement

ZAL has not opted to use the duration-based equity risk sub-module of the Solvency II regulations.

E.4 Differences between the standard formula and any internal model used

ZAL applies the Standard formula model and does not use an internal model to calculate the SCR.

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

ZAL has been compliant with both the Minimum Capital Requirement and Solvency Capital Requirement during 2016.

E.6 Any other information

There is no other information to report here.

Appendix 1 Subsidiary Undertakings

Appendix 1: Subsidiary undertakings

Company	Class of Share Capital	Percentage of nominal value held by the Company
50 Brook Green Management Company Limited	Ordinary	80
Access Franchise Management Limited	Deferred and Ordinary	100
Albert Road 1 UK Limited	Ordinary	100
Albert Road 2 UK Limited	Ordinary	100
Eagle Star (Leasing) Limited	Ordinary	100
Eagle Star (Malta) Limited	Ordinary	99.996
Eagle Star Computer Services Limited	Ordinary	100
Eagle Star Estates Limited	Ordinary	100
Eagle Star Farms Limited	Ordinary	100
Eagle Star Forests Limited	Ordinary	100
Eagle Star Holding Company of Ireland Unlimited Company	Ordinary	100
Eagle Star Loans Limited	Ordinary	100
Eagle Star Mortgages Limited	Ordinary	100
ES (Leeds) Nominee Limited	Ordinary	100
ES (Walsall) Nominee Limited	Ordinary	100
ES Camberley Nominee 1 Limited	Ordinary	100
ES Camberley Nominee 2 Limited	Ordinary	100
ES Cannock Nominee 1 Limited	Ordinary	100
ES Cannock Nominee 2 Limited	Ordinary	100
ES Coventry Nominee 1 Limited	Ordinary	100
ES Coventry Nominee 2 Limited	Ordinary	100
ES Dudley Nominee 1 Limited	Ordinary	100
ES Dudley Nominee 2 Limited	Ordinary	100
ES Hoddesdon Nominee 1 Limited	Ordinary	100
ES Hoddesdon Nominee 2 Limited	Ordinary	100
ES Plympton Nominee 1 Limited	Ordinary	100
ES Plympton Nominee 2 Limited	Ordinary	100
ES Ramsgate Nominee 1 Limited	Ordinary	100
ES Ramsgate Nominee 2 Limited	Ordinary	100
Graphene Capital Partners Limited	Ordinary	100
Grovewood Engineering Limited	Ordinary	100
Hawkcentral Limited	Ordinary	100
Ipsley Street 1 UK Limited	Ordinary	100
Ipsley Street 2 UK Limited	Ordinary	100
Kennet Road 1 UK Limited	Ordinary	100
Kennet Road 2 UK Limited	Ordinary	100
Logobrook Limited	Ordinary	100
Mentionland Limited	Ordinary	100
Meritclass Investments Limited	Ordinary	100
Nearheath Limited	Ordinary	100
Plot 8B Buckingway Management Limited	Ordinary	100
Zurich Assurance (2004) Limited	Ordinary	100
Zurich Group Pension Services (UK) Limited	Ordinary	100
Zurich International Solutions Limited	Ordinary	100
Zurich Pension Trustees Limited	Ordinary	100

The Companies listed above are incorporated in England and Wales with the exception of :-Eagle Star Holding Company of Ireland Unlimited Company which is incorporated in the Republic of Ireland and Eagle Star(Malta) Limited which is Incorporated in Malta.

Significant holdings in undertakings other than subsidiary undertakings

Company	Class of Share Capital	Percentage of nominal value held by the Company
Cambridge Research Park Management Co Limited	Ordinary	23
Dukes Green Property Management Limited	Ordinary	46
Interface Solihull Management Limited	Ordinary	29
Northampton Business Park Management Limited	Ordinary	23
Plot 6 Buckingway Management Limited	Ordinary	25
Rabone Park Management Company Limited	Ordinary	43
The Parklands (Birmingham) Management Company Limited	Ordinary	30.56
Wrexham Services Limited	Ordinary	33.30

The companies listed above are incorporated in England and Wales.

