Chesnara

Annual Report & Accounts
2013

Cautionary statement

This document may contain forward-looking statements with respect to certain of the plans and current expectations relating to the future financial condition, business performance and results of Chesnara plc. By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the control of Chesnara plc including, amongst other things, UK domestic, Swedish domestic and global economic and business conditions, market-related risks such as fluctuations in interest rates, currency exchange rates, inflation, deflation, the impact of competition, changes in customer preferences, delays in implementing proposals, the timing, impact and other uncertainties of future acquisitions or other combinations within relevant industries, the policies and actions of regulatory authorities, the impact of tax or other legislation and other regulations in the jurisdictions in which Chesnara plc and its subsidiaries operate. As a result, Chesnara plc's actual future condition, business performance and results may differ materially from the plans, goals and expectations expressed or implied in these forward-looking statements.

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NOTE ON TERMINOLOGY

As explained in Note 9 to the IFRS financial statements, the principal reporting segments of the Group are:

CA	which comprises the original business of Countrywide Assured plc, the Group's original UK operating subsidiary, and of City of Westminster Assurance Company Limited, which was acquired by the Group in 2005 and the long-term business of which was transferred to Countrywide Assured plc during 2006;
S&P	which was acquired on 20 December 2010. This business was transferred from Save & Prosper Insurance Limited and Save & Prosper Pensions Limited to Countrywide Assured plc on 31 December 2011 under the provisions of Part VII of the Financial Services and Markets Act 2000;
PL	which was purchased on 28 November 2013 from Direct Line Insurance Group plc. On acquisition the company was called Direct Line Life Insurance Company, and was subsequently renamed Protection Life Company Limited. PL is included within the Group's UK business; and
Movestic	which was purchased on 23 July 2009 and comprises the Group's Swedish business, Movestic Livförsäkring AB and its subsidiary and associated companies.

In this Report & Accounts:

i. The **CA**, **S&P** and **PL** segments may also be collectively referred to as the 'UK Business';

ii. The **Movestic** segment may also be referred to as the 'Swedish Business';

iii. '**CA plc**' refers to the legal entity Countrywide Assured plc, which includes the long-term business of **CA**, **CWA** and **S&P**;

iv. '**CWA**' refers to City of Westminster Assurance Company Limited or to its long-term business funds transferred to Countrywide Assured plc;

v. '**S&P**' may also refer collectively to Save & Prosper Insurance Limited and Save & Prosper Pensions Limited, as the context implies. Where it is necessary to distinguish reference to Save & Prosper Insurance Limited and Save & Prosper Pensions Limited, or to the businesses subsisting in those companies prior to the transfer referred to above, they are designated '**SPI**' and '**SPP**' respectively;

vi. '**PL**' refers to Protection Life Company Limited (previously Direct Line Life Insurance Company Limited), which was purchased on 28 November 2013; and

vii. '**Movestic**' may also refer to Movestic Livförsäkring AB, as the context implies.

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OVERVIEW

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AN INTRODUCTION

Chesnara plc is primarily a Life and Pensions closed book consolidator. It currently has books of business in the UK and Sweden. The UK business is predominantly closed to new business whereas our Swedish subsidiary continues to run a profitable new business operation.

Chesnara is a responsible and profitable company engaged in the management of Life and Pension policies in the UK and Sweden. Our focus is:

- Commitment to the core business of closed UK life and pensions book management.
- Further acquisitions where they meet stringent assessment criteria.
- Value enhancement through the writing of profitable new business in Sweden.
- Continued delivery of competitive returns to shareholders and policyholders.

Who we are

Chesnara plc, formed in 2004, is listed on the London Stock Exchange. The Group initially consisted of Countrywide Assured, a closed Life and Pensions book demerged from Countrywide plc, a large estate agency group. Since incorporation the Group has grown through the acquisition of three predominantly closed UK businesses, CWA, S&P and PL plus Movestic, an open Swedish Life and Pensions business.

What we do

- We administer c.870,000 Life and Pension policies (c.420,000 in the UK and c.450,000 in Sweden).

c.870,000
Life and Pension policies.

- We manage £4.7 billion of funds (£3.0 billion in the UK and £1.7 billion in Sweden).

£4.7bn
of total assets under management.

- We operate to high regulatory standards and ensure we offer efficient service levels and competitive returns to policyholders.
- We provide value to shareholders primarily by way of an established and attractive dividend strategy but also by value enhancement through acquisitions and the writing of profitable new business in Sweden.

How we operate

- We maintain a small professional corporate governance team responsible for ensuring regulatory best practice, risk and capital management, and oversight of both our Swedish subsidiary and our predominantly outsourced UK business.
- We maintain a robust regulatory, compliance and risk management regime.
- The governance team has significant experience and a proven track record in acquiring and successfully integrating Life and Pension businesses. The team engages professional partners and advisors to support the acquisition model, as required.
- Acquisitions are funded by a combination of cash, debt and equity as appropriate. We have tried and tested support from debt providers and from our established and supportive shareholder base.
- We maintain robust solvency levels.

How we create value

Policyholder
Effective customer service operations together with competitive fund performance, whilst always adopting exacting standards with regard to all regulatory matters ensures policyholders receive good returns in line with policy, industry and market expectations.

Shareholder
Efficient management of the policy base and good capital management practices means that surpluses emerge from the in-force books of business. These surpluses enable dividend transfers to be made from the subsidiaries to Chesnara, which fund the attractive dividend strategy.

In addition, growth from both the proven acquisition model and from writing profitable new business in Sweden has had a positive impact on the embedded value of the business (as shown at the bottom of the page).

GROUP EEV DEVELOPMENT HISTORY

The Embedded Value of the Group has grown significantly since incorporation. The reported growth is net of £149m of cumulative dividend payments. The chart illustrates Embedded Value growth and the impact of the acquisition strategy. Values quoted are as at 31 December of the relevant year.

'04 £126M
Chesnara lists on the London Stock Exchange, following its acquisition of CA plc.

'05 £176M
Chesnara acquired CWA from Irish Life and Permanent plc. EEV gain of £30.3m arising on acquisition and £22.0m new share capital issued.

'06 £189M
The long-term business of CWA was transferred to CA plc under the provisions of Part VII of FSMA.

'07 £187M
Steady operating profit on covered business to support dividend payment.

'08 £183M
Steady operating profit on covered business supports dividend payment in year.

GROSS CASH GENERATION £49.7M IN 2013

(2012: £34.0m).

2010	2011	2012	2013
£18.8M	£33.1M	£34.0M	£49.7M

Note 1: Cash generation is defined on page 34. The figures exclude any impact from acquisition funding arrangements including cash utilised to directly fund acquisitions.

TOTAL SHAREHOLDER RETURN

5 year TSR of 261%

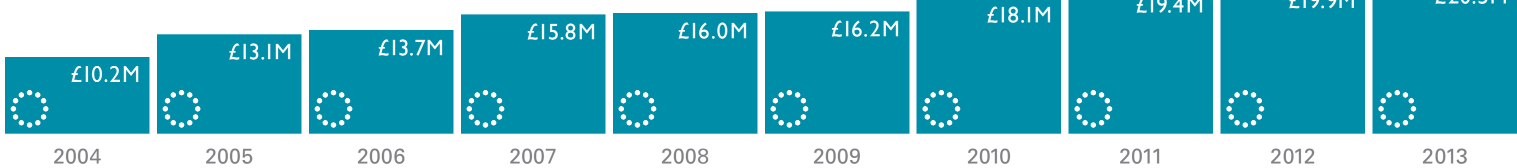
2013 TSR of 79%

The Chesnara investment proposition is dependent upon cash emerging from the in-force books of business at levels sufficient to fund the dividend strategy, support future acquisitions, fund Movestic and provide adequate surplus to protect against the potential for earnings volatility in the future.

The cumulative gross cash generation since 2010 of £136m is more than adequate to support the funding of the total dividend payments over that period, providing 174% coverage of paid and proposed dividends of £78m for the same period.

Capital management actions including Part VII transfers and regulator approved capital extractions ensure the cash generated is available for distribution to the fullest extent possible.

PROVEN ATTRACTIVE DIVIDEND HISTORY



'09 £263M

Chesnara acquired Movestic Liv, an open Swedish Life and Pensions business, resulting in an EEV gain of £54.2m on acquisition.

'10 £355M

Chesnara acquired SPI and its subsidiary, SPP, from JPMorgan and Movestic acquired the business of Aspis Liv, a small Swedish life and health insurer. These purchases resulted in a combined gain on acquisition of £41.0m. £25.7m new share capital issued.

'11 £295M

The long-term business of SPI and SPP were transferred to CA plc under the provisions of Part VII of FSMA. Falls in both equity markets and bond yields result in a reduction in EEV in the year.

'12 £311M

SPI and SPP were de-authorised from conducting activities regulated under the provisions of FSMA 2000. Investment market factors support the increase in EEV in the year.

'13 £376M

Chesnara acquired Protection Life (formerly Direct Line Life Insurance Company Limited) from Direct Line Group plc, with an EEV gain on acquisition of £12.3m. Strong investment markets drive EEV growth.

Notes

1. Throughout the Chairman's Statement, Business Review and Financial Review sections, all results quoted at a business segment level exclude the impact of consolidation adjustments. These consolidation adjustments are analysed by business segment on page 30.
2. Net cash generation in the year is defined as the net amount of the following items:

i. Gross cash generation, defined as:

a. the change in the excess of actual regulatory capital resources over target capital resources in respect of the CA, S&P and PL operating segments;

b. less capital contributions made by the Group to the Movestic operating segment; and

c. less cash utilised by Parent Company operations.

ii. Plus the cash impact of one-off management actions coupled with movements in the restrictions of policyholder funds to shareholder funds.

As such, the net and gross cash generation KPIs defined above do not align to the Cash Flow Statement as included in the IFRS Financial Statements.

Throughout the Annual Report & Accounts the following symbols are used to help distinguish between the various financial and non-financial measures reported:

- IFRS
- Cash generation
- EEV
- EEV earnings
- Solvency
- Dividend/Total Shareholder Return
- Part VII
- Operational performance
- Compliance
- New business market share
- Acquisitions

Throughout the Annual Report & Accounts the following colour themes are used to help distinguish between the five core Group strategic objectives:

1. Maximise value from the in-force book
2. Enhance value through new business
3. Acquire life and pension businesses
4. Maintain a strong solvency position
5. Adopt good regulatory practice at all times

2013 HIGHLIGHTS

FINANCIAL

208% INCREASE IN IFRS PRE-TAX PROFIT

Increase in IFRS pre-tax profit for the year ended 31 December 2013 to £60.6m (year ended 31 December 2012: £19.7m). This is stated after a gain arising on the purchase of Protection Life of £2.8m.

Financial Review Page 30

GROSS CASH GENERATION £49.7M

Gross cash generated in the year of £49.7m (year ended 31 December 2012: £34.0m).

Cash Generation Page 34

EEV INCREASE OF £65.3M

Increase in EEV from £311.1m at 31 December 2012 to £376.4m at 31 December 2013 after dividend distributions of £20.1m in the year.

Financial Review Page 37

EEV EARNINGS AFTER TAX OF £82.7M (PRE-MODELLING ADJUSTMENTS)

EEV earnings net of tax increased by £51.5m to £82.7m for the year ended 31 December 2013 (year ended 31 December 2012: £31.2m).

Financial Review Page 35

MOVESTIC NEW BUSINESS CONTRIBUTION OF £7.2M

Movestic has generated a new business contribution of £7.2m in the year (year ended 31 December 2012: £2.6m).

Financial Review Page 36

GROUP SOLVENCY 194%

Strong Insurance Group Directive solvency cover of 194% (31 December 2012: 244%).

Financial Management Page 25

FINAL DIVIDEND INCREASED BY 3.4%

Proposed interim dividend increased by 3.4% to 11.63p per share.

OPERATIONAL

PURCHASE OF PROTECTION LIFE

The purchase of Protection Life completed on 28 November 2013, in line with one of our core objectives of purchasing value-adding closed life books in the UK.

GOOD COMPLIANCE RECORD

Good regulatory compliance record continues.

MOVESTIC NEW BUSINESS GROWTH

Return of IFA support has driven a 61.9% increase in like for like APE new business volumes.

MOVESTIC NEW BUSINESS MARKET SHARE

Strong recovery of new unit-linked pensions business market share continues in the year to 8.0% (2012: 5.3%).

CHAIRMAN'S STATEMENT

2013 has been an extremely positive year for Chesnara. Operationally the business has delivered strongly across all of its stated strategic objectives. In particular, the successful acquisition of Direct Line Life (now Protection Life), the continued emergence of significant value from the in-force books and the generation of material Movestic new business profits demonstrates the effective delivery of the main value enhancement pillars of our corporate strategy. The operational performance has resulted in impressive financial results in the year. We commence 2014 with increasingly robust operational and financial foundations which bode well for the continued success of the Chesnara Group.

Peter Mason
Chairman

CHAIRMAN'S STATEMENT (CONTINUED)

I am pleased to report that Chesnara has performed towards the top end of realistic expectations across all aspects of the corporate strategy.

Objective	Outcome		
	Headline	Reference	Page
1 Maximise value from the in-force book	£49.7m of gross cash generation	Business review	19
2 Enhance value through new business	£7.2m of Swedish new business profit	Business review	22
3 Acquire life and pensions businesses	Successful acquisition of Direct Line Life	Business review	24
4 Maintain a strong solvency position	Group solvency of 194%	Business review	25
5 Adopt good regulatory practice at all times	Continued good regulatory record	Business review	27

The strong performance has enabled the continuation of our attractive dividend policy and the subsequent value enhancement has resulted in competitive share price growth. This has led to an impressive total shareholder return (TSR) of 79% in the year. My statement considers the more material components of our strategy in a little more detail as follows:

Maximise value from the in-force book

The UK in-force book is the primary source of IFRS surplus and cash generation. I am particularly pleased to report that significant value has emerged from the UK in-force book during the year. As explained in more detail in the Financial Review section of the Strategic Report, the in-force book can be characterised into two components in terms of value emergence dynamics. The "stable core", consisting of the CA, and CWA books (and now also Protection Life), has generated a strong level of surplus very much towards the higher end of expectations. The "variable element", namely S&P is known to be more sensitive to investment market conditions. During 2013 investment market conditions have been beneficial, resulting in a significant reduction in the expected exposure to policy guarantees. In addition, Management has, with regulatory approval, released £15.5m of capital previously constrained in S&P. Gross cash of £49.7m was generated and the total combined impact of the financial results, capital restrictions, Protection Life capital requirements and the exceptional capital release results in net cash available for distribution from the in-force book of £36.7m during 2013.

Cash available for distribution

2013: £36.7m

2012: £36.1m

Enhance value through new business

I noted in my statement in the 2012 Annual Report & Accounts that following a difficult period, I was encouraged that there were signs of recovery in the Movestic business. I am delighted to report that those early positive signs have resulted in a significant recovery in IFA support of the Movestic business during 2013.

This is illustrated by the 61.9% increase in APE new business volumes compared with 2012. This growth has been achieved without any discernible increase in the acquisition cost base and hence the results show a significant new business contribution for the year.

Movestic new business contribution in 2013

£7.2m

2012: £2.6m

From this profitable base and with the level of momentum and positive sentiment to the new business proposition, I expect Movestic, now that it has re-established its strong market position, to continue to make a significant contribution to the Embedded Value of the Group from its new business operations in the future.

Acquiring life and pension businesses
The acquisition of Protection Life during the year was a good transaction. The business fits well with the existing UK product portfolio and operating model. The transaction has created incremental embedded value of £12.3m which is consistent with the low level of risk associated with the acquired business.

In addition to the stand alone benefits of the Protection Life acquisition, the deal continues to give momentum to our acquisition strategy and reaffirms the strength of our acquisition proposition. The process confirms our continued presence in the consolidation market, the support of our investors and debt finance providers and our credibility with the regulatory authorities following the move to the dual regulation model.

I would like to thank those involved in the transaction including our business partners, advisors, the Chesnara governance team and also the management team of Direct Line Group who were professional and efficient throughout the acquisition process.

Maintain strong solvency position
It was mutually beneficial to both parties that Protection Life was acquired with no capital surplus and subsequently Chesnara recapitalised the business on acquisition. This, together with the fact that the PL purchase consideration was greater than the net worth acquired, has resulted in a reduction in the Group solvency position at the end of the year. The impact was as expected based on our assessment of the PL acquisition. The Part VII transfer planned for 2014 will have a positive impact such that much of the adverse effect is expected to be reversed. Despite the impact on Group solvency from the PL acquisition, the position remains strong and significantly higher than the internal governance target of 100%.

Group solvency
194%
2012: 244%

Adopt good regulatory practice at all times
2013 has seen a significant amount of regulatory change. The Solvency II programme has picked up more momentum as guidelines and timetables have become clearer. Reporting developments, including improvements to the way we articulate the performance of the business in the year and enhancements to the reporting of our remuneration policy, have been made and the improvements are incorporated in Section B "Strategic Report" and Section C "Corporate Governance" of the Report & Accounts. Our regulatory framework remains robust. I report on regulatory and governance matters in more detail in my governance overview on page 52.

Risk management
Risk management is not stated as a specific objective. It is ingrained in the culture and decision making in all we do as a business and is seen as an integral and key priority that feeds into all our objectives. We simply do not consider the delivery of any strategic objective as being successful if the appropriate balance between risk and reward has not been retained. As such I am reassured that our assessment is that we have marginally reduced the overall risk profile of the Group during the year.

Pension reforms
In his Budget announcement on 19 March, the Chancellor of the Exchequer announced significant changes which will affect the pensions and annuity markets. Chesnara's UK business does not have a significant exposure to annuities and has not sought to write such business for a number of years. We note the changes to flexibility of pensions arrangements however we are not expecting any immediate or significant change to our book of business, or the value of it.

Outlook
We commence 2014 with strong operational platforms in both the UK and Sweden, solvency margins are healthy and increased levels of cash generation provide a reassuring buffer against future potential earnings variability and a good source of funding for future potential acquisitions and dividend payments. This, together with the fact that we have reaffirmed our acquisition capabilities and credentials during the year, gives cause for optimism for the continued success of Chesnara in terms of providing value to both policyholders and shareholders.

Peter Mason
Chairman
27 March 2014

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STRATEGIC REPORT

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OUR VISION & STRATEGY

MISSION

Our mission is to deliver value for shareholders, while maximising returns to policyholders. Underpinning everything we do is a desire to maintain regulatory and legal compliance. Meeting these aims is achieved through attracting and retaining highly talented people who not only bring expertise and quality thinking into our business and industry, but also have a passion for improving outcomes for our customers and shareholders. All members of the Chesnara team share a common value in recognising their responsibility to shareholders and policyholders.

VISION

To be recognised as a responsible and profitable company engaged in the management of life and pensions books in the UK and Western Europe through:

- Commitment to the core business of closed UK life and pensions book management;
- Further acquisitions where they meet stringent assessment criteria;
- Realisation of increasing economies of scale; and
- Continued delivery of competitive returns to shareholders and policyholders.

While we focus on delivering value to shareholders primarily through dividend streams arising from strong cash generation as the UK life and pensions books run off, we also consider the acquisition of open businesses where there is clear value enhancement and where the scale is such that our core proposition of being principally a closed book consolidator and manager does not become unbalanced.

STRATEGIC OBJECTIVES

At Chesnara the strategic objectives, which support the fulfilment of our mission and the realisation of our vision are embedded in day-to-day business operations and underpin Management decisions. At the core of the business is the recognition by the Board and Management Team of their responsibilities to policyholders and shareholders, so that the values and principles of Management wholly align with strategic objectives. This value of responsibility is at the heart of the Chesnara business model. Our core strategic objectives are explained and evidenced on the following pages.

STRATEGIC OBJECTIVES

MAXIMISE VALUE FROM THE IN-FORCE BOOK

Why is this of strategic importance?
Chesnara is primarily a "closed book" operation and as such generating surplus and cash from the existing in-force books is at the heart of its investment proposition.

How do we deliver this strategic objective?
We proactively manage continuing financial exposures:

- Significant financial exposures in life and pensions portfolios typically arise from onerous policy options and guarantees, and compensation claims for past misselling of products. The Group's portfolios had, in earlier years, had very little exposure to the impact of investment market performance on options and guarantees. However, just over 29% of the policies managed by S&P, which was acquired in December 2010, contain guarantees to policyholders and therefore the Group's exposure to market performance increased. Furthermore, the Group continues to have exposure to market weakness by way of the impact on policyholders' linked funds, from which surplus is generated. We seek to minimise this exposure by regular review of investment asset holdings and by adjusting investment manager guidelines where appropriate and within the boundaries of our obligations to policyholders.

We operate in a manner that aims to ensure that policy attrition is as low as possible, as this is a key determinant of our future profitability and of the level and longevity of the emergence of surplus, which underpins our dividend-paying capacity. As such we continue to maintain a focus on the retention of policies where it is in the interest of customers to continue with their arrangements.

We continue to manage investment performance so as to provide a competitive level of return to our policyholders. The CA funds are primarily managed by Schroder Investment Management Limited while the CWA funds continue to be managed by Irish Life Investment Managers Limited. The S&P funds are managed by JPMorgan Asset Management (UK) Limited in order to maintain continuity for policyholders. We meet formally with fund managers on a quarterly basis to assess past performance and future strategy.

The Movestic funds are managed by a carefully selected range of fund managers who have strong performance records in the relevant sector. Performance is monitored very closely and regular meetings are held with fund managers. Should under-performance continue then an alternative manager is sourced and appointed to manage the relevant assets. Where a new market niche or specific opportunity is identified new funds may also be added.

We adopt a business operating model which ensures unit expenses remain appropriate for the scale of the in-force book.

- UK operations are predominantly outsourced, with contract charging structures that ensure a significant element of the cost base varies in line with the run-off of the business.
- Acquisitions are integrated into the Chesnara Group in a manner to ensure optimum operational and financial synergies.

Risks associated with this strategic objective

- Sustained adverse investment market conditions challenge our ability to manage financial risks inherent in the in-force portfolio.
- Despite the effective cost management model, in the absence of further acquisitions or management action, there remains a risk that unit costs will increase in the long-term.
- A number of factors including economic recession, adverse investment performance and a deterioration in customer servicing standards could lead to an increase in policy attrition.

ENHANCE VALUE THROUGH NEW BUSINESS IN SELECTED MARKETS

Why is this of strategic importance?

- The Chesnara business model primarily focuses on "closed book" consolidation. However, where acquisitions offer the potential to write new business at an adequate return on capital we will continue to invest in the new business operations so as to maximise value for the Group.
- Maintaining a flexible position regarding the willingness to remain open to new business will potentially increase the number of acquisition targets and indeed our attractiveness to such targets.

How do we deliver this strategic objective?
Currently the only part of the Chesnara Group writing material levels of new business is Movestic, our Swedish business. Movestic has a new business operation that delivers a positive new business contribution. There are detailed business plans in place that aim to increase new business profits through a combination of new product launches and improvements to operational effectiveness. Local and Group management receive management information to enable a continuous assessment of the performance to ensure being open to new business continues to enhance value.

Risks associated with this strategic objective

- New business volumes fall below levels required to ensure sufficient return on the acquisition cost base.
- Product margins fall to unsustainable levels due to factors including; market price pressures, reduced investment growth, increased policy lapse rates and increasing maintenance unit costs.

STRATEGIC OBJECTIVES (CONTINUED)

3 ACQUIRE LIFE AND PENSIONS BUSINESSES

Why is this of strategic importance?

- As with any business, it is important that we use our capital efficiently to provide optimum return to shareholders.
- As a primarily "closed book" operation, further acquisitions can maintain and increase the Group's cash flow and operational economies of scale.

How do we deliver this strategic objective?

Ultimately we rely on acquisition opportunities being available in the market, our target market being the UK and Western Europe.

We actively engage with various investment advisers (including Canaccord Genuity Limited on a retained basis) to ensure we are aware of acquisition opportunities.

We will leverage our proven track record in the consolidation market. Past experience suggests we maintain a high degree of credibility with regulators, policyholders, lenders and shareholders. All prior acquisitions have been delivered with no adverse impact in terms of treating customers fairly, regulatory standing or our reputation in the life and pensions consolidation market.

We will not pursue opportunities which do not meet very stringent assessment criteria.

Risks associated with this strategic objective

- If Chesnara makes no further acquisitions there will be a potential strain on the per policy unit costs of the existing business, with the potential impact on dividend sustainability.
- Any departure from the current, stringent acquisition assessment criteria and due diligence procedures could result in an acquisition that, under certain stress scenarios, adversely impacts the financial strength of the Group.

4 MAINTAIN A STRONG SOLVENCY POSITION

Why is this of strategic importance?

Adequate solvency capital:

- Protects against volatility particularly due to external economic conditions outside management control.
- Ensures compliance with regulatory requirements.
- Supports potential acquisition opportunities.
- Supports ongoing dividend capability.

How do we deliver this strategic objective?

The Board considers comprehensive information covering the actual solvency position, together with projections for expected and stressed scenarios. The management team tracks the performance of the key factors known to impact the solvency position. Trigger points are set and documented such that management action will be instigated should any of the key trigger points be reached. The setting and review of trigger points is an integral component of the Group's risk appetite model.

Potential acquisitions are assessed by taking a prudent view on not only the short-term impact on the Group's solvency position but also on the potential risk to long-term solvency.

Risks associated with this strategic objective

- Sustained adverse economic conditions outside of risk appetite tolerances will erode the solvency surplus.
- Changes in legal or regulatory requirements.

5 ADOPT GOOD REGULATORY PRACTICE AT ALL TIMES

Why is this of strategic importance?
Chesnara management fully recognises the benefits to both shareholders and policyholders of adherence to good regulatory practice. We comply not because the regulations insist but because the rules clearly reflect good, responsible business management and governance.

How do we deliver this strategic objective?
We maintain a strong internal risk management culture and regime throughout the Group and we maintain systems and controls which satisfy regulatory requirements at all levels.

The UK and Swedish life assurance and pensions industries are both highly regulated, in terms of the conduct of business operations and financial reporting. We place particular emphasis on managing our regulatory compliance through a proactive and prudent approach and on maintaining a positive relationship with our principal regulators, the Prudential Regulation Authority ('PRA') the Financial Conduct Authority ('FCA'), and the Finansinspektionen ('FI').

Accordingly, significant effort is directed towards ensuring that the operations are effectively managed in terms of conduct of business regulations and prudential solvency requirements and towards the significant change that is required in the business to implement Solvency II and to ensure continuing compliance with its requirements.

We have developed a strong Governance structure which sits at the heart of the Chesnara operating model, supported by a robust and effective Corporate Governance framework.

- All Governance roles, with direct impact on regulatory compliance, are carried out by people with significant industry experience.
- The level of investment in the Governance team reflects the Board's desire to ensure effective adherence to all regulatory best practice.
- The Chesnara culture ensures other objectives do not conflict with the objective of adopting good regulatory practice at all times.

Risks associated with this strategic objective
The key risk relating to regulatory compliance is that rules and regulations are poorly understood or implemented.

Underlying the fulfilment of strategic objectives is the core value shared by the Board and Management team of recognising responsibilities to all stakeholders on a balanced basis.

Often decisions are required that may have conflicting impacts on the different stakeholders. Maintaining a balanced view across the stakeholder groups is critical to ensuring Management continues to make decisions that benefit all stakeholders in the longer term.

The governance framework ensures controls and procedures are in place to protect all stakeholders.

THE CHESNARA BUSINESS

The history of the development of the Chesnara Group, together with a description of the characteristics of our operating businesses, illustrates how we have endeavoured to achieve our strategic objectives and how we have created the platform for their ongoing realisation.

The successive acquisitions made by Chesnara have progressively increased the overall longevity of its run-off portfolio, while diversifying the policy base. At 31 December 2013, the Group had 255,000 (2012: 258,000) pension policies and 615,000 (2012: 525,000) life policies in force.

Chesnara continues to seek to participate in the consolidation of life assurance and pensions businesses in the UK and Western Europe.

We primarily target acquisitions with an acquisition value of between £50m and £200m, although other opportunities are considered. All opportunities are assessed against a number of key criteria including size, risk (including actual or potential product and financial liabilities), discount to embedded value, capital requirements and the pattern and quality of predicted profit emergence. Our strategic approach, however, remains that such potential acquisitions should not detract significantly from, and should contribute to, the primary aim of delivering an attractive dividend yield, although opportunities which present a significant value uplift or growth opportunity will also be evaluated.

History (2004 – 2013)

’13 Chesnara acquired Direct Line Life Insurance Company Limited (now renamed Protection Life Company Limited) from Direct Line Group plc for £39.3m, funded by a mixture of bank debt and internal cash resources. PL is closed to new business, with a portfolio containing non-linked products, including mortgage life cover, fixed term life cover (both with and without critical illness cover) and over 50’s life cover to UK customers.

’12 SPI and SPP were de-authorised from conducting activities regulated under the provisions of the Financial Services and Markets Act 2000, thereby releasing £7.0m of solvency capital.

’11 The long-term business funds and part of the shareholder funds of SPI and SPP were transferred to CA plc under the provisions of Part VII of FSMA, thereby realising significant financial and operational synergies.

’10 Chesnara acquired SPI and its subsidiary, SPP, from JPMorgan Asset Management Limited for a consideration of £63.5m, funded by a mixture of debt and new equity capital. SPI and SPP are also closed UK Life and Pensions businesses whose portfolios predominantly comprise pensions policies (both unit-linked and with-profits), endowments (some with-profits) and protection policies.

Movestic acquired the in-force business, personnel, expertise and systems of Aspis Försäkrings Liv AB, a small Swedish life and health insurer, thereby complementing Movestic’s existing focus on pensions and savings contracts.

’09 Chesnara acquired Movestic Liv, an open predominantly unit-linked Swedish Life and Pensions business, for £20m, representing a significant discount to its embedded value. Subsequently a new subsidiary, Movestic Kapitalförvaltning was established to separate out fund selection and management activities from Movestic Liv and to develop these services in the wider marketplace.

’06 The long-term business of CWA was transferred to CA plc under the provisions of Part VII of the Financial Services and Markets Act 2000 (‘FSMA’), thereby realising significant financial and operational synergies.

’05 Chesnara acquired CWA from Irish Life and Permanent plc for a consideration of £47.8m, funded principally by a mixture of debt and new equity capital. CWA is also a substantially closed UK Life and Pensions business. Its portfolio, which is also predominantly unit-linked, comprises endowments, protection and pensions policies.

’04 Chesnara listed on the London Stock Exchange, following its acquisition of CA plc on the latter’s demerger from Countrywide plc, a large estate agency group. CA is a substantially closed UK Life and Pensions business whose portfolio predominantly comprises unit-linked endowment and protection policies.

BUSINESS MODEL

Business model
The following sets out the key operating characteristics of the Chesnara business:

Chesnara plc and the UK business activities are based in Preston, Lancashire, while Movestic is based in Stockholm in Sweden. Chesnara has 21 (2012:20) full-time equivalent employees in its corporate governance team in the UK. In Sweden, the headcount is 123 (2012:127).

UK

- The primary focus of the UK businesses is the efficient run-off of their existing life and pensions portfolios. This gives rise to the emergence of surplus which supports our primary aim of delivering an attractive dividend yield to our shareholders. By the very nature of the life business assets, the surplus arising will deplete over time as the policies mature, expire or are the subject of a claim.
- In the UK we maintain a small professional corporate governance team which is responsible for both the regulatory and operational requirements of the listed entity Chesnara and those of the UK business. Our team in the UK is intentionally small and focused in the interests of keeping the overall expense base tight. It has the capability to manage the UK business and to assess acquisition opportunities, and is supplemented from time to time by temporary resource if justified by operational or strategic demands.
- The operating model of our UK business is directed towards maintaining shareholder value by outsourcing all support activities to professional specialists. This typically embraces policy administration, systems, accounting, actuarial and investment management and reduces the impact of potential fixed and semi-fixed cost issues which would otherwise occur as the income streams arising from a declining in-force portfolio diminish. By securing long-term contracts to support these activities we aim to enhance the variability of the expense base with the size of the in-force policy portfolio. This also leads to the avoidance of the full weight of systems development costs, as these will, where possible, be shared with other users of the outsourcers' platforms.
- Oversight of the outsourced functions is a significant part of the responsibility of the central governance team. The maintenance of service and performance standards, and thereby the core interests of shareholders and policyholders, is maintained through a strict regime of service level agreements and through continuous monitoring of performance. This is reinforced by adherence to the principles and practice of treating customers fairly.

Sweden

- The primary focus of the Swedish business is to grow market share in the company-paid and individual pensions market, whilst developing further profitable business in other areas, in particular in the risk and health market. Writing new business requires funding to support the initial costs incurred: this is provided by way of external financial reinsurance or cash contributions from Chesnara. As the in-force business portfolio grows in scale the income generated by it eventually allows the business to self-fund and become a net generator of cash.
- In Sweden, as the Movestic book is open and in a growth phase, we retain a broader-based management and operational team. Rather than outsource core functions, we believe that it is important that the drive and team ethic of Movestic is preserved as they seek to grow profitable market share in our target markets. Whilst Movestic manages the selection of appropriate investment funds, investment decisions are made solely by the fund managers.

BUSINESS REVIEW

Introduction

The Business Review is structured to report on how we have performed against each of our stated strategic objectives. For each objective the review reports separately for our UK and Swedish operations to the extent separate reporting is relevant. For each objective the review focuses on:

- How we have performed generally
- Key developments or challenges
- Key performance indicators
- Risks associated with each objective

The strategic objectives are reassessed on an annual basis as part of the Group business planning process. The continued relevance of the objectives gives consideration to recent performance, emerging risks and future opportunity. They are assessed giving full regard to both internal and external influences e.g. changes to regulatory requirements.

The strategic objectives have not changed during 2013 nor is there expected to be any significant change in focus during 2014.

In addition to the five core objectives there is an over-arching objective to "Deliver value to stakeholders on a responsible and balanced basis". That is, over-arching the fulfilment of strategic objectives is the core value shared by the Board and Management team of recognising responsibilities to all stakeholders on a balanced basis. Often decisions are required that may have conflicting impacts on the different stakeholders. Maintaining a balanced view across the stakeholder groups is critical to ensuring Management continues to make decisions that benefit all stakeholders in the longer term.

The governance framework seeks to ensure that controls and procedures are in place to protect all stakeholders. The control environment has remained effective and robust throughout the year. Further details of the operation of the governance framework are included in Section C – Corporate Governance, including a governance overview from the Chairman.

Our over-arching objective: Deliver value to stakeholders on a responsible and balanced basis

Maximise value from the in-force book

Enhance value through new business

Acquire life and pension businesses

Maintain a strong solvency position

5

Adopt good regulatory practise at all times

BUSINESS REVIEW

I MAXIMISE VALUE FROM THE IN-FORCE BOOK | UK

Significant levels of cash have emerged from the in-force book during the year at levels towards the top end of realistic expectations.

Highlights
- £54.1m of gross cash generation (excluding Chesnara parent company cash).
- £15.5m exceptional cash release due to the removal of a capital constraint in S&P.
- 5% growth in funds under management.
- Positive EEV development.
- Strong fund performance.
- Improved policy attrition levels.

Review of the year

Operational performance has been strong across the three key areas of focus for the in-force book, namely: management of the assets, regulatory compliance and ensuring we continue to provide a high quality service to policyholders in terms of administration service levels and investment return.

Our administration and asset management outsource partners have all performed well during the year and generally exceeded service level arrangements and relevant benchmarks. Further assessment of our future expenses associated with our outsourcing model have led to a strengthening of our expense assumptions during the year.

The CA plc Investment Committee has continued its oversight of policyholder funds through regular meetings with the investment managers. We continue to work with our managers in order to ensure the underlying investment mix is the most appropriate for policyholders. In particular, the programme to move the ex-S&P Pension Property Fund from direct investment to collective funds has progressed well.

£54.1m of gross cash generated from business as usual operations

Cash generation during the year has been particularly strong. This is primarily due to the core product based surpluses remaining resilient together with a significant reduction in the cost of S&P guarantees. The S&P book has made a significant contribution of £28.9m to the 2013 cash generation. This is consistent with the fact that the S&P surplus is sensitive to investment market performance, which was generally favourable during the year.

In addition to the operational cash generated, a process has been undertaken whereby, with regulatory approval, £15.5m of constrained capital in Save & Prosper has been released to shareholder funds.

Unit-linked funds under management

The continuing strong level of unit-linked funds under management supports the on-going level of profitability of the UK businesses, as fund-related charges are an important component of profit.

The movement in the value of unit-linked funds under management is a function of:

i) performance of the funds across UK equities, international equities, property and fixed interest securities;

ii) received and invested premiums; and

iii) policies closed, due to surrender, transfer or claim.

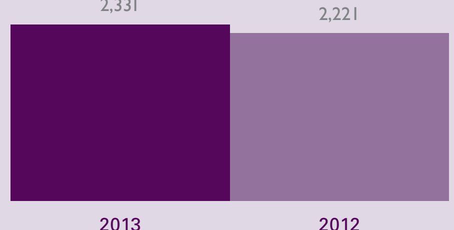
Good performance by our administration and investment management business partners has contributed positively to all three of the above factors.

5% growth in funds under management in the year

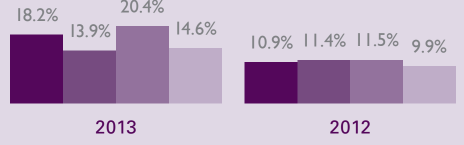
Risks associated with the strategic objective

The acquisition of S&P, as signalled at the time of the acquisition, has added an increased level of earnings volatility for the UK business. S&P has a proportion of its product base that provides guaranteed returns. The probability of guarantees being of value to policyholders increases when the value of assets held to match the policy liabilities fall or when, particularly for those guarantees expressed as an amount of pension, bond yields fall. To mitigate this risk, to some extent, assets held by shareholders to provide security for these guarantees are invested in cash and long bonds. As a consequence, our results will be negatively affected by falls in equity and property values, which impact assets backing policyholder liabilities, and/or falls in bond yields, which impacts the cost of providing the guarantees were to occur. Conversely, increasing markets and yields will positively affect the results. Close management of the portfolio backing these liabilities continues.

Funds under management year on year increase (£m)

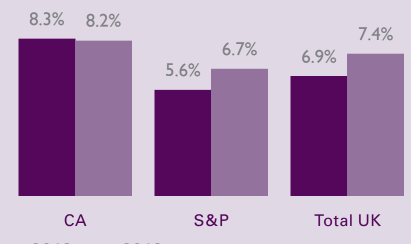


Fund performance



- CA Pension Managed
- CWA Balanced Managed Pension
- S&P Managed Pension
- Benchmark – ABI Mixed Inv 40%-85% shares

Policy attrition, based on policy count



BUSINESS REVIEW

I MAXIMISE VALUE FROM THE IN-FORCE BOOK | SWEDEN

Following a favourable investment market performance and the evident increase in IFA support, Movestic's funds under management have increased by 24.1% during 2013.

Highlights

- Strong growth in funds under management; increase of 24.1% during 2013.
- Positive EEV development.
- Fund performance improved significantly during 2013.
- Significant improvement in the ratio of transferred in business to transferred out business.

Review of the year

During 2013 the efforts to regain confidence in the market were manifested by the increased IFA support which was evident not only in new sales but also in the large amount of transferred in business and in the stabilised position for transferred out business. The focus to ensure that we continue to provide a high quality service to IFAs and policyholders in terms of administration service levels and investment return continues and independent market surveys show continuously improving ratings.

Within the Life & Health book of business, the portfolio continues to deliver high quality in terms of claims development with a gross loss ratio of 50.3% for 2013 (2012: 48.4%).

The scale of the Pension and Savings in-force book in Sweden is such that profits emerging from it are relatively modest in comparison to UK equivalents. As such, the challenge is to increase the value of the funds under management from which we earn income in the form of management charges and fund rebates. The following matrix illustrates the factors that directly influence the growth of the in-force book:

The general performance on all four factors has been positive resulting in strong fund growth. The factors are considered in more detail below:

New business

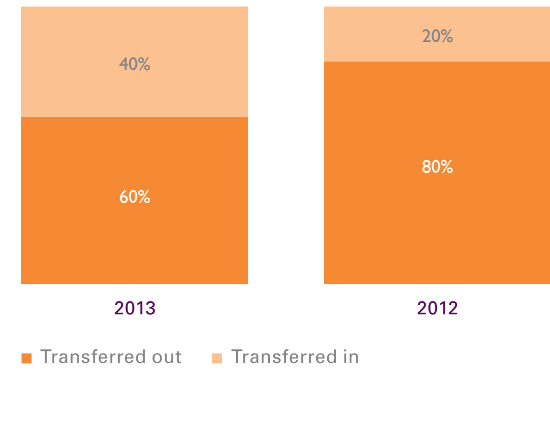
The review of the new business operation is covered in the "Enhance value from new business" objective review on page 22.

Policy attrition (fig 1 & fig 2 on the following page)

The strengthened IFA support so evident in the new business results has had a less marked impact on policy attrition levels. Whilst the lapse rates did improve significantly during 2013 the level of policy transfers out remains broadly stable. We believe this indicates that the levels of transfers experienced during 2013 are reflective of the broader dynamics of the IFA market, rather than being a direct reflection of customer service levels within Movestic. In light of this, the persistency assumptions were further strengthened during 2013. The embedded value, as reported within the 2013 results, therefore now broadly aligns to current levels of persistency. Management still believes that, in time, the impact of continued improvements in service levels, together with general external market developments, should have a positive impact on the long-term persistency levels. Any positive impact will only be recognised if improvements are seen in actual attrition rates.

Despite there being no improvements in transfer levels, the ratios of transferred in business to transferred out has improved from 1:4 during 2012 to 1:1.5 during 2013.

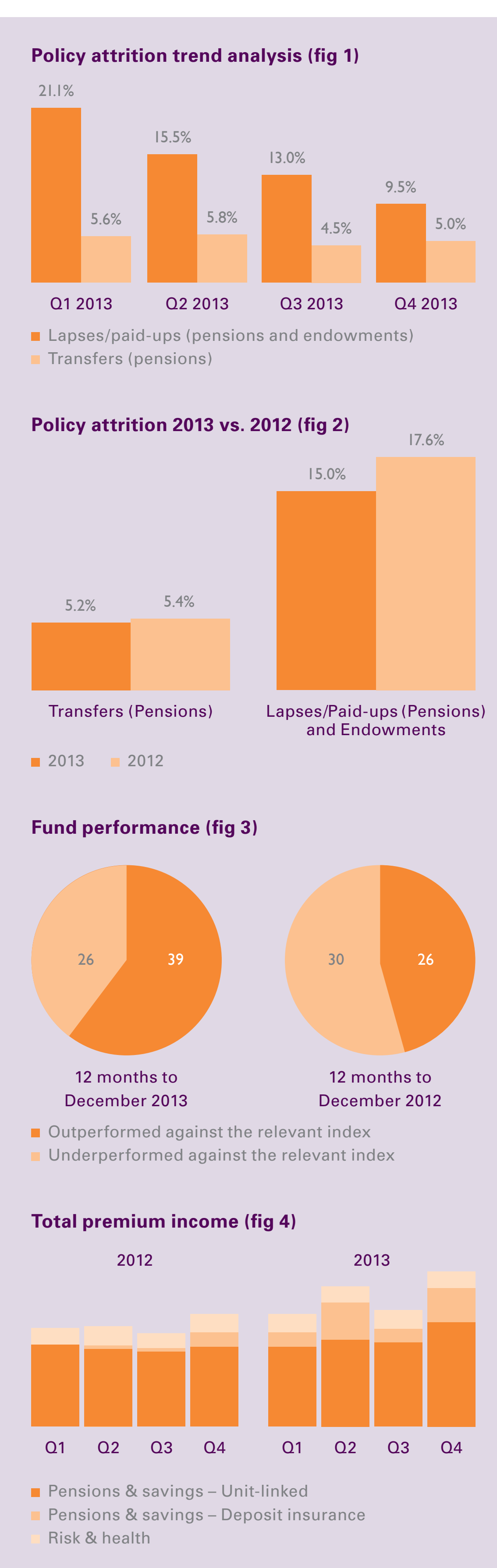
Significant improvement in the ratio of transferred in business to transferred out business.



BUSINESS REVIEW

I MAXIMISE VALUE FROM THE IN-FORCE BOOK | SWEDEN

(CONTINUED)



Fund performance (fig 3)

The increase in the number of funds out-performing their indices is a testament to our investment and fund selection strategy. One of Movestic's key differentiators is its approach to selecting the funds available to investors. Rather than adopt mainstream funds, which, in Sweden, are those predominantly managed by subsidiaries of banks which also have life assurance subsidiaries, we select a limited number of funds from a wide range of independent fund managers.

The funds selected are, in general, actively managed funds with a value approach. The performance of all funds is closely monitored and regular contact is made with managers to ensure that the underlying reason for fund performance, whether positive or negative, is fully understood. Funds that do not perform favourably compared with the relevant index are wholly replaced if there are no acceptable strategies for improvement. Where applicable we continue to add further funds to fill perceived gaps in the range.

The relative fund performance measure focuses on the number of funds under or over performing their relevant indices. An alternative and well established fund performance measure, produced by a respected industry magazine, compares the value of savers' average fund holdings. This measure best reflects the investment performance from a policyholder perspective. According to that measure, Movestic's fund range performed very well during 2013 with an average return of 13.8%, building on 7.7% in 2012, which maintains our strong market position.

Premium income (fig 4)

The increase in premium income is predominantly due to an increase in new business levels. The recurring regular premiums have increased marginally year on year for the Pensions and Savings business which is key to achieving sustained growth. Regular premiums for the Life and Health business have remained broadly flat year on year.

Risks associated with the strategic objective

The risk of high levels for persistency rates has somewhat altered during the year. It has become more evident that there is inherent risk in the Swedish market where customer awareness of the ability to transfer their pension is a feature with increasing influence as a consequence of intensified public discussion. The Movestic product proposition already offers significantly more portability for transferring pensions than the general market. As such, although higher transfer rates would create challenges, an increased right to transfer would be beneficial to Movestic in terms of its market position with other more traditional competitors.

BUSINESS REVIEW

2 ENHANCE VALUE THROUGH NEW BUSINESS | SWEDEN

IFA support of the Movestic proposition has continued to gain momentum as evidenced by a 61.9% increase in APE new business volumes compared with 2012.

Highlights

- 61.9% increase in new business volumes compared with 2012.
- Continued recovery in new business market share throughout the year.
- IFA support as measured by the number of IFA's that sell Movestic products, shows an increase of 32.5% in 2013.
- The development of innovative product concepts continues.

Review of the year

In light of the administration performance issues in 2011 and 2012 it is particularly encouraging to report the significant recovery in new business rates and also that the re-engineered processes have coped well with the sharp increase in new business volumes.

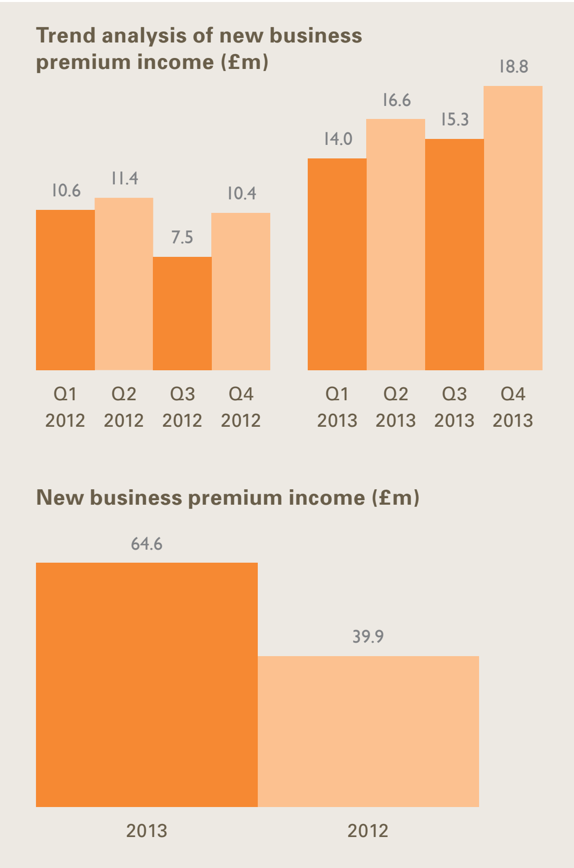
Changes to the senior management structure together with the transfer of certain IFA-critical processes to Stockholm have had a positive impact and ensure the operating model is now better suited to support the acquisition and marketing proposition.