Appendix 2 Quantitative Reporting Templates

S.02.01.02

Balance Sheet, Assets

in GBP thousands, as of December 31

		Solvency II value
		C0010
Assets		
Intangible assets	R0030	–
Deferred tax assets	R0040	626
Pension benefit surplus	R0050	–
Property, plant & equipment held for own use	R0060	2,396
Investments (other than assets held for index-linked and unit-linked contracts)	R0070	3,895,828
Property (other than for own use)	R0080	43,027
Holdings in related undertakings, including participations	R0090	(32,479)
Equities	R0100	202,059
Equities – listed	R0110	198,098
Equities – unlisted	R0120	3,961
Bonds	R0130	3,504,578
Government Bonds	R0140	1,812,577
Corporate Bonds	R0150	1,513,271
Structured notes	R0160	13,483
Collateralised securities	R0170	165,247
Collective Investments Undertakings	R0180	101,833
Derivatives	R0190	16,138
Deposits other than cash equivalents	R0200	60,672
Other investments	R0210	–
Assets held for index-linked and unit-linked contracts	R0220	32,168,371
Loans and mortgages	R0230	62,280
Loans on policies	R0240	60,248
Loans and mortgages to individuals	R0250	2,033
Other loans and mortgages	R0260	–
Reinsurance recoverables from:	R0270	16,314,425
Non-life and health similar to non-life	R0280	–
Non-life excluding health	R0290	–
Health similar to non-life	R0300	–
Life and health similar to life, excluding health and index-linked and unit-linked	R0310	2,449,370
Health similar to life	R0320	103,313
Life excluding health and index-linked and unit-linked	R0330	2,346,057
Life index-linked and unit-linked	R0340	13,865,054
Deposits to cedants	R0350	–
Insurance and intermediaries receivables	R0360	83,700
Reinsurance receivables	R0370	180,789
Receivables (trade, not insurance)	R0380	62,153
Own shares (held directly)	R0390	–
Amounts due in respect of own fund items or initial fund called up but not yet paid in	R0400	–
Cash and cash equivalents	R0410	184,924
Any other assets, not elsewhere shown	R0420	20,813
Total assets	**R0500**	**52,976,305**

S.02.01.02

Balance Sheet, Liabilities

in GBP thousands, as of December 31

		Solvency II value
		C0010
Liabilities		
Technical provisions – non-life	R0510	–
Technical provisions – non-life (excluding health)	R0520	–
TP calculated as a whole	R0530	–
Best Estimate	R0540	–
Risk margin	R0550	–
Technical provisions – health (similar to non-life)	R0560	–
TP calculated as a whole	R0570	–
Best Estimate	R0580	–
Risk margin	R0590	–
Technical provisions – life (excluding index-linked and unit-linked)	R0600	4,784,092
Technical provisions – health (similar to life)	R0610	276,189
TP calculated as a whole	R0620	–
Best Estimate	R0630	228,582
Risk margin	R0640	47,607
Technical provisions – life (excluding health and index-linked and unit-linked)	R0650	4,507,903
TP calculated as a whole	R0660	–
Best Estimate	R0670	4,415,158
Risk margin	R0680	92,745
Technical provisions – index-linked and unit-linked	R0690	45,271,852
TP calculated as a whole	R0700	–
Best Estimate	R0710	44,962,793
Risk margin	R0720	309,059
Contingent liabilities	R0740	–
Provisions other than technical provisions	R0750	31,351
Pension benefit obligations	R0760	–
Deposits from reinsurers	R0770	–
Deferred tax liabilities	R0780	181,183
Derivatives	R0790	25,475
Debts owed to credit institutions	R0800	–
Financial liabilities other than debts owed to credit institutions	R0810	–
Insurance & intermediaries payables	R0820	301,995
Reinsurance payables	R0830	185,875
Payables (trade, not insurance)	R0840	102,275
Subordinated liabilities	R0850	–
Subordinated liabilities not in BOF	R0860	–
Subordinated liabilities in BOF	R0870	–
Any other liabilities, not elsewhere shown	R0880	72,603
Total liabilities	**R0900**	**50,956,701**
Excess of assets over liabilities	**R1000**	**2,019,604**