There is a positive management environment which means that staff are well motivated and there is a strong collective sense of commitment to continue with improvements required to fully recover and consolidate its market position. The Group CEO made a statement in the 2012 Annual Report & Accounts that "The business foundations are significantly stronger than last year and from this improved base I am confident that Movestic can begin to deliver longer-term financial benefits to the Chesnara Group". The strong performance in 2013 is confirmation that the previous signs of recovery were real and have supported the development of a profitable new business operation.

New business premium income

New sales in the unit-linked business have shown substantial growth in 2013, with a 61.9% increase compared to 2012. A key driver of this is the recovery in IFA sentiment towards Movestic following the significant improvements in service levels when compared with prior years. The monthly trend is upwards and we expect new business growth to continue but at a more modest growth rate following the significant recovery.

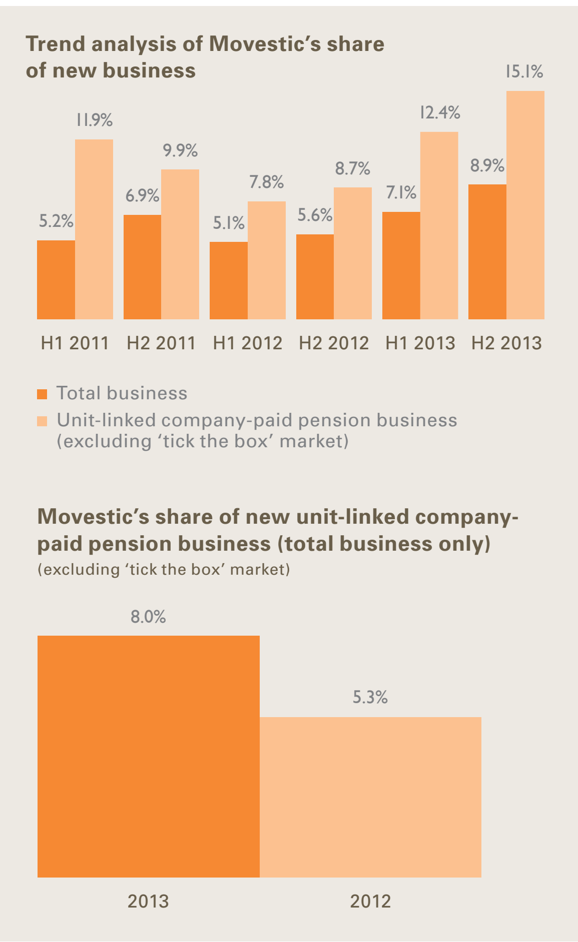
New business markets, as ever, remain challenging. Whilst some companies have continued to offer traditional investment products which have a lower risk profile and contain guarantees (which we believe to be unsustainable) we have started to see some movement to equity-linked products as a consequence of strong market performance. Further momentum in this area would have a positive impact on future new business potential.



Market share
In a mature market with low levels of overall growth, the increase in new business volumes means that the company has gained market share during the year, leading to a position within the top five suppliers in the core unit-linked company pension market. In fact during the third quarter of the year Movestic was the largest provider in terms of market share in our core unit-linked company pension market.

During the third quarter Movestic's 15.4% market share was the largest share of the unit-linked company contribution market.

This performance should be seen in the context of some of the traditional product providers having undertaken campaigns to move customers from traditional insurance contracts to 'new' unit-linked policies to address the challenges inherent in traditional guaranteed return products. Such internal switches are having an adverse distorting effect on the unit-linked market share figures from Movestic's perspective.



Development of innovative product concepts
The trend within the company-paid insurance solutions market in Sweden is to look for overall concepts where the pension plan is complemented by risk insurance products to cover the entire need for companies and their employees. Movestic's full range offering within both pension and risk products makes it possible to create such concepts and smaller variations to existing risk products packaged together with competitive pension plans, can provide the adapted solutions the market asks for.

A differentiating feature of Movestic is the carefully selected fund range which over time has proven to perform very well compared to similar offerings. The work to further develop and improve the fund range is continually given high priority.

Risks associated with the strategic objective
Economic conditions in Sweden have remained stable and it has proved to be relatively immune to economic pressures experienced across the rest of Europe. However, there remains a general sense of uncertainty that has led to consumers preferring more traditional investment products to equity-based unit-linked investments. Recent improvements in confidence and good equity market performance has led to a shift to equities and Movestic remains committed to the unit-linked market. We believe that as equity market confidence continues to recover and that as the traditional investment offerings become less sustainable for providers, there will be a gradual shift back towards unit-linked investments. New business volumes remain sensitive to market preferences and continued IFA support.

New business remains relatively concentrated towards several large IFA's. This is inevitable to some extent but the fact that Movestic has extended the breadth of IFA support in the year has reduced the concentration risk to some extent. The competitive market puts pressure on new sales margins and even though Movestic's margins have held up well, these external pressures have led to management focussing on achieving better terms in the fund operation.

BUSINESS REVIEW

3 ACQUIRE LIFE AND PENSION BUSINESSES

The acquisition of Direct Line Life (now Protection Life) during the year is a continuation of the successful acquisition track record of the Group. In addition to the direct financial benefits of the transaction, it reaffirms that Chesnara has the specialist skills, experience and reputation to complete value-adding deals in an increasingly active market.

Highlights
- Successful acquisition of Protection Life for £39.3m.
- EEV increase of £12.3m as a direct consequence of acquisition of Protection Life.
- General increase in acquisition market activity in the sector.

Review of the year
There has been a significant increase in general market activity in the UK and across Europe. The activity is due to a number of factors including larger financial organisations wishing to re-focus on core activities and the desire to release capital or generate funds from potentially capital intensive Life and Pension businesses. Chesnara has been involved in several opportunities and has progressed to various stages dependent on our view of how well the opportunities align to our assessment criteria. It is encouraging that Chesnara continues to be invited to consider many of the known opportunities which reflects well on our continued presence and credibility in the market. There is of course competition in the market and hence the completion of the acquisition of Protection Life towards the end of 2013 was particularly pleasing.

Protection Life
The Protection Life acquisition fits well with our stated strategy. It is however towards the lower end of our target value range and hence the absolute level of value enhancement is relatively modest in comparison to previous deals.

The acquisition of Direct Line Life (now Protection Life) resulted in an increase in embedded value of **£12.3m**

The level of incremental embedded value is however deemed to be attractive in the context of the funding structure for the acquisition and the risk profile of the Protection Life business:

- The transaction has been funded by a combination of bank debt and cash both of which represent a relatively low cost source of finance. We also utilised debt capacity due to pre-existing low levels of gearing and supportive debt providers.
- The Protection Life book has a low risk profile. The products are primarily straightforward term assurance policies, which are predominantly reinsured, with the matching assets being held in corporate bonds and the book being well managed by a small and effective dedicated team. The acquisition therefore has minimal impact on both the insurance and finance risk profiles of the Group.
- Whilst there is operational risk associated with the acquisition due to the planned migration of the business to our outsourcer's systems, the substantial migration experience of our outsourcing partner, the good progress made to date and the relatively simple nature of the products being migrated gives us confidence that the overall migration risk is low.

Acquisition process and approach
Chesnara is an established Life and Pensions consolidator with a proven track record. This together with a good network of contacts in the adviser community, who understand the Chesnara acquisition model and are mindful of our good reputation with the regulator, ensure we are aware of most viable opportunities in the UK and many opportunities in Europe.

We assess the financial impact of potential acquisition opportunities by estimating the impact on three financial measures namely; the cash flow of the Group, the incremental embedded value and the internal rate of return. The financial measures are assessed under best estimate and stress scenarios.

The measures are considered by the Board and Audit & Risk Committee, in the context of other non-financial measures including the level of risk, the degree of strategic fit and the opportunity of alternative acquisitions.

We engage specialists to support stringent due diligence procedures and the actual acquisition process.

Risks associated with the strategic objective
The risk of not effectively delivering this objective is two-fold. Firstly, there is the risk that Chesnara makes no further acquisitions and secondly there is the risk that we make an inappropriate acquisition that adversely impacts the financial strength of the Group. The general increase in market activity together with the momentum created by the Protection Life acquisition suggests that the risk of no further value adding acquisitions has actually reduced somewhat over the past year.

The Protection Life deal does not mean that other opportunities cannot be fully progressed should they become available.

During recent years and through the Protection Life assessment process, we have enhanced our financial projection modelling capabilities which improves the quality of financial information available to the Board. This strongly mitigates the risk of inappropriate opportunities being pursued. In addition, the increased financial strength of the Group means that any perceived risk that pressure to do a deal could result in a departure from the stringent assessment criteria will have reduced.

Acquisition outlook
We continue to see a reasonable flow of possible acquisition opportunities and assess them appropriately. The general market background is positive with, in particular, the now firm implementation date for Solvency II, leading portfolio holders and owners to review their strategic options.

BUSINESS REVIEW

4 MAINTAIN A STRONG SOLVENCY POSITION | UK AND SWEDEN

We have continued to demonstrate our commitment to maintaining a strong solvency position, with Group solvency being 194% at 31 December 2013.

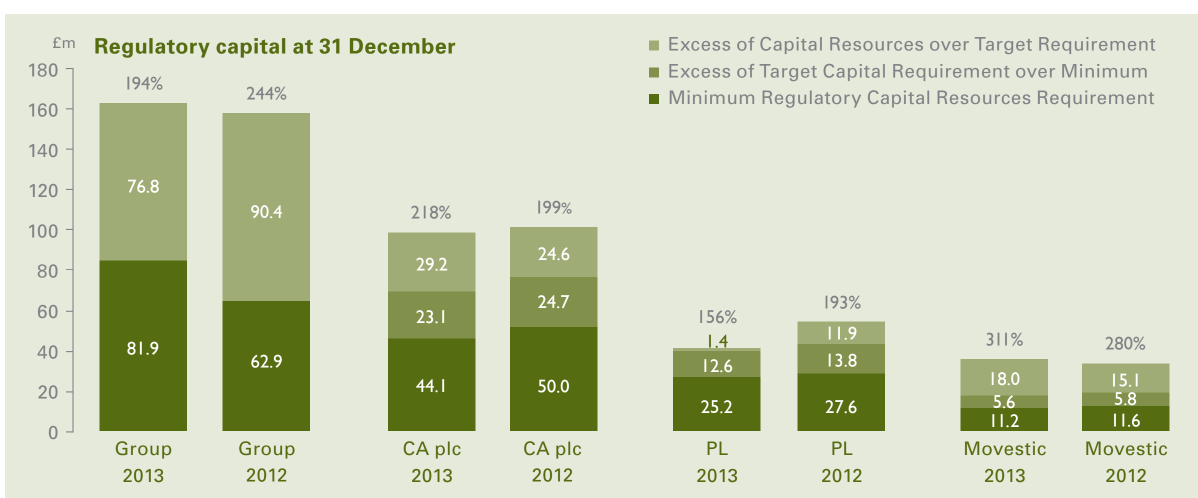
Highlights

- Group solvency continues to be strong at 194% (2012: 244%). This is stated after a proposed final dividend of £13.4m.
- The acquisition of Protection Life has had an expected adverse impact on our Group Solvency position due to it being purchased with a net worth equivalent to 100% of its regulatory capital requirements.

Objectives

One of the Group's key strategic objectives is to maintain a strong, but not excessive, solvency position. This brings a number of benefits, including supporting:

- One of our key financial management objectives of safeguarding policyholder interests.
- Delivering to the dividend expectations of our shareholders.
- Potential acquisition opportunities.
- Our ability to absorb volatility created by external economic conditions.



Notes

- The percentages in the chart above represent the excess of the capital resources over the minimum regulatory capital resources requirement.
- The target capital requirements stated above are based on the Board's internal minimum targets, and are set as follows:
  - Group – 100% of minimum regulatory capital resources requirement.
  - CA plc – 162.5% of the minimum long-term insurance capital requirement plus 100% of the resilience capital requirement.
  - PL – 150% of the minimum long-term insurance capital requirement.
  - Movestic – 150% of the capital resources requirement.
- Information in relation to PL for 2012 has been provided for illustrative purposes. Capital resources have reduced compared with 2012 as a result of distributions that were made to the previous owners prior to purchase by Chesnara.

BUSINESS REVIEW

4 MAINTAIN A STRONG SOLVENCY POSITION (CONTINUED) | UK AND SWEDEN

Group solvency (IGD)

The IGD represents the solvency of the Group, and is calculated using requirements imposed by the PRA. The IGD ratio at 31 December 2013 is 194% (2012: 244%) with the surplus having moved from £90.4m at 31 December 2012 to £76.8m at 31 December 2013. IGD is stated after foreseeable dividends of £13.4m (2012: £12.9m). The movement in IGD this year is a function of the following key items:

- **The purchase of Protection Life**; which has had a negative impact on IGD as a result of it needing to be recapitalised immediately on acquisition as a result of it being purchased with a net worth equivalent to 100% of its solvency requirement. An element of this dynamic is expected to reverse on successful completion of the Part VII transfer of the PL business into CA plc, which is expected to complete in 2014.

- **Group surplus in the year.** As reported elsewhere in the Report & Accounts the Group regulatory surplus in 2013 has been strong. This has resulted in a significant benefit to the IGD, outweighing the impact of the 2013 total dividend of £20.6m (interim dividend of £7.2m plus the proposed final 2013 dividend of £13.4m).

Solo solvency

The Board sets internal solvency targets for each of its regulated subsidiaries, which have remained unchanged when compared with the prior year. The graph on the previous page shows that the solvency positions of each regulated subsidiary continue to exceed the internal targets imposed by the Board.

- **CA plc solvency** has moved from 199% to 218%. This is stated after proposed dividends of £48.0m (2012: £40.0m), thereby showing that strong solvency is still being achieved whilst delivering strong cash flows to the Chesnara parent company.

- **Protection Life solvency** is 156% at 31 December 2013. The reduction when compared to the prior year is because prior to Protection Life being purchased dividends were paid to its previous owners such that it left net worth in the company equivalent to 100% of its solvency requirement. Post acquisition this was immediately increased to 150% by way of a capital injection of £13.1m by Chesnara plc. The Part VII transfer of Protection Life into CA plc is planned to take place during 2014 and this is expected to deliver capital efficiencies that will be reflected in the 2014 IGD. No dividends are proposed to be paid by Protection Life this year.
- **Movestic** had a solvency ratio of 311% at 31 December 2013. Whilst it has a very strong solvency ratio, Movestic does not currently pay dividends to Chesnara due to an additional liquidity constraint that is imposed by the Swedish FI.

Solvency II

The introduction of Solvency II will change the capital requirements of both the Group and its regulated subsidiaries. The final impact of Solvency II continues to be uncertain although we expect the Group impact to be manageable. Solvency II may also result in the Board re-assessing the internal targets imposed on each regulated entity. Further detail over the status of our Solvency II programme is included on page 47.

BUSINESS REVIEW

5 ADOPT GOOD REGULATORY PRACTICE AT ALL TIMES | UK AND SWEDEN

Chesnara continues to operate to high regulatory standards in both its day to day operations and its acquisition activity.

UK

Regulation and legal

As ever in this highly regulated industry there have been a number of new and ongoing initiatives that have led to various levels of attention and challenge. It is pleasing to report that none of these have given rise to significant issues. The commentary below sets out a list of the key activities during the year.

FSA

The FSA disbanded in April and was replaced by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). As a dual regulated business we maintain our commitment to maintaining a compliant operating model and a good relationship with both our regulators.

PRA

The PRA, a subsidiary of the Bank of England, focuses on prudential supervision. To assist their thematic supervisory work we have responded in a timely manner to a small number of requests for generic information, for example on asset valuation methodologies.

FCA

The FCA's focus is conduct and consumer protection. We are currently addressing rule changes on preparing product information, including new guidance to calculate inflation-adjusted illustrations for personal pensions and lower growth rates for life and pension illustrations, for implementation in April 2014.

Solvency II

With an implementation date of January 2016 now certain, planning, preparation and delivery has been re-energised. By January 2016 we will have the required models, data, processes, governance and reporting in place to be Solvency II compliant. Further information on our Solvency II project is provided on page 47.

ABI Retirement Code

During 2013 there was increasing scrutiny of the annuity market and we have continued to comply with the ABI retirement code to ensure that pension policyholders are provided with timely and clear information regarding the options available to them in the annuity market prior to vesting their pension. In his Budget announcement on 19 March, the Chancellor of the Exchequer announced significant changes which will affect pensions and the annuity market. CA plc does not have a significant exposure to annuities (having around 6,000 such arrangements) and has not sought to write such business for a number of years. Although we do have far more pensions policies (around 169,000) we do not expect any immediate and significant change to affect this book or the value of it.

Treating Customers Fairly (TCF)

We have continued to monitor performance against, and to continue the development of, our TCF measures. The results are discussed, where relevant, with our outsourcing partners and are reviewed by senior management and reported to the CA plc Board. No issues of significance have arisen.

Complaints

There has been a general downward trend in the overall volume of complaints received although we continue to receive a steady number of complaints from Complaint Management Companies in respect of endowment policies surrendered or lapsed many years ago. The Financial Ombudsman Service continues to agree with our decision on the majority of complaints referred to them for adjudication.

Policyholder investment funds

Through the auspices of the CA plc Investment Committee we have continued our oversight of policyholder funds through regular meetings with the investment managers. With them we continue to review the funds to ensure the underlying investment mix is the most appropriate for policyholders.

SWEDEN

Solvency II

Continued commitment to this project means that our progress remains in line with our plans. As the implementation date has, as widely expected, been postponed to 2016 this has given us the opportunity to review necessary progress, whilst bearing in mind that interim measures will be introduced. Therefore, we are continuing to develop the key aspects of the prospective regulations as they stand. Further information on our Solvency II project is provided on page 47.

Customer information

Movestic's legal and marketing departments have conducted a review of all the information sent to customers of savings products. This has led to more comprehensible and uniform information, which at the same time fulfils all legal requirements.

Pensions portability

The debate on the proposal to increase portability of pensions is intense in Sweden. As Movestic offers full right to transfer already, the risk for us can be described as the risk of no change. An increased right to transfer would be beneficial to Movestic as a part of the market that is now closed would become possible to approach.

FINANCIAL REVIEW

The Group's key financial performance indicators as at 31 December 2013 and for the year ended on that date demonstrate the financial performance and strength of the Group as a whole. A summary of these is shown and further analysis is provided in the following sections:

IFRS pre-tax profit

£60.6m

2012: £19.7m

What is it?

The presentation of the results in accordance with International Financial Reporting Standards (IFRS) aims to smooth the recognition of profit arising from written business over the life of insurance and investment contracts.

Why is it important?

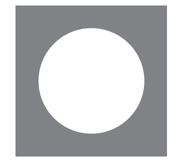
For businesses in run-off the reported profit is closely aligned with, and a strong indicator of, the emergence of surplus arising within the long-term insurance funds of those businesses. The emergence of surplus supports the payments of dividends from the regulated insurance businesses to Chesnara plc, which in turn enables the payment of dividends to our shareholders. IFRS pre-tax profit is a strong indicator of how we are performing against our stated strategic objectives to "maximise value from the in-force book" and "maintain a strong solvency position".

Highlights

- IFRS pre-tax profit of £60.6m shows a 208% improvement compared with the prior year of £19.7m.
- IFRS pre-tax profit is stated after a gain arising on the purchase of Protection Life of £2.8m.
- Profits from the core CA closed book remain significant, and have increased compared with the prior year (2013: £25.0m; 2012: £18.5m). The increase is predominantly due to investment market movements, with the core underlying product based surplus remaining resilient to book run-off. The CA surplus also reflects the impact of actuarial assumption changes, the key ones being a surplus arising from weakening mortality assumptions offset by a strengthening of our expense assumptions.
- The 2013 result includes a £36.4m profit from the S&P business. This compares favourably with the profit for 2012 of £14.6m, largely as a result of a reduction on the cost of guarantees driven by favourable investment market movements.
- There was a £1.2m improvement in the Movestic result when compared with the prior year.

Risks

The IFRS profit can be affected by a number of our principal risks and uncertainties as set out on pages 45 and 46. In particular, strong equity and property markets in 2013 coupled with positive yields on fixed interest securities have contributed to a strong IFRS pre-tax profit in the year. The corollary to this is that deteriorating markets can have a material negative impact on the IFRS pre-tax result.



Net cash generation

£36.7m

2012: £36.1m

What is it?

Net cash generation is a measure of how much distributable cash the subsidiaries have generated in the period. The dominating aspect of cash generation is the change in amounts freely transferable from the operating businesses, taking into account target statutory solvency requirements which are determined by the boards of the respective businesses. It follows that cash generation is not only influenced by the level of surplus arising but also by the level of target solvency capital.

Why is it important?

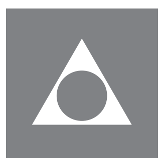
Cash generation is a key measure, because it is the net cash flows to Chesnara from its Life and Pensions businesses which support Chesnara's dividend capacity. Cash generation can be a strong indicator of how we are performing against our stated objective of "maximising value from the in-force book", although this KPI can also be negatively affected by our stated objective of "maintaining a strong solvency position".

Highlights

- At £23.6m cash generation in CA continues to be strong (2012: £15.1m).
- S&P has contributed £28.9m of operational cash generation in 2013 compared with £19.5m for 2012.
- PL has utilised cash of £11.5m. This is net of a £13.1m injection as a result of the business being purchased with net worth below the Board's stated target resources of 150% of the capital requirement. A large portion of this is expected to reverse following the planned Part VII transfer into CA plc during 2014.
- Movestic has required no capital support during the year (2012: £nil).
- Chesnara cash generation includes acquisition expenses of £2.4m as a result of acquiring PL during the year.

Risks

The ability of the underlying regulated subsidiaries within the Group to generate cash is affected by a number of our principal risks and uncertainties as set out on pages 45 to 46. Whilst cash generation is a function of the regulatory surplus, as opposed to the IFRS surplus, they are closely aligned, and therefore factors such as yields on fixed interest securities and equity and property performance contribute significantly to the level of cash generation within the Group. In addition to this, regulatory change, such as the introduction of Solvency II can also materially affect the ability of the regulated subsidiaries to generate cash.



EEV earnings, net of tax*

£82.7m

2012: £31.2m

*excluding modelling adjustments of £4.1m in 2013 (2012: £3.6m) .

What is it?

In recognition of the longer-term nature of the Group's insurance and investment contracts, supplementary information is presented in accordance with European Embedded Value 'EEV' principles.

The principal underlying components of the EEV result are:

- The expected return from existing business (being the effect of the unwind of the rates used to discount the value in-force).
- Value added by the writing of new business.
- Variations in actual experience from that assumed in the opening valuation.
- The impact of restating assumptions underlying the determination of expected cash flows.

Why is it important?

By recognising the net present value of expected future cash flows arising from the contracts (in-force value), a different perspective is provided in the performance of the Group and on the valuation of the business. EEV earnings are an important KPI as they provide a longer-term measure of the value generated during a period. The EEV earnings of the Group can be a strong indicator of how we have delivered to our strategic objectives, in particular the new business profits generated from "enhancing our value through new business in selected markets", coupled with "maximising our value from the in-force book".