Appendix 2 Quantitative Reporting Templates *continued*

S.05.01.02

Premiums, claims and expenses by line of business, Life

in GBP thousands, as of December 31

Premiums written	
Gross	R1410
Reinsurers' share	R1420
Net	R1500
Premiums earned	
Gross	R1510
Reinsurers' share	R1520
Net	R1600
Claims incurred	
Gross	R1610
Reinsurers' share	R1620
Net	R1700
Changes in other technical provisions	
Gross	R1710
Reinsurers' share	R1720
Net	R1800
Expenses incurred	**R1900**
Other expenses	**R2500**
Total expenses	**R2600**

	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
	196,223	16,411	208,928	448,686	–	–	2,609	–	872,858
	81,109	444	40,415	356,902	–	–	–	–	478,870
	115,115	15,967	168,512	91,784	–	–	2,609	–	393,987
	196,223	16,411	208,928	448,686	–	–	2,609	–	872,858
	81,109	444	40,415	356,902	–	–	–	–	478,870
	115,115	15,967	168,512	91,784	–	–	2,609	–	393,987
	100,172	246,547	1,635,834	364,316	–	–	1,583	–	2,348,452
	34,477	325	43,421	310,249	–	–	–	–	388,472
	65,695	246,222	1,592,413	54,067	–	–	1,583	–	1,959,980
	(106,902)	22,953	(4,409,851)	(600,708)	–	–	(115)	–	(5,094,623)
	(87,008)	–	(349)	(501,156)	–	–	–	–	(588,512)
	(19,895)	22,953	(4,409,502)	(99,552)	–	–	(115)	–	(4,506,111)
	49,200	**10,378**	**289,835**	**111,337**	**–**	**–**	**10**	**–**	**460,761**
									4,055
	–	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**464,816**

Appendix 2 Quantitative Reporting Templates *continued*

S.05.02.01

Premiums, claims and expenses by country, Life

in GBP thousands, as of December 31

		R1400
Premiums written		
Gross	R1410	
Reinsurers' share	R1420	
Net	R1500	
Premiums earned		
Gross	R1510	
Reinsurers' share	R1520	
Net	R1600	
Claims incurred		
Gross	R1610	
Reinsurers' share	R1620	
Net	R1700	
Changes in other technical provisions		
Gross	R1710	
Reinsurers' share	R1720	
Net	R1800	
Expenses incurred	**R1900**	
Other expenses	**R2500**	
Total expenses	**R2600**	

S.12.01.02

Life and Health SLT Technical Provisions

in GBP thousands, as of December 31

Technical provisions calculated as a whole	**R0010**
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	R0020
Technical provisions calculated as a sum of BE and RM	
Best Estimate	
Gross Best Estimate	**R0030**
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	R0080
Best estimate minus recoverables from reinsurance/SPV and Finite Re – total	R0090
Risk Margin	**R0100**
Amount of the transitional on Technical Provisions	
Technical Provisions calculated as a whole	R0110
Best estimate	R0120
Risk margin	R0130
Technical provisions – total	**R0200**