Highlights

- Significant economic profit of £71.1m (2012: £21.5m).
- Decrease in operating profit to £6.6m (2012: £14.6m).
- Movestic has generated a £15.0m EEV profit, which includes the adverse impact of a further strengthening of lapse assumptions during the year.
- Movestic has generated a new business contribution of £7.2m in the year (2012: £2.6m).
- One off profit arising on acquisition of Protection Life amounting to £12.3m.

Risks

The EEV earnings of the Group can be affected by a number of factors, including those highlighted within our principle risks and uncertainties as set out on pages 45 and 46. In addition to the factors that affect the IFRS pre-tax profit and cash generation of the Group, the EEV earnings can be more sensitive to other factors such as the expense base and persistency assumptions. This is primarily due to the fact that assumption changes in EEV affect our long-term view of the future cash flows arising from our books of business.

EEV

£376.4m

2012: £311.1m

What is it?

The European Embedded Value (EEV) of a life insurance company is the present value of future profits, plus adjusted net asset value. It is a construct from the field of actuarial science which allows insurance companies to be valued.

Why is it important?

As the EEV takes into account expected future earnings streams on a discounted basis, EEV is an important reference point by which to assess Chesnara's market capitalisation. A life and pensions group may typically be characterised as trading at a discount or premium to its embedded value. Analysis of EEV, distinguishing value in-force by segment and by product type, provides additional insight into the development of the business over time.

The EEV development of the Chesnara Group over time can be a strong indicator of how we have delivered to our strategic objectives, in particular the value created from acquiring life and pensions businesses and enhancing our value through new business in selected markets.

Highlights

- £85.4m increase in EEV before recognition of dividend payments. This is driven by strong investment market performance during the year contributing to the result, coupled with a gain of £12.3m arising on the acquisition of PL.
- Model enhancements generated a £4.1m increase in EEV in the year (2012: £3.6m). These related entirely to the Movestic business.
- A slight weakening of Swedish Krona against Sterling has contributed to a £1.4m decrease in embedded value in the year.
- Good balance of EEV across the operating segments.
- Good product diversification within the value in-force.

Risks

The Embedded Value of the Group is affected by economic factors such as equity and property markets and yields on fixed interest securities. In addition to this, whilst the other KPIs (which are all "performance measures") remain relatively insensitive to exchange rate movements (largely due to the proportion of IFRS pre-tax profit generated by Movestic compared with the other UK businesses) the EEV of the Group can also be materially affected by exchange rate fluctuations between Swedish Krona and Sterling. For example a 10% weakening of exchange rates between Swedish Krona and Sterling would reduce the EEV of the Group by 3%, based on the composition of the Group's EEV at 31 December 2013.

FINANCIAL REVIEW

IFRS pre-tax profit

£60.6m 2012: £19.7m

Executive summary

The IFRS results by business segment reflect the natural dynamics of each line of business. In summary the current financial model has three major components which can be characterised as: the "stable core", the "variable element", and the "growth operation". The results and financial dynamics of each segment are analysed further as follows:

Stable core

At the heart of surplus, and hence cash generation, is the CA business which is in run-off. During 2013 this has been supplemented as a result of the purchase of the Protection Life business, which, whilst not contributing significantly to the 2013 result as a function of the timing of the purchase, is a complementary addition to the stable core of the UK business.

The requirements of the CA and PL books are to provide a predictable and stable platform for the financial model and dividend strategy. As a closed book, the key is to sustain this income source as effectively as possible. The IFRS results during the year support this objective, with product-based deductions from CA of £28.7m continuing to emerge in a predictable fashion and at a level that compares favourably with 2012 (£26.3m). This level of product-based deductions has underpinned CA's ability to generate a significant level of IFRS pre-tax profit at £25.0m (2012: £18.5m). Assets under management within the CA segment have grown by 6.0%, from £1,638m to £1,736m, in the year. The PL segment, having only been owned for a month, contributed a modest IFRS surplus of £0.2m during 2013.

Further detail of the results of the CA and PL segments can be found on page 31 and 32 respectively.

Variable element

The S&P component brings an element of earnings volatility to the Group, with the results being particularly sensitive to investment market movements. This is illustrated by a material reduction in the reserve for costs of guarantees since the start of the year, giving rise to a £28.5m economic benefit to the result during the year, £8.5m of which was driven by investment market movements, with £20.0m arising from changes to the yield curve. For 2012 this same dynamic gave rise to a £2.5m surplus contribution, with investment market movements contributing £9.0m, offset by £6.5m negative movements as a result of changes in the yield curve. Product based deductions continue to remain strong, at £17.1m (2012: £16.9m).

Further detail of the results of the S&P segment can be found on page 32.

Growth operation

Movestic has posted an IFRS profit of £2.6m during the year (2012: £1.4m), a pleasing result showing that the results continue to trend in the right direction. The long-term financial model is based on growth, with levels of new business being targeted to more than offset the impact of policy attrition, leading to a general increase in assets under management and, hence, management fee income. There has been an increase in funds under management of 24.1% (on constant exchange rates) since 31 December 2012.

The Movestic result in 2013 is stated after an adverse DAC asset adjustment of £3.0m, predominantly arising from refinements to the DAC amortisation model that were made during the year. The impact on the Group IFRS results of this adjustment is muted as a large proportion of the adjustment (£2.6m) relates to DAC on policies that were in force on acquisition, and this is not recognised in the Group IFRS balance sheet.

Further detail of the results of the Movestic segment can be found on page 33.

IFRS results

The financial dynamics of Chesnara, as described above, are reflected in the following IFRS results:

Year ended 31 December	2013 £m	2012 £m	Note
CA	25.0	18.5	
S&P	36.4	14.6	2
PL	0.2	–	
Movestic	2.6	1.4	
Chesnara	(4.9)	(5.8)	3
Consolidation adjustments	(1.5)	(4.2)	
Total profit before tax and exceptional item	**57.8**	**24.5**	
Profit arising from PL acquisition	2.8	–	1
Exceptional tax item	–	(4.8)	4
Total profit before tax	**60.6**	**19.7**	
Tax	(11.2)	8.2	4
Total profit after tax	**49.4**	**27.9**	

Note 1 – The Group profit before tax is stated after recognition of a £2.8m gain arising as a result of the purchase of Protection Life. More detail over how the gain was calculated has been provided in Note 7 to the IFRS Financial Statements.

Note 2 – The S&P results for the year include a £28.5m surplus arising from the reduction in reserves held for products with guarantees. The reduction is driven by favourable asset growth and bond yield movements.

Note 3 – The Chesnara result represents holding company expenses. For 2013 this includes the impact of £1.6m of costs expensed during the year that were incurred in relation to the purchase of Protection Life.

Note 4 – The tax charge for 2013 is not affected by any significant one-off items. As explained in Note 5 to the IFRS financial statements, an exceptional item of £4.8m was reported in 2012 relating to the reclassification of policyholder tax liabilities within the S&P segment has been charged to IFRS profits. There is a corresponding deferred tax release of £4.8m included in the tax item above. The net of tax impact of these adjustments, which were made to align the treatment within the S&P segment with that within the CA segment, is accordingly £nil.

Consolidation adjustments

The adjustments arising on consolidation are analysed below:

Year ended 31 December	2013 £m	2012 £m	Note
CA – Amortisation of AVIF	(2.2)	(2.8)	
S&P – Amortisation of AVIF	(0.8)	(0.8)	
PL – Amortisation of AVIF	(0.2)	–	
Movestic:			
Amortisation of AVIF	(4.4)	(4.0)	
Write back of DAC	6.1	3.4	1
Total	1.7	(0.6)	
Total	**(1.5)**	**(4.2)**	

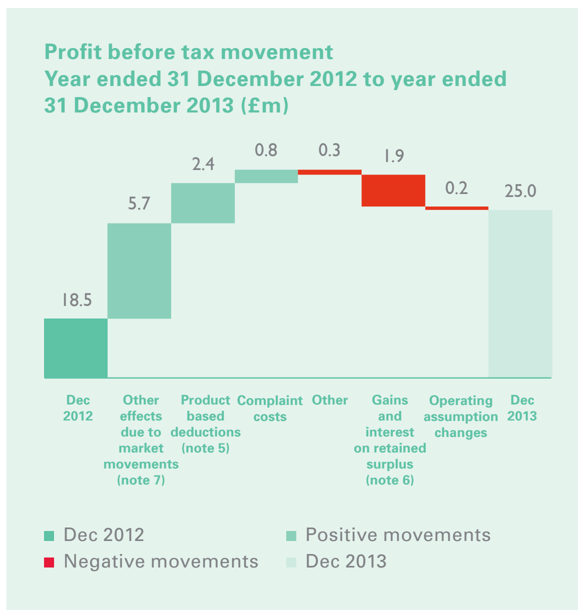
Note 1 – Included within consolidation adjustments is an item in relation to Movestic that reverses the amortisation charge on DAC relating to policies that were written prior to Chesnara ownership. This adjustment has increased in the year due to the additional charge that was booked in the year as a result of the refinements made to the DAC amortisation model. See page 33 for further detail.

The IFRS results by business segment are analysed in more detail as follows:

CA

A slight increase in product-based deductions, the core source of IFRS earnings, together with the impact of investment markets has contributed to an increase in the overall CA IFRS result as compared with the prior year. There are a number of complex aspects to the IFRS result but the primary drivers of this increase is the impact of market movements compared with the prior year, as illustrated below:

Profit before tax movement
Year ended 31 December 2012 to year ended 31 December 2013 (£m)



The key components of the 2013 IFRS result are summarised as follows:

Pre-tax IFRS profit	2013 £m	2012 £m	Note
Product-based deductions	28.7	26.3	2
Administration expenses	(7.0)	(7.6)	2
Gains and interest on retained surplus	3.5	5.4	
Operating assumption changes	(1.7)	(1.5)	3
Other effects due to market movements	3.3	(2.4)	
Complaint costs	(1.5)	(2.3)	4
Other	(0.3)	0.6	
Total	**25.0**	**18.5**	

Note 2 – Product-based deductions and returns on retained surplus remain significantly in excess of recurring administration expenses. The total level of product-based deductions has increased slightly when compared with the prior year despite the run-off of the book.

Note 3 – Operating assumption changes contain a number of items relating to the impact of certain assumption changes that were made during the year. In particular this includes a £7.5m strain arising from strengthening our expense assumptions following a management review of likely future expenses, offset by the positive effect of a £4.0m surplus arising from weakening our mortality assumptions, which has reduced the reserves held on our annuity business.

Note 4 – During the year ended 31 December 2012 complaint costs included the impact of the strengthening of the mortgage endowment mis-selling reserve. Some further strengthening has been made during 2013.

Note 5 – Product-based deductions continue to remain strong and are a core source of profit. The deductions during 2013 exceeded 2012 by £2.4m primarily driven by higher policyholder tax deductions.

Note 6 – Gains and interest on the retained surplus has fallen when compared with 2012, driven by a fall in bond values during the year.

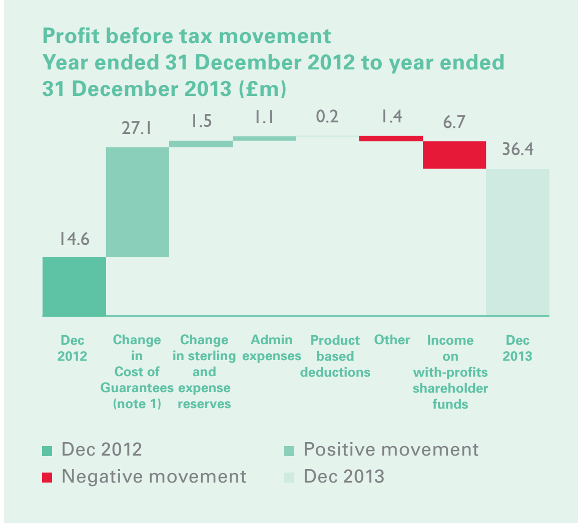
Note 7 – The impact of market movements on the result during 2013 is £5.7m higher than it was during 2012. This is primarily driven by asset mismatching contributing a positive impact of £4.0m during the year, in contrast with this same dynamic having a negative effect of circa £1.0m during 2012.

FINANCIAL REVIEW

IFRS PRE-TAX PROFIT (CONTINUED)

S&P

The S&P pre-tax profit has increased significantly compared with the prior year:



S&P posted a pre-tax IFRS profit of £36.4m for year, the key components of the result being:

Pre-tax IFRS profit	2013 £m	2012 £m	Note
Product based deductions	17.1	16.9	1
Administration expenses	(9.9)	(11.0)	1
Income on with-profits shareholder funds	(0.4)	6.3	2
Change in cost of guarantees in with-profit funds:			3
Investment market movements	8.6	9.0	
Change in yield curve	19.9	(6.5)	
Lapse experience	(3.7)	(3.3)	
Other	(0.4)	(1.9)	
Total	24.4	(2.7)	
Change in sterling and expense reserves	5.4	3.9	4
Other	(0.2)	1.2	
Total	36.4	14.6	

Note 1 – Product-based deductions have held up well as the book runs-off. These are supported by assets under management, which have increased from £1,089m to £1,113m in the year, driven by strong investment markets. Product deductions exceed administration expenses by £7.2m and £5.9m in 2013 and 2012 respectively.

Note 2 – The income on with-profits shareholder funds is driven by investment market performance. The 2013 result includes the impact of the reduction in bond values that has been witnessed during the year which did not occur during 2012.

Note 3 – During the year the impact of movements in reserves for the cost of guarantees was positive, resulting in a £24.4m benefit to the IFRS result (2012: £2.7m loss). The key drivers of this benefit in 2013 were a combination of increases in bond yields and increases in equity values during the year. Included within the change in the costs of guarantees is a lapse experience loss of £3.7m, driven by observed lapses being slightly less than assumed at the start of the year.

Note 4 – Sterling and expense reserves are sensitive to both the expense base and to investment market movements. As investment markets improve, the level of sterling reserves (which provide against situations where future policy-based revenue does not cover future administration costs) reduces. The profit of £5.4m in the year is predominantly driven by investment market movements.

PL

The purchase of PL was completed on 28 November 2013 and therefore the contribution to the Group IFRS profit, being £0.2m in 2013, is small.

As referred to above the acquisition of PL resulted in a one-off gain on acquisition of £2.8m.

Movestic

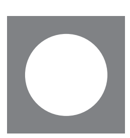
Pre-tax IFRS profit	2013 £m	2012 £m	Note
Pensions and Savings, before impact of DAC model change	2.2	(0.3)	1
Risk and health	2.2	0.9	2
Other	1.2	0.8	3
Total profit before impact of DAC model change	5.6	1.4	
Impact of DAC model change	(3.0)	–	4
Total profit before tax	**2.6**	**1.4**	

Note 1 – The Pensions and Savings business model is directly dependent upon fees and rebates earned on funds under management (FUM). The average FUM has increased during the year resulting in a £2.8m (13.5%) increase in fee and rebate income. This is partly offset by a £1.4m (7.7%) increase in expenses and brokerage fees. Reinsurance financing costs have also made a positive contribution to the year on year improvement, having reduced by £1.2m in the year.

Note 2 – The Risk and Health business, although not the core target growth operation, is significant to the Movestic financial and operating model. Unlike the longer-term Pension and Savings business the Risk and Health business tends to be cash generative in the short-term, thereby providing a source of internal funding. The Risk and Health business is operationally significant due to the size of the book, there being 363,000 short-term policies in force as at 31 December 2013 (2012: 404,000), which generated £39.3m of gross annual premiums in the year (2012: £36.0m). The Risk and Health business uses reinsurance arrangements which contain profit share elements. During the year the results benefited from profit share income of £1.2m. This was principally as a result of the strong technical profit in Modernac, Movestic's associate.

Note 3 – The "Other" component includes the results of the associate, Modernac, Movestic investment income and the impact of fair value adjustments to the Financial Reinsurance liability. The Modernac results have remained consistent year on year, at £1.3m. The financial reinsurance fair value adjustment for the year has generated a £0.9m loss compared with a £0.6m loss for 2012. All of these movements are predominately a consequence of investment market conditions.

Note 4 – During 2013 a review of the amortisation model that was used for spreading the costs of acquiring new policies was performed. As a result of this review the model was updated to provide more granular information and has resulted in the requirement, for certain policies underwritten in certain years, to shorten the period over which these costs are spread. This has resulted in a one-off accelerated DAC charge of £3.0m. A large proportion of this DAC amortisation charge related to polices that were in force when Movestic was purchased by Chesnara, and therefore the Group IFRS result only reflects £0.3m of this charge, this being the element of the charge that relates to policies that were written post acquisition. This is because the DAC at acquisition was written off as part of the acquisition accounting process, having been replaced by an intangible AVIF asset.



FINANCIAL REVIEW

Net cash generation

£36.7m 2012: £36.1m

The Group's cash flows are generated principally from the interest earned on capital, the release of excess capital as the life funds run down, policyholder charges and management fees earned on assets under management.

This information illustrates that gross and net cash generation within the Group continues to be robust. Key aspects underpinning the outcome are:

Highlights

- Gross cash generation in the UK run-off businesses has increased by £15.7m in the year compared with 2012, driven by more favourable investment markets driving the surplus.
- Net cash generation has benefitted from a one-off release from Save & Prosper. This is offset by the adverse impact of restricted surplus in the SPP with-profit fund (see note 3).
- As expected the acquisition of Protection Life has had a short-term adverse impact on net cash generation as a result of a day one capital injection being required to increase the capital resources to 150% of the minimum regulatory capital requirement. As can be seen from the table to the right, £1.6m of cash has been generated by PL since acquisition to offset this.
- The pause in Movestic funding has continued, with no additional funding being required in 2013 (2012: £nil).

The Group's closed life funds provide predictable fund maturity and liability profiles, creating stable long-term cash flows for distribution to shareholders and for repayment of outstanding debt. Cash flow generation will ultimately naturally decline over time as the UK businesses run-off. Despite this natural downward pressure there was an increase in cash generation in 2013 when compared with 2012.

Although investment returns are less predictable, a significant portion of the investment risk is borne by policyholders. However, the S&P segment continues to demonstrate short-term volatility. This arises from the impact of investment market movements and the cost to shareholders of guarantees within the S&P with profits funds. Although the short-term measure of this cost follows the fortunes of investment markets, we proactively manage the risk taking a longer-term perspective.

The following table identifies the source of internal net cash generation within the Group, representing the net change in funds available to service debt (interest and loan principal repayment) and equity (dividends):

Year ended 31 December Cash generated from/(utilised by):	2013 £m	2012 £m	Note
CA			
Surplus and profits arising in the year	20.4	13.4	
Change in target capital requirement	3.2	1.7	
S&P			
Surplus and profits arising in the year	25.1	14.4	
Change in target capital requirement	4.3	5.4	
Decrease in policyholder funds cover for target capital requirement	(0.5)	(0.3)	
PL			
Surplus and profits arising in the year	0.2	–	
Change in target capital requirement	1.4	–	
Movestic			
Additional capital contributions	–	–	
Chesnara			
Cash utilised by operations	(4.4)	(0.6)	
Total gross cash generation	**49.7**	**34.0**	
Items affecting ability to distribute cash			
Synergistic effects of Part VII transfer	–	7.0	1
PL capital injection	(13.1)	–	2
Release of capital from S&P WP fund	15.5	–	3
Restricted surplus in S&P WP fund	(15.4)	(4.9)	3
Net cash generation available for distribution	**36.7**	**36.1**	**4**

Items affecting the cash available for distribution:

Note 1 – As a result of the S&P Part VII transfer in 2011 we were able to de-regulate the S&P companies in 2012 thereby releasing £7m of capital.

Note 2 – PL was acquired at a solvency level lower than the target requirement. An immediate capital injection was made which has an impact on net cash available for distribution.

Note 3 – An element of the statutory surplus in the year emerges in the S&P WP fund. In the absence of management action the majority of the surplus is not available for distribution and the net cash generated recognises this restriction. Periodically Chesnara, with regulatory approval, can apply a waiver to release some of the previously restricted surplus within S&P. This process was undertaken during 2013 resulting in a £15.5m capital release.

Note 4 – The net cash generation KPI is a useful indicator of the dividend paying capacity of the Group's regulated subsidiaries. This is monitored closely by Management as cash generated by the Group's regulated subsidiaries is used by the Chesnara Parent Company for corporate transactions such as the servicing of debt, payments of dividends and the funding of future acquisitions. It should be noted that this KPI is quite distinct from the Group's Cash Flow Statement as included in the Group's IFRS Financial Statements, which is intended to reflect the movement in cash held by Chesnara and its subsidiaries but does not reflect that most of the subsidiary cash balances are held in regulated insurance funds and are therefore not available for use by the Parent Company.

FINANCIAL REVIEW

EEV earnings*

£82.7m

2012: £31.2m

*excluding modelling adjustments

EEV result

Summary

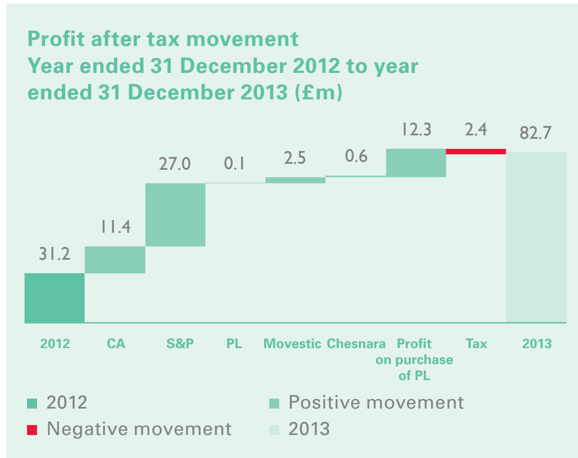
The headline EEV result has improved significantly during the year. The improvement relates directly to investment market conditions. The results benefit from both economic experience and assumption profits, which are driven predominately from equity market growth and an increase in the yield curve.

The EEV operating profit of covered business of the Group has reduced from £19.0m in 2012 to £8.9m in 2013. The reduction is primarily due to the 2012 comparatives including some £13m due to positive assumption changes relating to broker and fund manager rebates in Movestic that have not been replicated to the same degree during 2013. Excluding this there has been an underlying increase from £6.0m to £8.9m.

A significant proportion of the operating profit is also directly the result of investment market movements. The return on shareholder net worth loss of £0.3m reflects a reduction in bond capital values. During 2012 reducing bond yields contributed to a corresponding £7.9m profit.

The following tables analyse the Group EEV earnings after-tax by source and by business segment:

Profit after tax movement
Year ended 31 December 2012 to year ended 31 December 2013 (£m)



Analysis of the EEV result in the year by business segment

	2013 £m	2012 £m
CA	24.5	13.1
S&P	42.7	15.7
Movestic	15.5	13.0
PL	0.1	–
Chesnara	(5.1)	(5.7)
Profit before tax and gain on acquisition	**77.7**	**36.1**
Gain on acquisition of Protection Life	12.3	–
Profit before tax	**90.0**	**36.1**
Tax	(7.3)	(4.9)
Profit after tax	**82.7**	**31.2**

Analysis of the EEV result in the year by earnings source

	2013 £m	2012 £m
New business contribution	7.9	2.9
Return from in-force business		
Expected return	5.5	5.8
Experience variances	5.8	0.4
Operating assumption changes	(10.0)	2.0
Return on shareholder net worth	(0.3)	7.9
Operating profit of covered business	**8.9**	**19.0**
Variation from longer term investment return	54.7	28.0
Effect of economic assumption changes	16.4	(6.5)
Profit on covered business before tax and before gain on acquisition	**80.0**	**40.5**
Tax	(7.6)	(6.0)
Profit on covered business after tax and before gain on acquisition	**72.4**	**34.5**
Gain on acquisition of Protection Life	12.3	–
Uncovered business and other group activities	(2.3)	(4.4)
Tax on uncovered business	0.3	1.1
Profit after tax	**82.7**	**31.2**

Economic conditions

As indicated above, the EEV result is sensitive to economic conditions. Economic experience and assumption changes contributed a profit of £71.1m in the year compared with a profit of £21.5m for 2012. The results are sensitive to both equity markets and bond yields (further sensitivity analysis is provided in Note 7 of EEV Supplementary Information). Economic assumption changes are dominated by bond yield movements, which following a period of decline during 2012, have increased relatively sharply during 2013. The "variation from longer term investment return" profit is predominantly due to continued equity market growth. The impact of these effects on each operating segment is illustrated below:

Economic experience and assumption changes	2013 £m	2012 £m
CA	18.7	4.7
S&P	33.9	8.3
PL	–	–
Movestic	18.4	8.5
Total	**71.1**	**21.5**

The S&P profit in 2013 includes the impact of a reduction in the estimate of costs on products with guarantees of some £21.0m, coupled with the positive impact of bond yield increases across the rest of the book.

FINANCIAL REVIEW

EEV EARNINGS (CONTINUED)

As can be seen on the previous page the CA segment has benefitted from positive economic conditions, with profits improving by £14.0m compared with 2012. In particular favourable tax deductions and movements in tax liabilities that are a direct result of investment market performance have significantly contributed to the economic experience in the year. Off-setting this are adverse economic assumption changes of £3.6m.

The Movestic business is sensitive to movements in equity markets due to its core income stream being dependent upon management charges levied on funds under management, which are primarily equity-based. Of the £18.4m economic profit, £20.8m relates to equity growth in the year. Off-setting against this is an adverse economic assumption change of c £2.4m. This is driven by a number of factors, including the effect of inflation on future expenses.

New business contribution

The new business contribution relates primarily to the Movestic Pensions and Savings business. Movestic also writes Risk and Health policies, but due to its more short-term nature the Risk and Health business is reported as uncovered business and hence does not contribute to the new business result. The Movestic contribution is £7.2m, of which £2.7m relates to the value of premium increments received on existing policies. Profits on "new contract" business of £4.5m, compared with the 2012 equivalent of £0.2m. The recent recovery is due to a 61.9% increase in new business volumes following the rectification of the 2012 servicing issues that arose from a 2011 systems migration.

Experience variances	2013 £m	2012 £m
CA	7.6	5.2
S&P	4.7	3.1
PL	–	–
Movestic	(6.5)	(7.9)
Total	**5.8**	**0.4**

The CA favourable variances relate to policy persistency and mortality experience being better than assumed. The S&P favourable variances in 2013 relate principally to policyholder tax deductions and better than assumed expense and lapse experience.

The Movestic experience variance includes expense and commission overruns of some £2.7m coupled with the net adverse impact of a number of other experience variances such as changes to rebate levels, changes in investment mix and changes to certain policyholder funding structures. Off-setting this is a small positive persistency profit of £0.5m, which compares favourably with the 2012 loss of £6.0m. This would be expected given that persistency assumptions were further strengthened during the first half of 2013, the impact of which is included in the operating assumption changes.

Operating assumption changes

Operating assumption changes	2013 £m	2012 £m
CA	(4.3)	(0.3)
S&P	4.5	(2.9)
PL	–	–
Movestic	(10.2)	5.2
Total	**(10.0)**	**2.0**

The CA segment operating assumption change loss of £4.7m is predominantly driven by the positive effect of lapse and mortality assumptions being weakened during the year resulting in a profit of £5.5m, offset by a £10.0m adverse impact due to expense assumptions being strengthened, of which £7.5m arises as a result of further assessment of potential future administration expenses.

The S&P segment includes an operating assumption change profit of £4.4m arising from changes to expense assumptions. This is driven by reduced forecast governance overhead costs as a result of reduced property spend coupled with a reduction in salary spend. The 2012 result reflected a loss of £3.7m following a change in lapse assumptions. This has not been repeated this year.

Movestic has reported an operating assumption change loss of £10.2m, compared with a £5.2m positive operating assumption change profit in 2012. The loss in the year includes the impact of the aforementioned persistency assumption strengthening, contributing an adverse variance of some £6.0m. In addition, increases in maintenance expense assumptions have resulted in a further negative assumption change loss of £2.6m. During 2012 the Movestic long-term persistency assumptions were strengthened, with a total adverse impact of £7.9m. This was more than offset by positive assumption changes relating to broker and fund manager rebates totalling some £13.0m.

Gain on acquisition of Protection Life

The EEV results for the year includes the impact of one-off gain of £12.3m arising from the purchase of Protection Life. Further detail is provided in Note 9 to the EEV supplementary information.

Uncovered business and other group activities

Uncovered business and other group activities	2013 £m	2012 £m
Chesnara	(5.0)	(5.7)
Movestic	2.7	1.3
Total	**(2.3)**	**(4.4)**

The result includes Chesnara parent company costs relating to corporate governance and business development, not attributable to the covered business. The 2013 expense is reflective of the steady state cost base coupled with the costs incurred associated with the purchase of PL, which amounted to £2.4m, £1.6m of which has been reported as an expenses, with the remainder relating to loan arrangement fees, which are being spread over the life of the loan. The 2012 comparison included a £2.5m one-off increase in a provision to cover future contractual property costs associated with the Group Head Office.

The Movestic result is impacted by:

i) Risk and Health results: This business is less long-term in nature and hence is not modelled as covered business. Profit of £2.2m is £1.3m higher than the prior year profit of £0.9m.

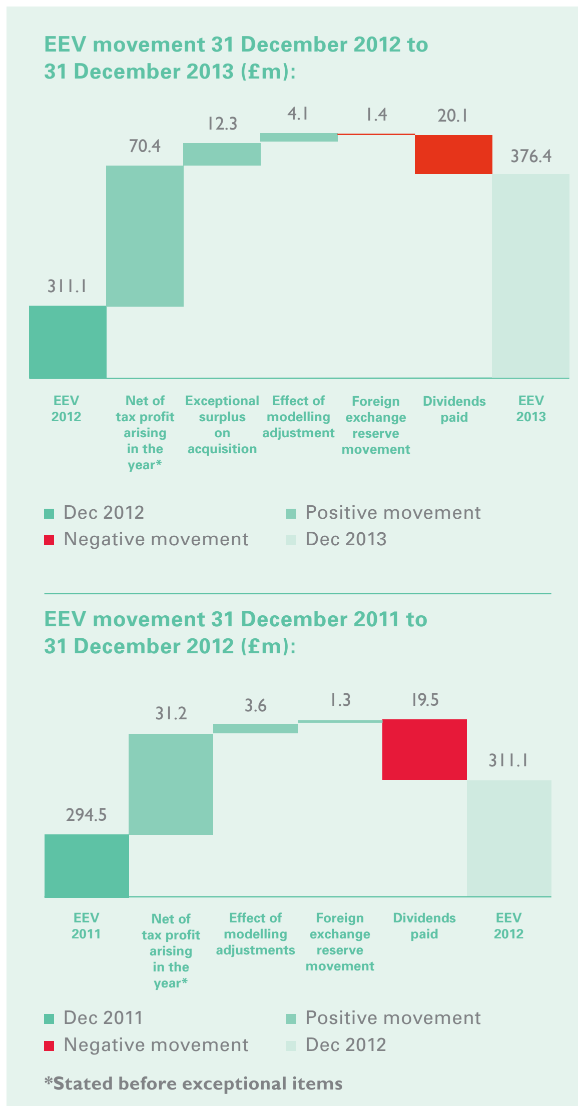
ii) Profit from the Modernac associate, which at £0.9m for 2013 has decreased slightly compared with a profit of £1.2m for 2012.

FINANCIAL REVIEW

European Embedded Value

£376.4m

2012: £311.1m



Summary

The EEV of the Chesnara Group represents the present value of the estimated future profits of the Group plus an adjusted net asset value. Movements between different periods are a function of the following components:

- Net of tax profit arising in the year, pre exceptional items;
- Exceptional items, such as:
  - the surplus arising on the acquisition of Protection Life; and
  - Modelling adjustments;
- Foreign exchange movements arising from retranslating the EEV of Movestic into Sterling; and
- Dividends that are paid in the year.

More detail behind each of these components has been provided below:

Net of tax profit

The EEV profit arising during the year is analysed in more detail within the preceding section.

Exceptional surplus on acquisition

The purchase of Protection Life has resulted in a surplus arising on acquisition of £12.3m. The surplus has arisen because the EEV of Protection Life at the acquisition date amounted to £51.6m, which is £12.3m higher than the purchase price of £39.3m.

Effect of modelling adjustments

Year ended 31 December 2013

Modelling adjustments during the year have reduced when compared with those included in the prior year.

Positive modelling adjustments this year of £4.1m relate entirely to the Movestic business. These have arisen due to refinements being made to the way in which modelling of commission is performed, which is now performed at a more granular level.

Year ended 31 December 2012

The modelling adjustments that were reported during 2012 included more materially individual items, contributing to an increase in EEV of £3.6m, comprising:

Movestic

As a result of a review of the model during 2012 the following adjustments were reflected in the EEV at 31 December 2012:

i) Levels of commission claw-back within the future cash flow projections were overstated by £7.9m; and

ii) Several enhancements to policy fee cash flow estimates and data input routines were identified with a total net adverse impact of £1.1m.

UK

The CA and CWA EEV models previously assumed a single average rate of investment return for all durations as opposed to the use of a full yield curve. As at 31 December 2012 the models were enhanced to recognise differing rates of return across the different durations of the yield curve, resulting in a net of tax increase of £12.6m.

Foreign exchange reserve movements

The £1.4m foreign exchange reserve movement during 2013 has arisen as a result of a slight weakening of the Swedish Krona against Sterling by 0.6% since the end of 2012.

Dividends paid

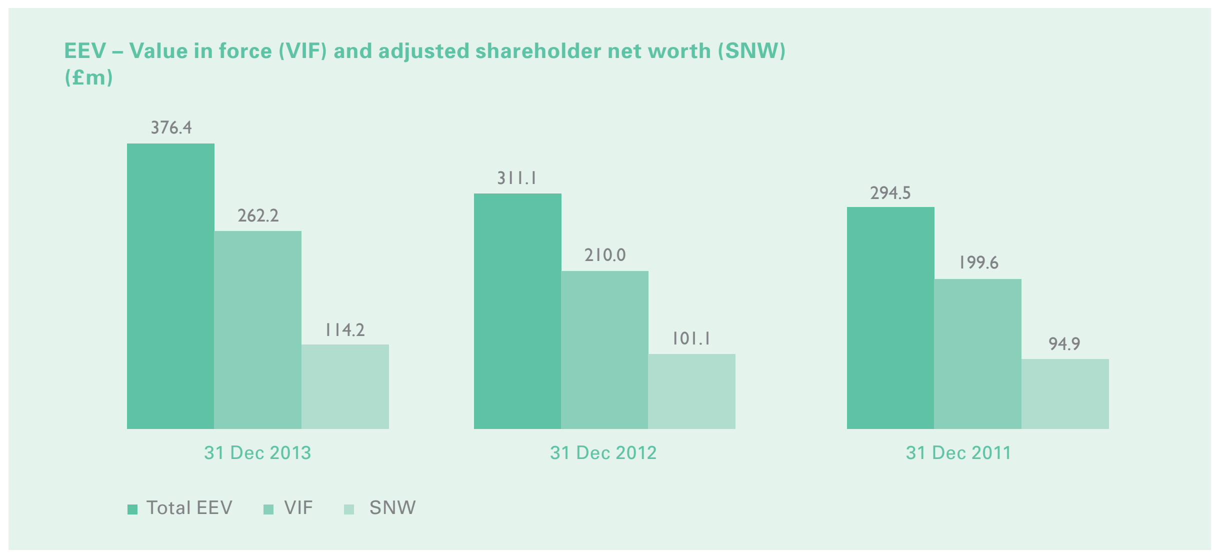
Dividends of £20.1m were paid during 2013, being the final dividend from 2012 of £12.9m and the interim dividend from 2013 of £7.2m.

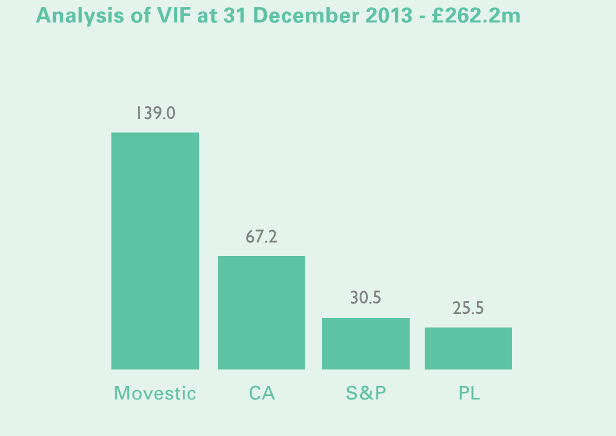
FINANCIAL REVIEW

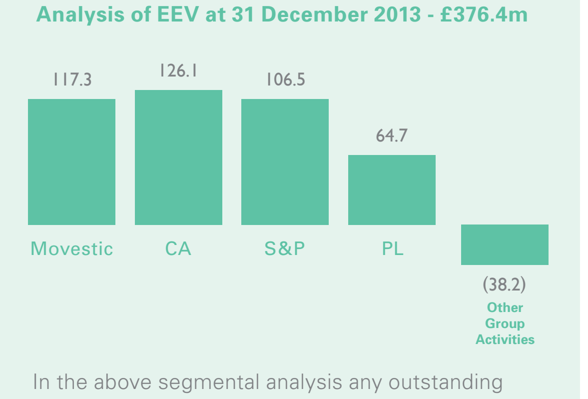
EUROPEAN EMBEDDED VALUE (CONTINUED)

Analysis of EEV

The information on this page provides some further analysis of the EEV of the Group, both in terms of the split between different operating segments and also the split between the adjusted shareholder net worth and the value of the in-force (VIF) business. The adjusted shareholder net worth represents the IFRS net worth of the Group, but adjusted for items that are measured differently under EEV measurement rules and the VIF represents Management's best estimate of the present value of the future profits that will arise out of each book of business.







In the above segmental analysis any outstanding debt in relation to the S&P and PL acquisitions is included in "Other Group Activities".

Highlights

- There is a good balance in EEV across the core business segments, with the UK businesses representing the majority (79.0%) of the total EEV, which includes the supplementary addition of the Protection Life business during the year. The value in-force component is dominated by the Swedish business which represents 53.0% of the total Group VIF.
- The Group EEV includes £64.7m in relation to Protection Life. Offsetting this is the reduction in the EEV in "Other Group Activities", primarily due to the purchase price and one-off capital injection relating to this acquisition.
- There is a significant level of product diversification within the VIF. When adjusted to recognise the impact of the S&P cost of guarantees which are predominantly pension contract related, 61.8% of the total product level value in-force relates to pension contracts, 24.5% to protection business and 10.9% to endowments.

Analysis of VIF by policy type

The tables below set out the value of in-force business by major product line at each year end. Analysis of the composition of the VIF by business and major product category provides a useful insight into the commercial dynamics underpinning the value of Chesnara.

31 December 2013	Number of policies					Value of in-force business				
	CA 000's	S&P 000's	PL 000's	Movestic 000's	Total 000's	CA £m	S&P £m	PL £m	Movestic £m	Total £m
Endowment	34	4	–	11	49	24.1	2.9	–	8.0	35
Protection	40	4	146	–	190	46.2	3.9	36.0	–	86.1
Annuities	6	–	–	–	6	4.0	1.1	–	–	5.1
Pensions	44	123	–	82	249	29.7	44.6	–	140.0	214.3
Other	3	11	–	–	14	3.9	4.9	–	–	8.8
Total at product level	**127**	**142**	**146**	**93**	**508**	**107.9**	**57.4**	**36.0**	**148.0**	**349.3**
Valuation adjustments:										
Holding company expenses						(6.5)	(3.4)	–	(8.9)	(18.8)
Other						(16.5)	(21.2)	–	–	(37.7)
Cost of capital/ frictional costs						(1.0)	(2.3)	(4.0)	(0.1)	(7.4)
Value in-force pre-tax						**83.9**	**30.5**	**32.0**	**139.0**	**285.4**
Taxation						(16.7)	–	(6.5)	–	(23.2)
Value in-force post-tax						**67.2**	**30.5**	**25.5**	**139.0**	**262.2**

31 December 2012	Number of policies					Value of in-force business				
	CA 000's	S&P 000's	PL 000's	Movestic 000's	Total 000's	CA £m	S&P £m	PL £m	Movestic £m	Total £m
Endowment	39	5	–	12	56	27.7	3.8	–	8.1	39.6
Protection	43	5	–	–	48	49.2	3.7	–	–	52.9
Annuities	6	–	–	–	6	7.8	0.9	–	–	8.7
Pensions	46	128	–	78	252	33.6	55.0	–	124.2	212.8
Other	3	12	–	–	15	3.2	3.3	–	–	6.5
Total at product level	**137**	**150**	**–**	**90**	**377**	**121.5**	**66.7**	**–**	**132.3**	**320.5**
Valuation adjustments:										
Holding company expenses						(7.0)	(3.9)	–	(7.7)	(18.6)
Other						(28.6)	(41.8)	–	–	(70.4)
Cost of capital/ frictional costs						(1.1)	(2.4)	–	(0.1)	(3.6)
Value in-force pre-tax						**84.8**	**18.6**	**–**	**124.5**	**227.9**
Taxation						(17.8)	–	–	–	(17.8)
Value in-force post-tax						**67.0**	**18.6**	**–**	**124.5**	**210.1**

The value-in-force represents the discounted value of the future surpluses arising from the insurance and investment contracts in force at each respective year end. The future surpluses are calculated by using realistic assumptions for each component of the cash flows.

Holding company expenses are apportioned across the segments pro-rata to the total product-based VIF.

'Other' valuation adjustments in CA principally comprise expenses for managing policies which are not attributed at product level. In S&P they represent the estimated cost of guarantees to with-profits policyholders.

Taxation in the value-in-force is modelled on a combined CA and S&P basis and, in the analysis above, is attributed wholly to the CA segment.

FINANCIAL MANAGEMENT

The Group's financial management framework is designed to provide security for all stakeholders, while meeting the expectations of policyholders and shareholders.

The following diagram illustrates the aims, approach and outcomes from the financial management framework:

OBJECTIVES

The Group's financial management framework is designed to provide security for all stakeholders, while meeting the expectations of policyholders, shareholders and regulators. Accordingly we:

- Maintain solvency targets
- Meet the dividend expectations of shareholders
- Optimise the gearing ratio to ensure an efficient capital base
- Ensure there is sufficient liquidity to meet obligations to policyholders, debt financiers and creditors
- Maintain the Group as a going concern

HOW WE DELIVER OUR OBJECTIVES

In order to meet our obligations we employ and undertake a number of methods. These are centred on:

1. Monitor and control solvency
2. Project key financial variables
3. Responsible investment management

OUTCOMES

Key outcomes from our financial management process, in terms of meeting our objectives, are set out below:

1. SOLVENCY	2. SHAREHOLDER RETURNS	3. CAPITAL STRUCTURE	4. LIQUIDITY AND POLICYHOLDER RETURNS	5. MAINTAIN THE GROUP AS A GOING CONCERN
Group Solvency Ratio of 194%	2013 TSR 79% 2013 dividend yield 5.6% Based on share price as at 31 December 2013 of 321.75p and full year 2013 dividend of 17.88p.	Gearing ratio of 29.6% following acquisition of PL This does not include the financial reinsurance that is held within the Swedish business.	Competitive fund performance Policyholders' realistic expectations maintained	Group remains a going concern (see Directors' Report on pages 85 to 86)

HOW WE DELIVER OUR FINANCIAL MANAGEMENT OBJECTIVES

1. MONITOR AND CONTROL RISK AND SOLVENCY

The Board sets internal solvency targets that are based on solvency requirements imposed by our regulators. The targets are set with the intention of balancing the requirements of both our shareholders and policyholders.

i) **a** Pillar 1 calculation, which compares regulatory capital resource requirements, based on the characteristics of the in-force life business, with an associated measure of capital as prescribed by regulation; and

ii) **a** Pillar 2 calculation which compares a risk-based assessment of solvency capital with an associated measure of capital based on a realistic assessment of insurance liabilities; and

iii) the amount of required regulatory solvency capital is then determined by the method which gives rise to the lower excess of regulatory capital over requirements.

These calculations are monitored continually.

2. LONGER-TERM PROJECTIONS

Long-term projections are performed covering, as a minimum:

i) Segmental earnings and surplus arising in the long-term insurance funds;

ii) Chesnara holding company cash flows;

iii) Regulatory solvency and capital resources and requirements; and

iv) European embedded value.

The projections are prepared for a base case, using latest board-approved assumptions, and for various individual and multiple economic and non-economic sensitivities.

In addition:
Financial condition reports are prepared on an annual basis which includes assessments of the ability of the business to withstand key adverse events, including increased rates of policy lapse, expense overruns and unfavourable market conditions.

Reverse stress testing techniques are employed which assess events and circumstances which would cause the business to become unviable. In this context, unviable is defined as the point at which the market loses confidence in the firm being able to carry out its normal business activities.

3. RESPONSIBLE INVESTMENT MANAGEMENT

Investment management

We aim to promote customer retention by pursuing good relative investment performance across both our UK and Swedish businesses.

We use third party investment managers in both the UK and Sweden. They are charged with operating within pre-determined guidelines which are set having regard to the nature of the fund and to contractual obligations to policyholders. For the with-profits funds these are also in accordance with the published Principles and Practices of Financial Management. In Sweden a larger number of fund managers are used, which are subject to very stringent initial selection and ongoing monitoring criteria.

A conservative approach to the investment of shareholders' funds is also adopted within the Group.

FINANCIAL MANAGEMENT (CONTINUED)

OUTCOMES FROM IMPLEMENTING OUR FINANCIAL MANAGEMENT OBJECTIVES

Key outcomes from our financial management process, in terms of meeting our objectives are set out below:

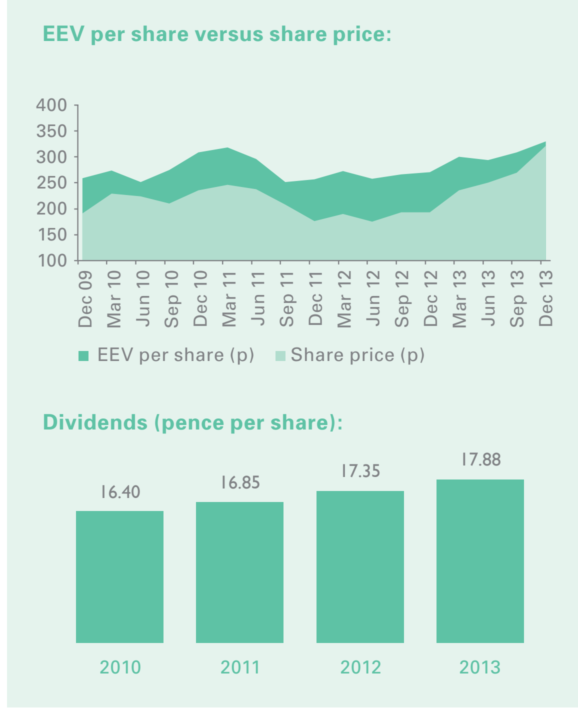
1. Solvency
The solvency and regulatory capital of the Group and its regulated subsidiaries is monitored continually. Further detail of the year end solvency positions has been summarised in the Business Review on pages 25 to 26.

2. Shareholder returns
The Board's primary aim is to provide an attractive dividend flow to its shareholders. With Movestic in its growth phase, shareholder dividend flows are currently generated by the UK run-off businesses within CA plc, by way of the emergence of surpluses in, and transfer of surpluses from, its long-term insurance funds to shareholder funds and by the return on shareholder net assets.

Dividend flows from CA plc to Chesnara are utilised in the first instance for the repayment and servicing of debt, coupled with bearing central corporate governance costs which cannot be fairly attributed to the long-term insurance funds, and which arise largely in connection with Chesnara's obligations as a listed company.

Returns to shareholders can be assessed by reference to many measures including the actual share price, the yields on the shares and the comparison of total market capital to embedded value. The graphs below illustrate:

– how the EEV per share has compared with the share price over recent years, up to 31 December 2013; and
– the dividend growth per share over this same period.



Throughout 2013 and up to 25 March 2014 there has been a general appreciation in the share price, having increased by 55% from 193.0p per share at 1 January 2013 to 300.0p per share at 25 March 2014. The combined impact of the share price growth throughout 2013 and the continuing attractive dividends means shareholders have achieved strong total shareholder return.