Home Country		Top 5 countries (by amount of gross premiums written) – life obligations				Total Top 5 and home country
C0150	C0160	C0170	C0180	C0190	C0200	C0210
	HK	MT	IM			
C0220	C0230	C0240	C0250	C0260	C0270	C0280
842,026	30,157	674	–			872,858
476,942	1,928	–	–			478,870
365,084	28,228	674	–			393,987
842,026	30,157	674	–			872,858
476,942	1,928	–	–			478,870
365,084	28,228	674	–			393,987
2,300,534	38,687	6,588	2,643			2,348,452
385,646	885	–	1,940			388,472
1,914,888	37,802	6,588	702			1,959,980
(5,000,460)	(93,075)	(541)	(546)			(5,094,623)
(588,144)	–	–	(368)			(588,512)
(4,412,316)	(93,075)	(541)	(178)			(4,506,111)
453,977	**6,436**	**224**	**124**			**460,761**
						4,055
	–	**–**	**–**			**464,816**

	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		
Insurance with profit participation		Contracts without options and guarantees	Contracts with options or guarantees		Contracts without options and guarantees	Contracts with options or guarantees		Accepted reinsurance	Total (Life other than health insurance, incl. Unit-Linked)
C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0150
–	–			–			–	–	–
–	–			–			–	–	–
1,644,981		–	44,962,793		–	2,770,177	–	–	49,377,951
(548)		–	13,865,054		–	2,346,605	–	–	16,211,111
1,645,529		–	31,097,739		–	423,572	–	–	33,166,840
73,721	309,059			19,024			–	–	401,804
–	–			–			–	–	–
–		–	–		–	–	–	–	–
–	–			–			–	–	–
1,718,701	**45,271,852**	**–**	**–**	**2,789,201**	**–**	**–**	**–**	**–**	**49,779,755**

Appendix 2 Quantitative Reporting Templates *continued*

S.12.01.02

Life and Health SLT Technical Provisions

in GBP thousands, as of December 31

Technical provisions calculated as a whole
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole
Technical provisions calculated as a sum of BE and RM
Best Estimate
Gross Best Estimate
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default
Best estimate minus recoverables from reinsurance/SPV and Finite Re – total
Risk Margin
Amount of the transitional on Technical Provisions
Technical Provisions calculated as a whole
Best estimate
Risk margin
Technical provisions – total

	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			
	C0160	C0170	C0180	C0190	C0200	C0210
R0010	–			–	–	–
R0020	–			–	–	–
R0030		–	226,578	–	2,004	228,582
R0080		–	103,313	–	–	103,313
R0090		–	123,265	–	2,004	125,269
R0100	47,607			–	–	47,607
R0110	–			–	–	–
R0120		–	–	–	–	–
R0130	–			–	–	–
R0200	274,185	–	–	–	2,004	276,189

Appendix 2 Quantitative Reporting Templates *continued*

S.23.01.01

Own funds

in GBP thousands, as of December 31		Total	Tier 1 – unrestricted	Tier 1 – restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation (EU) 2015/35						
Ordinary share capital (gross of own shares)	R0010	236,132	236,132		–	
Share premium account related to ordinary share capital	R0030	–	–		–	
Iinitial funds, members' contributions or the equivalent basic own – fund item for mutual and mutual-type undertakings	R0040	–	–		–	
Subordinated mutual member accounts	R0050	–		–	–	–
Surplus funds	R0070	197,934	197,934			
Preference shares	R0090	–		–	–	–
Share premium account related to preference shares	R0110	–		–	–	–
Reconciliation reserve	R0130	1,559,032	1,559,032			
Subordinated liabilities	R0140	–		–	–	–
An amount equal to the value of net deferred tax assets	R0160	626				626
Other own fund items approved by the supervisory authority as basic own funds not specified above	R0180	–	–	–	–	–
Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds						
Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds	R0220	–	–	–	–	–
Deductions						
Deductions for participations in financial and credit institutions	R0230	–	–	–	–	–
Total basic own funds after deductions	**R0290**	**1,993,724**	**1,993,098**	**–**	**–**	**626**
Ancillary own funds						
Unpaid and uncalled ordinary share capital callable on demand	R0300	–			–	
Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual – type undertakings, callable on demand	R0310	–			–	
Unpaid and uncalled preference shares callable on demand	R0320	–			–	–
A legally binding commitment to subscribe and pay for subordinated liabilities on demand	R0330	–			–	–
Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	R0340	–			–	
Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	R0350	–			–	–
Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	R0360	–			–	
Supplementary members calls – other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	R0370	–			–	–
Other ancillary own funds	R0390	–			–	–
Total ancillary own funds	**R0400**	**–**	**–**	**–**	**–**	**–**