3. Capital structure
The Group's UK operations are ordinarily financed through retained earnings and through the current emergence of surplus in the UK life businesses.

These flows are used:

i) to repay our debt obligations;

ii) to support dividend distributions to shareholders; and

iii) to support the medium-term requirements of Movestic to meet regulatory solvency capital requirements as it expands.

The acquisition of S&P in December 2010 for £63.5m was accomplished by way of debt: equity financing broadly in a ratio of 2:1. This introduced a modest level of gearing to the structure of Group financing.

The acquisition of PL in November 2013 for £39.3m was funded using a combination of debt and existing cash resources. The process for raising the debt to fund the purchase of PL also gave rise to a restructuring of the existing facilities that were initially arranged to fund the purchase of S&P. The result is that, at 31 December 2013 bank borrowings amounted to £73.0m, which is being repaid over a five year term.

The purchase of Movestic was financed by internal cash resources. On an ongoing basis the Movestic business is financed by a combination of external financial reinsurance arrangements and capital contributions from Chesnara.

With respect to acquisitions the Group seeks to finance these through a suitable mix of debt and equity, within the constraints imposed by the operation of regulatory rules over the level of debt finance which may be borne by Insurance Groups without breaching solvency requirements.

Other factors which may place a demand on capital resources in the future include the costs of unavoidable large scale systems developments such as those which may be involved with changing regulatory requirements. To the extent that ongoing administration of the UK life businesses is performed within the terms of its third-party outsourcing agreements, the Group is sheltered, to a degree, from these development costs as they are likely to be on a shared basis.

4. Liquidity and policyholder returns
Key aspects of policyholder fund performance in respect of the UK Business and in respect of the Swedish Business are set out in the Business Review.

The current profile and mix of investment asset holdings between fixed-interest securities and cash deposits is such that realisations to meet obligations to third parties and to support dividend distributions can be made in an orderly and efficient way.

5. Maintain the Group as a going concern
The Group's cash flow position, together with the return on financial assets in the parent company, supports the ability to trade in the short-term. Accordingly, the underlying solvency position of the UK life business and their ongoing ability to generate surpluses which support cash transfers to shareholders' funds is critical to the ongoing ability of the Group to continue trading and to meet its obligations as they fall due.

The information set out in 'Maintain strong solvency position' on pages 25 and 26 indicates a strong solvency position as at 31 December 2013 as measured at both the individual regulated life company levels in both the UK and Sweden and at the Group level. In addition, in respect of the UK business, the financial condition report and reverse stress testing assessments indicate that it is able to withstand the impact of adverse scenarios, including the effect of significant investment market falls, while the business's outsourcing arrangements protect it from significant expense overruns.

Notwithstanding that the Group is well capitalised, the current financial and economic environment continues to present specific threats to its short-term cash flow position and it is appropriate to assess other relevant factors. In the first instance, the Group does not rely on the renewal or extension of bank facilities to continue trading – indeed, as indicated, its day to day operations are cash generative. The Group does, however, rely on cash flow from the maturity or sale of fixed interest securities which match certain obligations to policyholders: in the current economic environment there remains a continuing risk of bond default, particularly in respect of financial institutions. In order to manage this risk we ensure that our bond portfolio is actively monitored and well diversified. Other significant counterparty default risk relates to our principal reassurers. We monitor their financial position and are satisfied that any associated credit default risk is low. It is noteworthy that we have negligible exposure to Euro-denominated sovereign debt.

Our expectation is that, notwithstanding the risks set out above, the Group will continue to generate surplus in its UK long-term businesses sufficient to meet its debt obligations as they fall due, to continue to pursue an attractive dividend policy and to meet the short-term financing requirements of Movestic. The Director's Report on pages 85 and 86 provides confirmation that the IFRS Financial Statements have been prepared on the Going Concern basis.

RISK MANAGEMENT

Risk management processes
Overlaying all the day-to-day and development activity we undertake is a focused risk management culture and regime.

In both the UK and Swedish businesses we maintain processes for identifying, evaluating and managing the significant risks faced by the Group, which are regularly reviewed by the Group Audit & Risk Committee. Our risk processes have regard to the significance of risks, the likelihood of their occurrence and take account of existing controls and the cost of mitigating them. The processes are designed to manage rather than eliminate risk and, as such, provide reasonable, but not absolute, assurance against loss.

At the subsidiary level in the UK businesses we maintain, in accordance with the regulatory requirements of the PRA and FCA, a risk and responsibility regime. Accordingly, the identification, assessment and control of risk are firmly embedded within the organisation and the procedures for the monitoring and updating of risk are robust. As part of this we have a Risk Committee in CA plc, which comprises solely of Non-executive Directors. This Committee receives quarterly updates of the key risk registers, as maintained by the senior management, for review and challenge. The Committee reports directly to the CA plc Board which also reviews reports from the compliance and internal audit functions. The Risk Committee reports are also reviewed by the Chesnara Audit & Risk Committee on a quarterly basis. Since its acquisition similar arrangements have been established for Protection Life.

The key risk registers have been designed to complement the production of Individual Capital Assessments, which we are required to submit to the PRA on request and maintain on an ongoing basis. We categorise all risks against the following relevant categories - insurance, market, credit, liquidity, operational and Group - and identify potential exposures and the necessary capital requirements accordingly.

In the Swedish business, at the Movestic subsidiary level, there is full compliance with the regulatory requirement in that its Board and Managing Director have responsibility for ensuring that the management of the organisation is characterised by sound internal control, which is responsive to internal and external risks and changes in them. The Board has responsibility for ensuring that there is an internal control risk function, which is charged with (i) ensuring that there is information which provides a comprehensive and objective representation of the risks within the organisation and (ii) proposing changes in processes and documentation regarding risk management. These obligations are evidenced by regular compliance, internal audit, general risk and financial risk reports to the Movestic Board. The latter is supplemented by quarterly returns to the Swedish regulator, Finansinspektionen, which set out estimated capital requirements in respect of insurance, market, credit, liquidity, currency and operational risks.

Risk management processes are enhanced by stress and scenario testing, which evaluates the impact on the Group of certain adverse events occurring separately or in combination. There is a strong correlation between these adverse events and the risks identified in 'principal risks and uncertainties' below. The outcome of this testing provides context against which the Group can assess whether any changes to its risk management processes are required.

Group and subsidiary auditors regularly report to management on identified control weaknesses together with suggested improvements.

In accordance with the need to comply with the requirements of Solvency II on an EU-wide basis, we are currently reviewing and upgrading our risk management processes, so that Group-wide they will be enhanced in a uniform and consistent manner, embracing:

- articulation of risk appetite statements, following from documented strategic objectives;
- formulation and monitoring of associated risk metrics;
- risk identification and assessment;
- calculation of risk-based capital; and
- the embedding of risk management processes so that they are at the forefront of, and underpin, strategic and operating decisions.

These developments have continued during 2013 and are planned to continue during 2014 and into 2015.

Principal risks and uncertainties
Risks and uncertainties are assessed by reference to the extent to which they threaten, or potentially threaten, the ability of the Group to meet its core strategic objectives. These currently centre on the intention of the Group to maintain an attractive dividend policy.

The specific principal risks and uncertainties subsisting within the Group are determined by the fact that:

i) the Group's core operations centre on the run-off of closed life and pensions businesses in the UK;

ii) notwithstanding this, the Group has a material segment, which comprises an open life and pensions business operating in a foreign jurisdiction; and

iii) these businesses are subject to local regulation, which significantly influences the amount of capital which they are required to retain and which may otherwise constrain the conduct of business.

The following identifies the principal risks and uncertainties, together with a description of their actual or potential impact and of the way in which the Group seeks to control the specific insurance and financial risks it faces. The acquisition of Protection Life has not introduced any new principal risks and uncertainties to the Group.

PRINCIPAL RISKS AND UNCERTAINTIES

Risk	Impact	Control
Adverse mortality/ morbidity/longevity experience	To the extent that actual mortality or morbidity rates vary from the assumptions underlying product pricing, so more or less profit will accrue to the Group.	– Effective underwriting techniques and reinsurance programmes. – Option on certain contracts to vary premium rates in the light of actual experience. – Partial risk diversification in that the Group has a portfolio of annuity contracts where the benefits cease on death.
Adverse persistency experience	Persistency rates significantly lower than those assumed will lead to reduced Group profitability in the medium to long-term.	– In closed life and pensions books, persistency rates tend to improve over time due to policyholder/investor inertia. – Active investment management to ensure competitive policyholder investment funds. – Outsourcer service levels ensure strong customer service standards. – Proactive customer retention processes.
Expense overruns and unsustainable unit cost growth	For the closed UK life and pensions businesses, the Group is exposed to the impact of fixed and semi-fixed expenses, in conjunction with a diminishing policy base, on profitability. For the Swedish open life and pensions business, the Group is exposed to the impact of expense levels varying adversely from those assumed in product pricing.	– For the UK businesses, the Group pursues a strategy of outsourcing functions with charging structures such that the cost is sensitive to book run-off to the fullest extent possible. – The Swedish operations assume growth through new business such that the general unit cost trend is positive. – For both the UK and Swedish businesses, the Group maintains a strict regime of budgetary control.
Significant and prolonged equity and property market falls	A significant part of the Group's income and, therefore, overall profitability derives from fees received in respect of the management of policyholder and investor funds. Fee levels are generally related to the value of funds under management and, as the managed investment funds overall comprise a significant equity and property content, the Group is particularly exposed to the impact of significant and prolonged equity market falls, which may lead to policyholders switching to lower-margin, fixed-interest funds.	– Individual fund mandates may give rise to a degree of diversification of risk and within those funds, hedging techniques are used where appropriate. – Investment management costs fall in line with market falls and hence cost savings partially hedge the impact on income. – There is a wide range of investment funds and managers so that there is no significant concentration of risk.
Adverse Sterling: Swedish Krona exchange rate movements	Exposure to adverse Sterling: Swedish Krona exchange rate movements arises from actual planned cash flows between the Swedish subsidiary and its UK parent company and from the impact on reported IFRS and EEV results which are expressed in Sterling.	– The Group monitors exchange rate movements and the cost of hedging the currency risk on cash flows when appropriate.

RISK MANAGEMENT (CONTINUED)

PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

Risk	Impact	Control
Adverse movements in yields on fixed interest securities	The Group maintains portfolios of fixed interest securities **(i)** in order to match its insurance contract liabilities, in terms of yield and cash flow characteristics, and **(ii)** as an integral part of the investment funds it manages on behalf of policyholders and investors. It is exposed to mismatch losses arising from a failure to match its insurance contract liabilities or from the fact that sharp and discrete fixed interest yield movements may not be associated fully and immediately with corresponding changes in actuarial valuation interest rates.	– The Group maintains rigorous matching programmes to ensure that exposure to mismatching is minimised. – Active investment management such that, where appropriate, asset mixes will be changed to mitigate the potential adverse impact on declines in bond yields.
Counterparty failure	The Group carries significant inherent risk of counterparty failure in respect of: – its fixed interest security portfolio; – cash deposits; and – amounts due from reinsurers.	– Operation of guidelines which limit the level of exposure to any one counterparty and which impose limits on exposure to credit ratings. – In respect of exposure to one major reinsurer, Guardian Assurance Limited ('Guardian'), the Group has a floating charge over the reinsurer's related investment assets, which ranks the Group equally with Guardian's policyholders.
Failure of outsourced service providers to fulfil contractual obligations	The Group's UK life and pensions businesses are heavily dependent on outsourced service providers to fulfil a significant number of their core functions. In the event of failure by either or both service providers to fulfil their contractual obligations, in whole or in part, to the requisite standards specified in the contracts, the Group may suffer loss as its functions degrade.	– Rigorous service level measures and management information flows under its contractual arrangements. – Continuing and close oversight of the performance of both service providers. – The supplier relationship management approach is conducive to ensuring the outsource arrangements deliver to their obligations. – Under the terms of the contractual arrangements the Group may impose penalties and/or exercise step-in rights in the event of specified adverse circumstances.
Key man dependency	The nature of the Group is such that, for both its Group-level functions and for its UK life and pensions operations, it relies on a small, professional team. There is, therefore, inevitably a concentration of experience and know how within particular key individuals and the Group is, accordingly, exposed to the sudden loss of the services of these individuals.	– The Group promotes the sharing of know how and expertise to the fullest extent possible. – It periodically reviews and assesses staffing levels, and, where the circumstances of the Group justify and permit, will enhance resource to ensure that know how and expertise is more widely embedded. – The Group maintains succession plans and remuneration structures which comprise a retention element. – The Group complements its internal expertise with established relationships with external specialist partners.
Adverse regulatory and legal changes	The Group operates in jurisdictions which are currently subject to significant change arising from regulatory and legal requirements. These may either be of a local nature, or of a wider nature, following from EU-based regulation and law. Significant issues which have arisen and where there is currently uncertainty as to their full impact on the Group include: **i)** the implementation of Solvency II requirements; and **ii)** potential change in the regulatory environment in Sweden.	The current opinion is that the implementation of Solvency II will strengthen the long-term risk management environment of Chesnara (as is its intention). The Solvency II programme is covered in more detail on the next page. The key risks are mitigated as follows: – Proposed appointment of external specialist Quality Assurance partner; – Dedicated internal resource; and – Robust programme governance framework. Management continually reviews the potential impact of any prospective regulatory changes.

SOLVENCY II

Our Solvency II programme remains well on track to ensure we are ready for the planned implementation date.

Solvency II is a fundamental review of the capital adequacy regime for the European insurance industry. It aims to establish a revised set of EU-wide capital requirements and risk management standards that will replace the current solvency requirements. Solvency II's primary objective is to strengthen policyholder protection by aligning capital requirements more closely with the risk profile of the company. The regime has a three pillar structure, with each pillar governing a different aspect of the Solvency II requirements and approach. As well as requiring firms to disclose their capital and risk frameworks, the Directive also asks firms to demonstrate how and where the requirements are embedded in their wider activities. The planned implementation date is now 1 January 2016 and interim measures have been agreed by the PRA which require us to develop and implement various aspects of Solvency II in the lead up to the revised implementation date.

Chesnara's approach

Pillar 1

Pillar 1 considers the quantitative requirements of the system, including the calculation of technical provisions and the rules relating to the calculation of the Minimum Capital Requirement (MCR) and the Solvency Capital Requirement (SCR). Under Solvency II there are two prescribed methods for assessing an insurer's SCR; either a Standard Formula set by the regulator or an Internal Model specific to that insurer and which is subject to regulatory approval. Chesnara has opted for the Standard Formula approach for CA plc, PL and Movestic on the grounds that it is a good fit and appropriate for its businesses at the current time. However, we will continue to monitor our position on the choice of approach as our businesses evolve.

Progress update

The majority of the Pillar 1 development is now complete and the initial dry runs for the CA and Movestic businesses were undertaken during Q1 2013 and reported to the respective boards in Q1 and Q2 2013 and consolidated Pillar 1 results for the Group were produced in Q2 2013. Revised Pillar 1 plans have been developed to support the interim requirements and were reviewed by the Chesnara board in January 2014.

Pillar 2

Pillar 2 deals with two main areas: firstly, that our businesses have in place effective strategies and controls to assess and manage the risks it is exposed to and to assess and maintain its solvency capital based on its own risk profile and, secondly, that its strategies, controls and assessment of its solvency capital are subject to supervisory review. This pillar requires us to produce either, an Own Risk and Solvency Assessment (ORSA) for each subsidiary and one for the Group or a single Group-wide ORSA. We will be producing an ORSA for each subsidiary and the Group ORSA. Each ORSA is subject to review and scrutiny by the relevant regulator who will have the power to impose a higher capital requirement should it find any inadequacies in the approach to calculating the SCR or in the risk and governance controls in operation.

Progress update

Following confirmation of the new implementation date work has re-commenced on developing our SII-compliant approach to risk management, business planning, projections, stress testing solvency assessment and governance. Revised Pillar 2 plans have been developed to support the interim requirements and were reviewed by the Chesnara board in January 2014.

Pillar 3

Pillar 3 seeks to enhance market discipline on regulated firms by requiring them to disclose publicly key information that is relevant to market participants. As such, in choosing which information should be selected for disclosure under Pillar 3, supervisors will be guided by the actual needs of market participants rather than by their own information needs. The key reporting requirements are a Solvency & Financial Condition Report (SFCR) and a Regular Supervisory Report (RSR). The SFCR is for public disclosure and will follow a prescribed format. The RSR is not public and is only communicated to the relevant supervisor and, again, will largely follow a prescriptive format.

Progress update

To date, the main focus of Pillar 3 development has been on the analysis of the Quantitative Reporting Templates (QRT'S). This work will identify the source of the data required for populating the QRT's and estimate the development work required to deliver the completed QRT's. The analysis is now mostly complete with some further work required with one of our outsourcers during 2014. Revised Pillar 3 plans have been developed to support the interim requirements and were reviewed by the Chesnara board in January 2014.

CORPORATE AND SOCIAL RESPONSIBILITY

Social and environmental issues are taken seriously by Chesnara, with particular emphasis given to developing and maintaining high standards.

We do not, however, consider that these aspects are critical to the achievement of our strategic aims or that they should form any significant element of remuneration or reward.

Equal opportunities

Chesnara is committed to a policy of equal opportunity in employment and it will continue to select, recruit, train and promote the best candidates based on suitability for the role and treat all employees and applicants fairly regardless of race, age, gender, marital status, ethnic origin, religious beliefs, sexual orientation or disability. Chesnara will ensure that no employee suffers harassment or intimidation.

The table below shows the gender split of employees of the Chesnara Group split across different categories:

	2013		2012	
	Male	**Female**	**Male**	**Female**
Directors of Chesnara plc	7	1	7	–
Senior management of the Group (other than Directors of Chesnara plc)	1	–	1	–
Heads of business units and Group functions	6	6	6	6
Employees of the Group	60	62	61	65
Total	**74**	**69**	**75**	**71**

Senior management includes employees other than Group Directors who have the responsibility for planning, directing or controlling the activities of the company, or a strategically significant part of the company. In Chesnara's case, this is the Managing Director of the Swedish subsidiary, Movestic Livförsäkringar AB.

The Board has not identified any senior management as defined by the Companies Act outside of the Board of Directors and subsidiary Directors. However, to give additional information in keeping with the spirit of the Company's focus on diversity we have provided additional disclosures to cover the employees within the Group. We have provided an analysis of diversity which shows "Heads of Business Units and Group functions" separately from the remainder of employees within the Group.

Disabled employees

Chesnara will provide employment for disabled persons wherever the requirements of the business allow and if applications for employment are received from suitable applicants. If existing employees become disabled, every reasonable effort will be made to achieve continuity of employment.

Health, safety and welfare at work

Chesnara places great importance on the health, safety and welfare of its employees. Relevant policies, standards and procedures are reviewed on a regular basis to ensure that any hazards or material risks are removed or reduced to minimise or, where possible, exclude the possibility of accident or injury to employees or visitors.

The policies, standards and procedures are communicated to employees through contracts of employment, the staff handbook and employee briefings and all employees have a duty to exercise responsibility and do everything possible to prevent injury to themselves and others.

Social, environmental and ethical issues

Chesnara aims to be sensitive to the cultural, social and economic needs of our local community and endeavours to protect and preserve the environment where it operates. To support this we allow each of our UK employees two days release on full pay each year where they can support a local charity project of their choice.

We seek to be honest and fair in our relationships with our customers and provide the standards of products and services that have been agreed.

Being primarily office-based financial services companies, the Directors believe that the Group's activities do not materially contribute to pollution or cause material damage to the environment. However, the Group takes all practicable steps to minimise its effects on the environment and encourages its employees to conserve energy, minimise waste and recycle work materials.

Greenhouse gas reporting

Disclosure of emissions

Global GHG emissions data for the period from 1 January 2013 to 31 December 2013:

	Tonnes of CO_2e
Emissions from:	
Combustion of fuel and operation of facilities (scope 1)	–
Electricity, heat, steam and cooling purchased for own use (scope 2)	121.3
Travel (scope 3)	87.8
Company's chosen intensity measurement = tonnes of CO_2e per square metre of office space occupied	0.117
Emissions reported above normalised to per tonne of product output	

Methodology used to calculate emissions
We have followed the requirements of the GHG Protocol Corporate Accounting and Reporting Standard (revised edition) and the Carbon Trust conversion factors to measure and report greenhouse gas emissions, as well as the disclosure requirements in Part 7 of the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013. The financial control method, which captures the sources that fall within our consolidated financial statements, has been used. Although we operate an outsourced model, these outsourcers do not work exclusively for the Group and therefore it is not deemed appropriate to include emissions outside of the Group consolidated financial statements. The Group's carbon reporting falls under three scopes as shown in the table on the previous page.

There are 16 company-leased vehicles in total in the UK and Sweden which are used primarily for commuting and not business-related activities. Commuting mileage is a personal expense of the employee and is not therefore included in the consolidated financial statements.

Approved by the Board on 27 March 2014 and signed on its behalf by:

Peter Mason	Graham Kettleborough
Chairman	Chief Executive Officer

SECTION C

CORPORATE GOVERNANCE

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GOVERNANCE OVERVIEW FROM THE CHAIRMAN

During 2013 a number of significant narrative reporting changes have been introduced that affect how we report our governance of the Group.

This section of the Report & Accounts provides me with an opportunity to provide insight into the governance of the Company. 2013 has been a year of significant change regarding the way that this is reported, and has resulted in a reasonable level of re-structuring of the front half of our Report & Accounts. In particular the new remuneration reporting rules and the implementation of the strategic report have resulted in a number of key changes. I have taken this opportunity to highlight the key changes below:

The new strategic report

In August 2013 Parliament approved the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013. The new strategic report replaces the old "Performance" section of our 2012 Report & Accounts and has been used to articulate a number of key aspects of our business, such as our strategic aims, our business model, a business and financial review of the year, our approach to risk management and an insight into Chesnara's approach towards corporate and social responsibility. We have used the draft Guidance on the Strategic Report as issued in August 2013 by the Financial Reporting Council to assist with structuring this section.

As can be seen this revised section has brought us a new opportunity to articulate the key Chesnara messages, including how the various elements of our business interlink (such as how our strategic aims have been implemented in the year). This section also includes new information regarding our greenhouse gas consumption coupled with new disclosure requirements for gender diversity among our employees and directors.

The new strategic report is included on pages 11 to 49.

New remuneration reporting and incentive scheme re-design

This year has also seen the introduction of new remuneration rules, in regard to both the process for setting and agreeing Directors' remuneration and also how this is reported. This represents the biggest change in this field for some time. Our new remuneration report on pages 60 to 81 addresses this new legislation and will assist with providing our shareholders with a clearer picture on the processes that we use to determine how our Directors are remunerated, and how these processes link with our strategic goals. The new report has three key sections:

- **The Remuneration Committee Chairman's annual statement:** This provides an overview of the work of the Remuneration Committee during the year.
- **Remuneration policy report:** This articulates the policy that, subject to shareholder approval, will be effective from the AGM and will govern the way we set and manage Directors' remuneration.
- **Annual remuneration report:** This report shows the level of remuneration paid to our Directors in the financial year. The new rules have introduced a new concept of a "single figure" of remuneration for each Director, and now provides more analysis over the pay of the Chief Executive Officer, including comparison to other financial metrics, coupled with a 5-year history of his pay.

I would like to thank the Chairman of the Remuneration Committee, Veronica France, for her work in delivering a report that meets these new requirements.

The 2012 Corporate Governance Code

As referred to in our 2012 Report & Accounts Chesnara developed its Corporate Governance practices and procedures during 2012 with a view to establishing a platform by which we can demonstrate we are meeting the Governance requirements specified by the UK Corporate Governance Code (2012) "the Code", which has been applied for the first time this year.

As can be seen in our Corporate Governance report on pages 55 to 59 we continue to demonstrate how that the Board is committed to the principles of the code and that we have complied with the provisions of the Code in full during the year.