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Own funds

in GBP thousands, as of December 31

		Total	Tier 1 – unrestricted	Tier 1 – restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
Available and eligible own funds						
Total available own funds to meet the SCR	R0500	1,993,724	1,993,098	–	–	626
Total available own funds to meet the MCR	R0510	1,993,098	1,993,098	–	–	
Total eligible own funds to meet the SCR	R0540	1,993,724	1,993,098	–	–	626
Total eligible own funds to meet the MCR	R0550	1,993,098	1,993,098	–	–	
SCR	**R0580**	**1,155,390**				
MCR	**R0600**	**292,356**				
Ratio of Eligible own funds to SCR	**R0620**	**173%**				
Ratio of Eligible own funds to MCR	**R0640**	**682%**				

		C0060
Reconciliation reserve		
Excess of assets over liabilities	R0700	2,019,604
Own shares (held directly and indirectly)	R0710	–
Foreseeable dividends, distributions and charges	R0720	–
Other basic own fund items	R0730	434,692
Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	R0740	25,880
Reconciliation reserve	**R0760**	**1,559,032**
Expected profits		
Expected profits included in future premiums (EPIFP) – Life business	R0770	285,125
Expected profits included in future premiums (EPIFP) – Non-life business	R0780	–
Total Expected profits included in future premiums (EPIFP)	**R0790**	**285,125**

Appendix 2 Quantitative Reporting Templates *continued*

S.25.01.21

Solvency Capital Requirement – for undertakings on Standard Formula

in GBP thousands, as of December 31		Gross Solvency Capital Requirement	USP	Simplifications
		C0110	C0090	C0100
Market risk	R0010	372,596		No
Counterparty default risk	R0020	269,114		
Life underwriting risk	R0030	489,675	No	No
Health underwriting risk	R0040	54,092	No	No
Non-life underwriting risk	R0050	–	No	No
Diversification	R0060	(353,679)		
Intangible asset risk	R0070	–		
Basic Solvency Capital Requirement	**R0100**	**831,798**		

		C0100
Calculation of Solvency Capital Requirement		
Operational risk	R0130	90,711
Loss-absorbing capacity of technical provisions	R0140	(63,082)
Loss-absorbing capacity of deferred taxes	R0150	(24,036)
Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	R0160	–
Solvency Capital Requirement excluding capital add-on	**R0200**	**835,390**
Capital add-on already set	R0210	320,000
Solvency Capital Requirement	**R0220**	**1,155,390**
Other information on SCR		
Capital requirement for duration-based equity risk sub-module	R0400	–
Total amount of Notional Solvency Capital Requirement for remaining part	R0410	737,067
Total amount of Notional Solvency Capital Requirements for ring fenced funds	R0420	98,323
Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	R0430	–
Diversification effects due to RFF nSCR aggregation for article 304	R0440	–

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

in GBP thousands, as of December 31		C0040	
MCR(L) Result	R0200	292,356	

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
		C0050	C0060
Obligations with profit participation – guaranteed benefits	R0210	1,448,442	
Obligations with profit participation – future discretionary benefits	R0220	197,086	
Index-linked and unit-linked insurance obligations	R0230	31,097,739	
Other life (re)insurance and health (re)insurance obligations	R0240	548,841	
Total capital at risk for all life (re)insurance obligations	R0250		28,289,054

		C0070
Linear MCR	R0300	292,356
SCR	R0310	1,155,390
MCR cap	R0320	519,925
MCR floor	R0330	288,847
Combined MCR	R0340	292,356
Absolute floor of the MCR	R0350	3,164

		C0070
Minimum Capital Requirement	**R0400**	**292,356**

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