The Audit & Risk Committee report has also been updated this year to incorporate the revisions to the Code. Key areas of note are the disclosures surrounding the support that that Committee has provided to the Board in making the statement that the Report & Accounts when taken as a whole are fair, balanced and understandable, and the further disclosures on the Audit & Risk Committee's role in the appointment and interaction with the external auditor.

Peter Mason
Chairman
27 March 2014

BOARD OF DIRECTORS

Peter Mason was appointed as Chairman of Chesnara plc and Chairman of the Nomination Committee on 1 January 2009 and was appointed as Chairman of Movestic Livförsäkring AB with effect from 23 July 2009. He is also a member of the Remuneration Committee. He was the Investment Director and Actuary of Neville James Group, an investment management company and was admitted as a Fellow of the Institute of Actuaries in 1979. He has over 40 years' experience in financial services and held several non-executive posts within the industry.

Graham Kettleborough is the Chief Executive of Chesnara plc. He joined Countrywide Assured plc in July 2000 with responsibility for marketing and business development and was appointed as Managing Director and to the Board in July 2002. He was appointed as a Non-executive Director of Movestic Livförsäkring AB and as Chairman of Movestic Kapitalförvaltning AB with effect from 23 July 2009. He has lifetime experience in the financial services industry, primarily in customer service, marketing and product and business development, gained with Scottish Provident, Prolific Life, City of Westminster Assurance and Target Life.

Frank Hughes is the Business Services Director of Chesnara plc. He joined Countrywide Assured plc in November 1992 as an IT Project Manager and was appointed to the Board as IT Director in May 2002. He has 26 years' experience in the life assurance industry gained with Royal Life, Norwich Union and CMG.

Peter Wright is an Independent Non-executive Director who was appointed to the Chesnara plc Board on 1 January 2009. At the same date he was appointed as Chairman of the Audit & Risk Committee. He was appointed as a member of the Nomination Committee with effect from 9 July 2009. He retired as a Principal of Towers Perrin on 1 January 2008 and is a former Vice President of the Institute of Actuaries, having been admitted as a Fellow in 1979. He is Chairman of the Risk Committee and of the With-profits Committee of Countrywide Assured plc.

Veronica France is an Independent Non-executive Director who was appointed to the Chesnara plc Board on 16 January 2013. She serves on the Nomination and Audit & Risk Committees and took over the role of Chairman of the Remuneration Committee when Mike Gordon stepped down on 17 May 2013. She is currently a Non-executive Director of Family Assurance where she is a member of their Risk & Audit and Nominations Committees and chairs their Remuneration Committee. Having held a number of positions within life companies, including Marketing Director, in 1992, Veronica set up her own financial services consultancy business advising on strategy, business development, product development and related activities. Veronica was Chairman of the trade body, the Investment and Life Assurance Group in 2002/3 and served on its Management Committee for over ten years before stepping down in 2010.

David Brand is an Independent Non-executive Director who was appointed to the Chesnara plc Board and the Board of Movestic Livförsäkring AB on 16 January 2013. He serves on the Nomination, and Audit & Risk Committees. He was appointed as a Non-executive Director at Exeter Friendly Society in January 2014, where he sits on the Audit, Risk and Compliance Committee and the Investment Committee. He is a qualified actuary who, prior to his retirement in June 2012, had worked for the Hannover Re Group in the UK, acting as the Managing Director of the UK life reinsurance subsidiary since 2003. David had been with the company since 1988, and a Director since 1990. During his career David has also held various roles with the Institute of Actuaries, including being a member of Council and he also served on the ABI Health Committee from 2006 to 2012.

Mike Evans is an Independent Non-executive Director who was appointed to the Chesnara plc Board on 4 March 2013. He serves on the Audit & Risk, Nomination and Remuneration Committees. Mike became Senior Independent Director on the retirement of Mike Gordon on 17 May 2013. He is currently Non-executive Chairman of Hargreaves Lansdown plc, a FTSE 100 listed company, a position he has held since 2009, and serves on the Remuneration and Nomination Committees. He originally joined the Hargreaves Lansdown Board as a Non-executive Director in 2006 and has served on their Audit Committee. Mike is also a Non-executive Director of esure Group plc where he serves on the Remuneration, Risk and Audit Committees, a Non-executive Director of CBRE Global Investors Group (UK) and a member of the advisory board of Spectrum Corporate Finance. He is Chairman of the Board of Trustees of Wessex Heartbeat. Mike is a qualified actuary and served in a number of Director level positions within Skandia UK between 1991 and 2006.

David Rimmington was appointed as Group Finance Director with effect from 17 May 2013. He trained as a chartered accountant with KPMG, has more than 17 years' experience in financial management within the life assurance and banking sectors and has had a significant role in a number of major acquisitions and business integrations. Prior to joining Chesnara plc in 2011 as Associate Finance Director David held a number of financial management positions within the Royal London Group including 6 years as Head of Group Management Reporting.

BOARD PROFILE

The Board's mix of skills and experience creates a solid platform to govern the Group and deliver its strategic objectives.

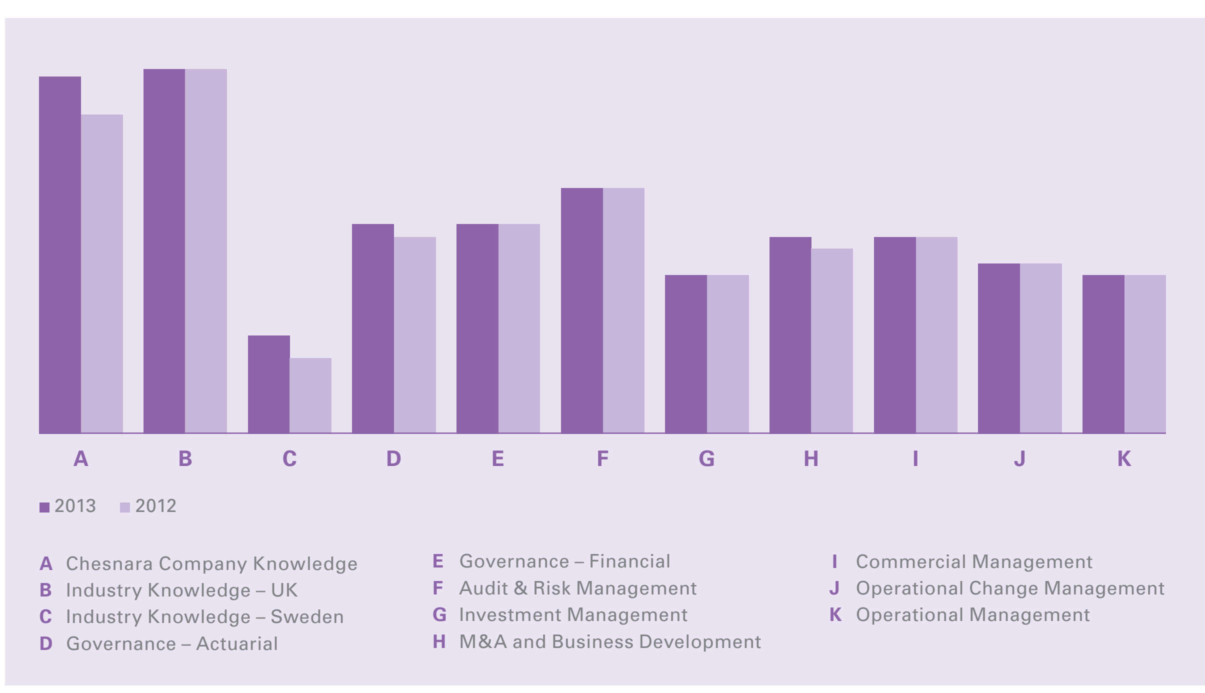
This part of the assessment focuses on ensuring the appropriate breadth and depth of competencies and experience.

A competency matrix is defined for the Board which is aligned to the strategic objectives set out on pages 13 to 15. Each Board member is assessed and scored against the core competencies and cumulative scores provide a competency profile for the Board as a whole, as set out below.

The profile is used to ensure that the Board as a whole possesses an appropriate skills and experience base for effective governance of the Group. The chart below compares the position as at 31 December 2013 with the prior year assessment both of which reflect the impact of the Board composition changes during 2013.

Highlights of the current profile and including changes compared with 2012 are:

- In general the Board changes early in 2013 were deemed to have a positive impact on the lower-ranking competency measures at the expense of a slight adverse impact on the very high ranking measures, thereby creating a general improvement in the balance of the overall Board competency profile.
- In particular, the fact that members with a long established involvement with Chesnara plc were replaced was deemed to have an inevitable temporary adverse impact on the Chesnara Company knowledge measure, with the corollary that fresh viewpoints were brought to the Group. It was also recognised that the changes resulted in a short-term reduction in the overall level of knowledge of the Swedish business. These temporary impacts were recognised in the Board profile reported in 2012. Subsequently, induction programmes and on-going familiarisation during 2013 have had a positive impact and these competencies ratings have increased in 2013.
- The level of knowledge of the Swedish Insurance market is adequate to enable effective Board oversight of the Swedish business for which the deeper specialist knowledge is devolved to the local Board and executive management team.



CORPORATE GOVERNANCE REPORT

The Directors are committed to achieving a high standard of corporate governance including compliance with the principles and practices of the UK Corporate Governance Code (the 'Code'), as published by the Financial Reporting Council in June 2010 and updated in September 2012.

The following statement, together with the Directors' Remuneration Report on pages 60 to 81 and the Audit & Risk Committee Report on pages 82 to 84 describes how the principles set out in the Code have been applied by the Company and details the Company's compliance with the Code's provisions for the year ended 31 December 2013.

During the year under review the UK life and pensions businesses of the Group subsisted in two UK subsidiary companies being Countrywide Assured plc and Protection Life Company Limited. Protection Life Company Limited was formerly known as Direct Line Life Insurance Company Limited and became part of the Group on 28 November 2013.

Compliance with the Code

The Company has complied throughout the year with all of the relevant provisions of the Code.

The Board

At the end of the year ended 31 December 2013, the Board comprised a Non-executive Chairman, four other Non-executive Directors and three Executive Directors.

During the year, there have been changes to the Board membership.

Two new Non-executive Directors, Veronica France and David Brand, were appointed to the Board with effect from 16 January 2013. A further Non-executive Director, Mike Evans was appointed to the Board on 4 March 2013. Two of the existing Non-executive Directors, Mike Gordon and Terry Marris stepped down from the Board from 17 May 2013, the date of the Annual General Meeting. Mike Gordon was the chairman of the Remuneration Committee and that role has been assumed by Veronica France from 17 May 2013. Mike Evans has assumed the role of Senior Independent Director from Mike Gordon.

In addition, Ken Romney stepped down from the Board and left the Company on 17 May 2013, with David Rimmington being appointed to the Board as Finance Director from that date.

Biographical details of all current Directors are given on page 53 and a Board Profile, which assesses the core competencies required to meet strategic objectives, is provided on page 54. The Board, which plans to meet eight times during the year, has a schedule, which it reviews annually, of matters reserved for its consideration and approval. These matters include:

- setting corporate strategy;
- approving the annual budget and medium-term projections;
- reviewing operational and financial performance;
- approving acquisitions, investments and capital expenditure;
- reviewing the Group's system of financial and business controls and risk management and setting risk appetite parameters;
- approving appointments to the Board and to its Committees;
- appointment of the Company Secretary; and
- approval of policies relating to Directors' remuneration.

In addition:

i) the Directors of the Company are also the Directors of Countrywide Assured plc ('CA plc'), a UK-based life and pensions business subsidiary of the Group. Under PRA Regulation the Directors of CA plc have responsibility for maintenance and projections of solvency and for assessment of capital requirements, based on risk assessments, and for establishing the level of long-term business provisions, including the adoption of appropriate assumptions;

ii) five Directors of the Company Messrs Mason, Evans, Kettleborough and Rimmington, and Ms France are also Directors of Protection Life Company Limited ("PL") a UK-based life business subsidiary of the Group. Under PRA Regulation the Directors of PL have responsibility for maintenance and projections of solvency and for assessment of capital requirements, based on risk assessments, and for establishing the level of long-term business provisions, including the adoption of appropriate assumptions;

iii) three Directors of the Company, being Messrs Mason, Kettleborough and Brand, are also Directors of Movestic Livförsäkring AB ('Movestic'), the principal subsidiary company in which the Swedish-based life and pensions business of the Group subsists. Under regulation by Finansinspektionen, the Directors of Movestic have responsibility for ensuring that Movestic complies with regulatory solvency requirements. Mike Gordon stepped down from the Movestic Board when he left the Chesnara Board on 17 May 2013 and was replaced by David Brand.

The responsibilities that the Board has delegated to the respective Executive Management teams, of the UK and Swedish businesses include: the implementation of the strategies and policies of the Group as determined by the Board; monitoring of operational and financial results against plans and budget; prioritising the allocation of capital, technical and human resources and developing and managing risk management systems.

CORPORATE GOVERNANCE REPORT (CONTINUED)

The roles of the Chairman and Chief Executive
The division of responsibilities between the Chairman of the Board, Peter Mason, and the Chief Executive, Graham Kettleborough, is clearly defined and has been approved by the Board. The Chairman leads the Board in the determination of its strategy and in the achievement of its objectives and is responsible for organising the business of the Board and supplying timely information, ensuring its effectiveness, encouraging challenge from Non-executive Directors and setting its agenda. The Chairman has no day-to-day involvement in the management of the Group. The Chief Executive has direct charge of the Group on a day-to-day basis and is accountable to the Board for the financial and operational performance of the Group.

Senior Independent Director
The Board has designated Mike Evans as Senior Independent Director. He is available to meet shareholders on request and to ensure that the Board is aware of shareholder concerns not resolved through the existing mechanisms for shareholder communication.

Directors and Directors' independence
The Board considers that Peter Mason was independent on his appointment as Chairman on 1 January 2009. In making this determination, the Board has carefully considered the fact that he is also a Non-executive Director of Countrywide Assured plc, a position which he has held since 1 October 1990, and a Non-executive Director of Countrywide Assured Life Holdings Limited ('CALHL'), the parent company of Countrywide Assured plc, a position he has held since 18 November 1991.

With regard to Peter Mason the Board considers that the characteristics, aims and mode of operation of the relevant activities of the Company are sufficiently different from those prevailing when he held the relevant position, that the judgement and independence of mind exercised on behalf of the Company are not adversely affected or circumscribed. The Board is of the view that his considerable specific experience and knowledge in the business of the Group outweighs any residual risk in the historical relationships described above.

The Board considers that all Non-executive Directors are independent. In making this determination, the Board has carefully considered that Peter Wright had, within the last three years prior to his appointment, held regulatory actuarial roles at Countrywide Assured plc and had otherwise provided actuarially-based consultancy advice, all such services being provided under an agreement with his employer at the time, Tillinghast Towers Perrin.

With regard to Peter Wright, the nature of the services he provided, being subject either to FSA regulation at that time or to professional standards and guidance prescribed or issued variously by the Institute of Actuaries or by the Financial Reporting Council Board of Actuarial Standards, was such that he was required to maintain a vigorous independence of mind and to prepare recommendations in accordance with the highest professional standards.

There were no comparable matters to consider in respect of Veronica France, David Brand or Mike Evans.

The Board is satisfied that the overall balance of the Board continues to provide significant independence of mind and judgement and further considers that, taking the Board as a whole, the Independent Directors are of sufficient calibre, knowledge and number that they are able to challenge the Executive Directors and their views carry significant weight in the Company's decision making. The Board feels that the changes in Board membership have further enhanced the Board's skills, diversity and experience and formal induction and training have been provided to new Non-executive Directors to ensure the Board continues to operate effectively.

The Directors are given access to independent professional advice, at the Company's expense, when the Directors deem it necessary, in order for them to carry out their responsibilities.

Details of the Chairman's professional commitments are included in his biography on page 53. The Board is satisfied that these are not such as to interfere with his performance, which is based around a commitment of between fifty and sixty hours in any three-month period.

Professional development
The Directors were advised, on their appointment, of their legal and other duties and obligations as Directors of a listed Company. This has been supplemented by the adoption and circulation to each Director of a written Code of Conduct, covering all aspects of the specific operation of Corporate Governance standards and of policies and procedures within the Group. Throughout their period in office, the Directors have, through the conduct of business at scheduled Board meetings, been continually updated on the Group's business and on the competitive and regulatory environment in which it operates. Through their membership of the CA plc Board, and where relevant PL Board, all of the Directors who served during the period under review have considerable knowledge and experience of the UK-based businesses of the Chesnara plc Group. Similarly, Messrs Mason, Kettleborough and Brand, through their membership of the Movestic Board, have considerable knowledge and experience of the Swedish-based business of the Group.

Information
Regular reports and information are circulated to the Directors in a timely manner in preparation for Board and Committee meetings.

As stated above, the Company's Directors are also variously members of the Boards of CA plc, PL and Movestic. These Boards hold scheduled quarterly meetings, which are serviced by detailed regular reports and information, which cover all of the key areas relevant to the direction and operation of that subsidiary including:

For CA plc and PL:

- Earnings report;
- Report from the Actuarial Function Holder and With-profits Actuary;
- Compliance report;
- Investment report; and
- Outsourcing reports.

CA plc and PL monitor risk management procedures, including the identification, measurement and control of risk through the offices of a Risk Committee. These committees are accountable to and reports to their Boards on a quarterly basis.

In addition, annual reports are produced which cover an assessment of the capital requirements of the life assurance subsidiaries, their financial condition and a review of risk management and internal control systems.

For Movestic:

- Earnings report;
- Operating reports, including sales and fund performance;
- Financial risk report;
- General risk report, including an estimate of risk-based capital, in accordance with Swedish regulatory requirements;
- Compliance report; and
- Report on subsidiaries and the associated company.

In addition, Movestic is required to submit to the Chesnara Audit & Risk Committee a quarterly risk report, an annual report on risk management and internal control systems and all internal audit reports.

On a monthly basis, the Directors receive summary high level information, relating to total Group operations, prepared by the Group Chief Executive, which enables them to maintain continuing oversight of the Group's and management's performance against objectives.

In addition to these structured processes, the papers are supplemented by information which the Directors require from time to time in connection with major events and developments, where critical views and judgements are required of Board members outside the normal reporting cycle.

Performance evaluation

During the period under review the Chairman undertook a formal performance evaluation of the Board and Nomination Committees, and of individual directors. To that end he devised a series of questionnaires to provide a framework for the evaluation process and to provide a means of making year-on-year comparisons. Individual Director assessments were supplemented by discussions between the Chairman and each Director on a one-to-one basis.

The Chairman of the Audit & Risk Committee performed a similar evaluation in respect of this Committee. Given the extensive changes to the composition of the Remuneration Committee in May and July 2013 its evaluation will take place within a year of these changes taking effect. In addition, and using similar methods to those described above, the Non-executive Directors, led by the Senior Independent Director, met to conduct a performance evaluation of the Chairman.

The Company Secretariat facilitated the process to ensure that the performance evaluations were conducted in a timely and objective manner while the Head of UK Internal Audit, reporting to the Chairman of the Group Audit & Risk Committee, monitors the assessment and follow through of the issues arising in the evaluation process. As stated previously the Board considers its approach to the evaluation of Board effectiveness on an annual basis.

Company Secretary

The Company Secretary is responsible for advising the Board, through the Chairman, on all governance matters. For the period under review, Mary Fishwick held the position of Company Secretary. The Directors have access to the advice and services of the Company Secretary.

Board Committees

The Board has established the Committees set out below to assist in the execution of its duties. Each of these Committees operates according to written terms of reference and the Chairman of each Committee reports to the Board. The constitution and terms of reference of each Committee are reviewed at least annually to ensure that the Committees are operating effectively and that any changes considered necessary are recommended to the Board for approval. During the year the terms of reference of all the Committees were reviewed and changes made, where required, to reflect updated guidance on corporate governance. The terms of reference of each Committee are available on the Company's website at **www.chesnara.co.uk** or, upon request, from the Company Secretary.

The attendance record of each of the Directors at scheduled Board and Committee meetings for the period under review is:

	Scheduled Board	Nomination Committee	Remuneration Committee	Audit & Risk Committee
Peter Mason – Non-executive Chairman	9 (9)	2 (2)	3 (3)	4 (4)
Terry Marris – Non-executive Director (resigned 17 May 2013)	2 (2)	n/a	1 (1)	1 (1)
Mike Gordon – Non-executive Director (resigned 17 May 2013)	2 (2)	n/a	1 (1)	1 (1)
Peter Wright – Non-executive Director	9 (9)	2 (2)	2 (2)	6 (6)
Graham Kettleborough – Executive Director	9 (9)	n/a	n/a	n/a
Ken Romney – Executive Director (resigned 17 May 2013)	2 (2)	n/a	n/a	n/a
Frank Hughes – Executive Director	9 (9)	n/a	n/a	n/a
Veronica France – Non-executive Director (appointed 16 January 2013)	9 (9)	2 (2)	3 (3)	6 (6)
David Brand – Non-executive Director (appointed 16 January 2013)	9 (9)	2 (2)	2 (2)	6 (6)
David Rimmington – Executive Director (appointed 17 May 2013)	7 (7)	n/a	n/a	n/a
Mike Evans – Non-executive Director (appointed 4 March 2013)	8 (8)	2 (2)	3 (3)	5 (5)

The figures in brackets indicate the maximum number of meetings in the period during which the individual was a Board or Committee member. The information above relates to the period from 1 January 2013 to 31 January 2014. Peter Mason resigned from the Audit and Risk Committee on 17 October 2013 having served the maximum nine year term as a member.

CORPORATE GOVERNANCE REPORT (CONTINUED)

Nomination Committee
During the period under review, the Nomination Committee comprised Peter Mason, who also served as Chairman of the Committee and Peter Wright, both of whom served throughout the period. David Brand, Veronica France and Mike Evans joined from the date on which they were appointed to the Chesnara Board. The Terms of Reference for the Committee can be found on the company website, **www.chesnara.co.uk**

The role of the Nomination Committee is to:

- review the balance and composition of the Board and its Committees, ensuring that they remain appropriate;
- be responsible for overseeing the Board's succession planning requirements including the identification and assessment of potential Board candidates and making recommendations to the Board for its approval; and
- keep under review the leadership needs of, and succession planning for, the Group in relation to both its Executive Directors and other senior executives.

This includes the consideration of recommendations made by the Chief Executive Officer for changes to the executive membership of the Board.

The Nomination Committee considers the mix of skills and experience that the Board requires and seeks the appointment of Directors to ensure that the Board is effective in discharging its responsibilities.

During the period, the Committee met twice to consider the continuing mix of skills and experience of the Directors.

Remuneration Committee
Full details of the composition and work of the Remuneration Committee are provided in the Directors' Remuneration Report on pages 60 to 81.

Audit & Risk Committee
Full details of the composition and work of the Audit & Risk Committee are provided in the Audit & Risk Committee Report on pages 82 to 84.

Relations with shareholders
The Chief Executive, Graham Kettleborough, and the Finance Director, David Rimmington, meet with institutional shareholders on a regular basis and are available for additional meetings when required. Should they consider it appropriate, institutional shareholders are able to meet with the Chairman, the Senior Independent Director and any other Director. The Chairman is responsible for ensuring that appropriate channels of communication are established between the Chief Executive and the Finance Director on the one part and the shareholders on the other and is responsible for ensuring that the views of shareholders are known to the Board. This includes twice yearly feedback prepared by the Group's brokers on meetings the Executive Directors have held with institutional shareholders.

Annual and interim reports are distributed to other parties who may have an interest in the Group's performance and those reports, together with a wide range of information of interest to existing and potential shareholders, are made available on the Company's website, **www.chesnara.co.uk**

Regular meetings are held with industry analysts and commentators so that they are better informed in formulating opinions and making judgements on the Group's performance.

Private investors are encouraged to attend the Annual General Meeting ('AGM') at which the results are explained and opportunity is provided to ask questions on each proposed resolution. The Chairmen of the Board Committees will be available to answer such questions as appropriate. Details of the resolutions to be proposed at the AGM on 16 May 2014 can be found in the notice of the meeting on pages 195 to 196.

Internal control
The Board is ultimately responsible for the Group's system of internal control and for reviewing its effectiveness. In establishing the system of internal control, the Directors have regard to the significance of relevant risks, the likelihood of risks occurring and the costs of mitigating risks. It is, therefore, designed to manage rather than eliminate the risks which might prevent the Company meeting its objectives and, accordingly, only provides reasonable, but not absolute, assurance against the risk of material misstatement or loss.

In accordance with 'Internal Control: Guidance for Directors on the Combined Code' (The 'Turnbull Guidance') the Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group, that this process has been in place for the year under review and up to the date of approval of the Annual Report & Accounts, and that the process is regularly reviewed by the Board and accords with the guidance.

In accordance with the regulatory requirements of the PRA, CA plc has established and maintained a risk and responsibility regime. This ensures that the identification, assessment and control of risk are firmly embedded within the organisation and that there are procedures for monitoring and update of the same. The CA plc and PL Risk Management functions review and report quarterly on this regime to the relevant CA plc and PL Boards.

The Group also maintains a Key Risk Register which ensures that there is identification, assessment and control of the significant risks subsisting within the Company, CA plc, PL and Movestic. The maintenance of the key risk registers is the responsibility of senior management, who respectively report on them quarterly to the CA plc Risk Committee, PL Risk Committee and to each Chesnara Audit & Risk Committee meeting. In accordance with the requirements of the Swedish regulator, the Finansinspektionen, Movestic has also established and maintained a risk and responsibility regime, which requires inter alia that:

- the Movestic Board and Chief Executive have responsibility for ensuring that the organisation and management of the operation are characterised by sound internal control, which is responsive to internal and external risks and to changes in them;
- the Movestic Board has responsibility for the satisfactory management and control of risks through the specification of internal procedures; and
- there is an explicit risk control function, which is supported by compliance and internal control functions.

As an integral part of this regime Movestic also maintains a detailed risk register, which identifies, monitors and assesses risk by appropriate classification of risk.

As stated above, all of the Chesnara Directors are also members of the CA plc Board and the Company thereby has effective oversight of the maintenance and effectiveness of controls subsisting within CA plc. Regarding PL and Movestic, such oversight is exercised by way of the membership of a number the Chesnara Directors of their Boards, together with quarterly reporting by PL and Movestic to the Chesnara Audit & Risk Committee.

In addition, the Chesnara Board confirms that it has undertaken a formal annual review of the effectiveness of the system of internal control for the year ended 31 December 2013, and that it has taken account of material developments between that date and the date of approval of the Annual Report & Accounts. The Board confirms that these reviews took account of reports by the internal audit functions on the operation of controls, internal financial controls, and management assurance on the maintenance of controls and reports from the external Auditor on matters identified in the course of statutory audit work.

The Board also confirms the continuing appropriateness of the maintenance of a UK Internal Audit Function, which reports to the Chairman of the Audit & Risk Committee. The Internal Audit function in Sweden is provided by external consultants who, in accordance with Swedish insurance regulations, must report formally to the Movestic Board.

Financial reporting

Management is responsible for establishing and maintaining adequate internal controls over financial reporting. These controls are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes.

The Group has comprehensive planning, budgeting, forecasting and monthly reporting processes in place. A summary of the Group's financial results supported by commentary and performance measures is provided to the Board before each Board Meeting.

In relation to the preparation of the Group financial statements, the controls in place include:

- the finance governance team review new developments in reporting requirements and standards to ensure that these are reflected in Group accounting policies; and
- the finance governance team develop the Group's financial control processes and procedures which are implemented across the Group.

The reporting process is supported by transactional and consolidation finance systems. Reviews of the applications of controls for external reporting purposes are carried out by senior finance management. The results of these reviews are considered by the Board as part of its monitoring of the performance of controls around financial reporting. The Audit & Risk Committee reviews the application of financial reporting standards and any significant accounting judgements made by management.

Going concern

The Directors' Statement on Going Concern is included in the Directors' Report on page 86.

Directors

The present Directors of the Company and their biographical details are set out on page 53.

DIRECTORS' REMUNERATION REPORT

THE REMUNERATION COMMITTEE CHAIRMAN'S ANNUAL STATEMENT

Changes to the Remuneration Committee
This is my first report since taking over from Mike Gordon as Chairman of the Remuneration Committee in May last year. Following some changes to the Committee that I will come onto later, the other Committee members are Mike Evans (Senior Independent Director) who joined the Chesnara Board in March last year and Peter Mason (Chairman of Chesnara). By invitation, our CEO, Graham Kettleborough attends our meetings and our Company Secretary, Mary Fishwick provides secretarial services.

Chesnara's Business and number of employees
Chesnara plc is a holding company engaged in the management of life and pension books of business in the UK and Western Europe and at year end had a market capitalisation of £370.2m. As a result of its UK operating model predicated on the use of outsourcing, Chesnara has a small UK workforce of 21 employees including three Executive Directors. Chesnara's Swedish business, which is open to new business, has a larger workforce of 123 people including one with executive responsibilities within the subsidiary.

Business performance
The company has delivered very good financial results in 2013, with IFRS pre-tax profit of £60.6m being £40.9m higher than in 2012, and Group EEV growing by 21% to £376.4m. The Group has delivered total shareholder return over the last year of 79%, compared with the FTSE 350 High Yield TSR of 15% in the same period.

Looking at these results through the lens of the Remuneration Committee, we have to look through the headline results and consider the influence that management action has had on these positive results and also assess the extent to which management is taking action in support of the continuation of good results for shareholders into the future. Undoubtedly, positive investment markets have played a significant role in the company's results for 2013 but I am confident that what shareholders are also seeing is a reflection of the Directors' prudent management of the company and delivery on its longer-term strategy.

With a significant proportion of its book being closed to new business, in the medium to longer-term, acquisitions are very important for sustaining future performance. So from a strategic perspective important management actions within the last year have been to identify an acquisition that meets the company's stringent acquisition criteria; to successfully complete the deal to acquire what is now known as Protection Life from the Direct Line Group and to begin the process of integration in order that maximum value may be derived for shareholders.

Management continues to seek further acquisitions to help sustain shareholder returns into the future, for which success will be rewarded primarily through the new Long-Term Incentive scheme.

Effect of business performance on variable remuneration
On the back of the favourable IFRS results which exceeded the stretch target under the 2013 Annual Bonus Scheme, the Directors have been awarded the maximum bonus potential of 100% of salary. The effect of this maximum award means that there will be no payout under the 2013 Long-Term Incentive plan as a result of the maximum potential being shared across the two schemes. This shape of reward, maximum annual payout with no headroom left for rewards for longer-term performance is something we are seeking to change with our proposals for two new incentive schemes which I cover later in this report.

You will see in our Annual Remuneration Report that the CEO and the Business Services Director have both been paid deferred performance related bonuses that were awarded in 2010 following the successful acquisition of Movestic. That performance metric having been met at the end of 2012 – the deferred elements have been paid in full during 2013 and are included in the 2012 single earnings figures.

There is no further deferred payment from legacy bonus awards in respect of the acquisition of Save and Prosper which was paid to the participating Directors without adjustment in January 2014.

2012 shareholder voting – a clear message
Last year's voting on the Remuneration Report (74.8% in favour) gave the Committee the clear message that our shareholders were not totally happy with the remuneration approach at Chesnara. Having undertaken a review, we appreciate that shareholders and governance agencies find certain aspects of the current incentive schemes hard to support, in particular:

- use of a single performance measure;
- awards being totally in cash;
- absence of any deferral; and
- absence of any minimum shareholding requirement for Directors.

As already mentioned, acquisition activity is a key part of Chesnara's strategy. Going back four to five years, there was no Long-Term Incentive scheme in place and acquisition activity (Movestic and Save and Prosper) was rewarded with discretionary bonuses. This was addressed in 2012 with the introduction of an LTIP Scheme with performance based on an adjusted Group European Embedded Value (EEV) measure and cash based awards – we now think it appropriate to further develop the Company's approach to Director remuneration and better align the Director's interests with those of shareholders.

As a result of our review, we have concluded that we should make a number of changes to the Executive Directors' incentive schemes in order to:

- assess performance on a broader range of metrics;
- improve the transparency of the performance measures;
- improve the alignment of Director and shareholder interests;
- better balance Executive's interests in short-term vs. longer-term performance; and importantly
- ensure that the schemes are simple and easy to understand.

To achieve these objectives, we are recommending to shareholders that the current plans are replaced with two new incentive schemes; a Short-Term Incentive (STI) scheme and a Long-Term Incentive (LTI) scheme. These are being supported with the implementation of a minimum shareholding requirement for the Executive Directors equal to one times salary.

Summaries of the principle terms are on page 66, the table below provides a high level summary.

Annual Bonus Plan v new STI Scheme		LTIP v new LTI Scheme	
Current	**New**	**Current**	**New**
1 year performance period.	No change.	3 year performance period.	No change.
Single performance measure (IFRS).	May include a range of measures. For 2014 these will be IFRS, EEV operating profit and strategic group objectives.	Combination of Group EEV and share price performance relative to the EEV.	50% TSR linked to FTSE 350 High Yield Index. 50% projected Group EEV.
100% cash.	65% cash.	100% cash.	100% share awards.
No deferral.	35% deferred for 3 years into shares to be held until the new minimum shareholding requirement is met.	No deferral.	No deferral – but shares awarded to be held until the new minimum shareholding requirement is met.
Maximum potential 100% of salary.	2014 scheme 75% of salary with potential for future awards to be up to 100%.	Maximum between 0% and 100% depending upon payout under Annual Bonus Plan.	2014 scheme 75% of salary with potential for future awards to be up to 100%.

As is currently the case, the three Executive Directors only will be invited to participate in these Schemes. Shareholder approval is being sought at the AGM for both Schemes and assuming a favourable outcome, they will be put into effect following the AGM with performance periods starting on 1 January 2014.

DIRECTORS' REMUNERATION REPORT

THE REMUNERATION COMMITTEE CHAIRMAN'S ANNUAL STATEMENT (CONTINUED)

Major decisions on Director Remuneration
Aside from the decisions taken in connection with the Executive Directors' incentive schemes, the Committee made the following notable decisions during the course of the year:

1. Agreed to implement a minimum shareholding requirement for the Executive Directors equal to one times salary which will take effect from the date of the AGM.

2. In May 2013 David Rimmington was appointed to succeed Ken Romney as Finance Director on a lower salary to reflect his experience at operating at this level. We have been impressed with the competent way in which David has, in his first few months of being FD dealt not only with the day-to-day requirements of the role but has also led the finance area successfully through an acquisition (Protection Life). As a result, in November 2013 we made the first step in taking his salary towards the competent point for this role and increased his salary from £150,000 to £175,000 which still leaves him on a lower salary than his predecessor and modestly paid as compared to the FD role in many similar sized organisations.

3. Where justified by the Company's results and the satisfactory performance of individuals, it is our normal practice to award Executive Directors, and indeed all employees, an annual salary increase broadly in line with inflation. This year, Executive Directors (with the exception of David Rimmington) were granted a pay rise of 2.5% of salary. Other UK employees received pay increases depending upon performance, which averaged slightly more than this.

4. The effect of Government changes to pension limits means that some Executive Directors (and other UK employees) may find they that they are unable to put all their pension benefit into their scheme. Where this is the case, the Remuneration Committee has agreed that cash payments may be made in lieu of pension contributions.

5. The Remuneration Committee together with the CEO (without the Chairman being present) undertook a review of fees for the position of Chairman and concluded that since the last increase in 2010, the Chairman's fee had fallen behind that generally being paid for this role in similar sized organisations and recommended to the Board that the Chairman's fees be increased by 11% to £100,000. This having been agreed by the Board became effective on 1 January 2014.

Role and composition of Committee
Following the recruitment of three Non-Executive Directors and a review by the Board of its Committee composition, the size of the Remuneration Committee was reduced from five to three. Peter Wright and David Brand left the Committee in July.

The key objectives of the Remuneration Committee are:

– To ensure that the Group's Executive Directors are fairly rewarded for their individual contributions to the Group's overall performance by determining their pay and other remuneration.

– To demonstrate to all shareholders that the remuneration of the senior executive members of the Group is set by a Committee of the Chesnara plc Board members who have no personal interest in the outcome of the decisions and who will give due regard to the interests of the shareholders and to the financial and commercial health of the Group.

– To ensure there is a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration of individual directors.

– To recommend fees for non-executive directors. Approval of NED fees, other than those of the Chairman, will be by the Chairman and executive directors in a meeting without the other NEDs being present. Approval of the Chairman's fees will be by the Board in a meeting without the Chairman present.

The full terms of reference of the Remuneration Committee can be found on Chesnara's website **www.chesnara.co.uk**

Committee's activities
During the year the Committee held three meetings. In addition to the matters already noted, during the year and into 2014 the Committee:

– Engaged the services of KPMG for advice on the design of two new incentive schemes.

– Engaged PwC to support the drafting of the rules to the Chesnara 2014 STI and LTI schemes and the associated shareholder resolutions.

– Discussed and agreed the outcome of prior years' achievements against target in respect of the current annual bonus and LTI plans.

– Discussed and set performance targets for the new STI and LTI Schemes (in anticipation of gaining shareholder approval for the schemes).

– Reviewed its Remuneration Policy without substantial change to its principles and we believe that it now better articulates how the policy will operate in practice.

The Committee welcomes dialogue with shareholders. I hope this statement together with all elements of the remuneration report provides you with a clear account of the operation of the Remuneration Committee, its policy and its execution of that policy. We are of the view that the changes proposed as part of the new incentive schemes make a step change to improving the alignment of interests between the Executive Directors and shareholders and hope you feel able to support the enabling resolutions on which we are seeking approval at the Company's AGM on 16 May 2014.

Veronica France
27 March 2014

DIRECTORS' REMUNERATION REPORT

REMUNERATION POLICY REPORT

Introduction

Remuneration policy

This section sets out the Company's policy on Directors' remuneration which is subject to a binding shareholder vote at the 2014 Annual General Meeting. This has been developed by the Remuneration Committee (the Committee) to provide a clear framework for reward which is linked to the strategy of the Company and aligns the interests of executives and shareholders.

Shareholder approval is being sought for this Policy at the next AGM and if approval is granted, it will take effect from the date of the AGM. It is the intention of the Committee that this Policy remains in place for the next three years at which point it will, once again, be put to shareholders for approval. Any commitments made by the Company prior to the approval and implementation of this Policy which were consistent with the remuneration policy in force at the time, can be honoured, even if they would not be consistent with this Policy at the time the commitment is fulfilled.

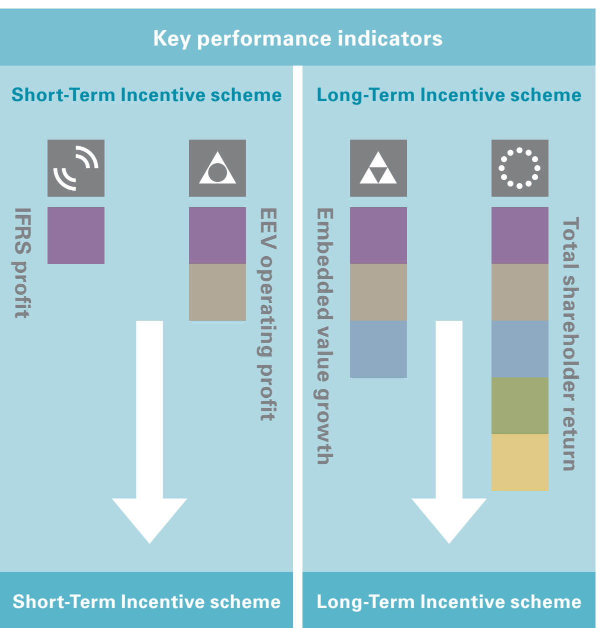
In developing its policy and making decisions about Executive Director remuneration the Committee has taken into account the terms and conditions of employment for employees throughout the Company, together with the strategy and objectives for the business, and developments in the external marketplace. The Company has not consulted with employees.

Chesnara plc is a holding company engaged in the management of life and pension books of business in the UK and Western Europe. With an operating model in the UK which extensively utilises the benefits of outsourcing, Chesnara has 21 employees in the UK including three Executive Directors. Chesnara has a wholly owned life insurance subsidiary in Sweden, Movestic which is open to new business and employs 123 people.

The schematic below illustrates how the Company's KPI's align to the strategic objectives and in turn how those KPIs are recognised as key components of both the new short and long-term incentive schemes. Reading across the chart shows how the KPIs cover the objectives. For example, "Maximise the value from the in-force book", "Enhance value from new business" and "Acquire life and pensions businesses" will all directly impact the EEV growth of the Group. Likewise all objectives should have an impact on the TSR to varying degrees. Strong performance in terms of "maximising value from the in-force book" should positively influence all four KPIs.

The diagram demonstrates that the remuneration policy aligns well to all aspects of the Group's objectives. In addition to the KPIs shown, the Short-Term Incentive scheme includes a measure that assesses how effectively the Executive Directors have performed in delivering strategic initiatives. The initiatives will include any major regulatory projects and hence the objective to "Adopt good regulatory practice at all times" is also directly covered by the remuneration policy as well as being indirectly covered by way of the TSR measure.

Strategic objectives
Deliver shareholder value
1 Maximise value from the in-force book
2 Enhance value through new business
3 Acquire life and pensions businesses
4 Maintain a strong solvency position
5 Adopt good regulatory practice at all times



DIRECTORS' REMUNERATION REPORT

REMUNERATION POLICY REPORT (CONTINUED)

Overall remuneration policy aims are:

- to maintain a consistent remuneration strategy based on clear principles and objectives;
- to ensure remuneration structures do not encourage or reward excessive risk-taking which is outside the boundaries of our stated risk appetite;
- to link remuneration clearly to the achievement of our business strategy and ensure executive and shareholder reward is closely aligned;
- to enable the Company to attract, motivate and retain high-calibre executives; and
- for the policy to be easy to understand and communicate.

The implementation of this policy involves:

- paying salaries that reflect individual roles and sustained individual performance and contribution, taking account of the external competitive market;
- enabling executives to enhance their earnings by meeting and out-performing stretching short and long-term targets in line with the Group's strategy;
- requiring executives to build and maintain shareholdings in the Company;
- rewarding executives fairly and responsibly for their contribution and paying what is commensurate with achievement of these objectives; and
- including malus provisions, as appropriate in the Short-Term Incentive scheme (including the deferred share award) and the Long-Term Incentive scheme.

For the avoidance of doubt, the Directors' Remuneration Policy includes authority for the Company to honour any commitments entered into with current or former Directors that have been disclosed to shareholders in previous Remuneration Reports. Details of any payments to former Directors will be set out in the implementation section of this report as they arise.

The following tables give an overview of the Company's policy on the different elements of the remuneration package.

Future policy table

Executive Directors' remuneration

Purpose and link to strategy	Operation	Performance measures and maximum	Changes to 2013 policy
Basic salary			
To recruit and retain individuals with the skills and experience needed for the role and to contribute to the success of the Group.	In setting salaries for new executive roles or reviewing the salaries for existing roles, the Committee will take into account, as it considers appropriate, some or all of the following factors: – assessment of the responsibilities of the role and the experience and skills of the jobholder – the Company's salary budgets and results – the jobholder's performance – with the use of periodic benchmarking exercises, the external market for roles of a similar size and accountability – inflation and salaries across the Company – balance between fixed and variable pay to help ensure good risk management. Where a new appointment is made, pay may be initially below that applicable to the role and then may increase over time subject to satisfactory performance. Salaries are usually reviewed annually There may be reviews and changes during the year in exceptional circumstances (such as new appointments to executive positions). Since the last Report salaries for the CEO and Business Services Director have risen by 2.5% – slightly below the average increase awarded to all staff – and are effective 1 January 2014. (see table below) The Finance Director, David Rimmington was newly appointed to the role in May 2013 and has quickly demonstrated an ability to operate at a higher level of competency than his starting salary suggested and was awarded an increase of 16.6% in November 2013 taking his salary to £175,000 which remains below that appropriate for the role and may be adjusted further subject to continued satisfactory performance.	Personal and Group performance is taken into consideration when deciding whether a salary increase should be awarded – but salary increases may not be awarded on the strength of performance alone.	There have been no changes to the 2013 policy.
Taxable benefits			
To recruit and retain individuals with the skills and experience needed for the role and to contribute to the success of the Group and to minimise the potential of ill health to undermine Executive's performance.	Executive Directors receive life assurance, a company car, fuel benefit and private medical insurance. A cash equivalent may be paid in lieu of a car. Benefits may be changed in response to changing circumstances whether personal to an Executive Director or otherwise subject to the cost of any changes being largely cost neutral.	No performance measures attached.	There have been no changes to the 2013 policy.
Pensions			
To recruit and retain individuals with the skills and experience needed for the role and to contribute to the success of the Group and to encourage responsible provision for retirement.	The Executive Directors participate in a defined contribution pension scheme with employer contributions varying between 7.5% and 9.5% of basic salary. If regulatory maxima have been reached, the executive can elect to receive the balance of the contribution as cash.	No performance measures attached.	Change to allow pension contributions to be taken in cash once regulatory maxima have been reached.

Director	Increase	Basic salary from 1 January 2014
Graham Kettleborough	2.5%	£328,189
Frank Hughes	2.5%	£202,814

DIRECTORS' REMUNERATION REPORT

REMUNERATION POLICY REPORT (CONTINUED)

Future policy table (continued)

Executive Directors' remuneration (continued)

Purpose and link to strategy	Operation	Performance measures and maximum	Changes to 2013 policy
Short-Term Incentive (STI) scheme			
To drive and reward achievement of the Group's business plan and key performance indicators. To help retention and align the interests of Executive Directors with those of shareholders.	The 2014 STI Scheme is discretionary. Awards are based on the Committee's assessment and judgement of performance against specific performance targets and Group strategic objectives, assessed over a financial year. Provided the minimum performance criteria is judged to have been achieved then an award will be granted in two parts; at least 35% into deferred share awards in the shape of nil cost options which will vest after a 3 year deferral period and the balance in cash. Dividend equivalents accrue in cash with interest thereon in respect of the deferred share awards between the date the share award is granted and the date the options are exercised. It is the intention of the Committee to grant awards annually and the performance criteria will be set out in the corresponding Implementation Plan. The Committee can apply malus provisions to unvested awards, for example, in the event of misstated performance or misconduct.	Performance is measured based on the financial results of the Group and its strategic priorities, together with the performance of the Executives in relation to specific objectives. The main weighting is given to financial results – typically 80%. The targets may include costs, IFRS pre-tax profit, EEV operating profit, cash generation, Group objectives and personal performance. STI Scheme targets are commercially sensitive and therefore, not disclosed. Actual targets and results will be disclosed in the Annual Report immediately following each performance period. For the 2014 STI award the measures and their weighting are: – IFRS pre-tax profit 50% – EEV operating profit 30% – Group Strategic objectives 20% The Committee may substitute, vary or waive the performance measures in accordance with the Scheme Rules. The maximum award is 100% of basic salary, however the STI Scheme award for 2014 is limited to 75%.	The Remuneration Committee has undertaken a review of the remuneration policy during 2013. This is a new scheme for which shareholder approval is being sought at the AGM. More information is set out in the notes to this table and in the Resolution on page 199.
Long-Term Incentive (LTI) scheme			
To incentivise the delivery of the longer-term strategy by the setting of stretching targets based on shareholder value, and to help retain key executives and increase their share ownership in the Company.	The 2014 LTI Scheme is discretionary. Awards are made under a performance share plan, with no exercise price. The right to receive shares awarded will be based on achievement of performance conditions over a minimum three-year period. It is the intention of the Committee to grant awards annually and the performance criteria will be set out in the corresponding Implementation Plan. The Committee may apply malus provisions to unvested awards, for example, in the event of misstated performance or misconduct.	For 2014 vesting is dependent on two equally weighted performance measures: 1. **Total Shareholder Return:** Performance conditions are based on total shareholder return of the Company when compared to that of the companies comprising the FTSE 350 High Yield Index. No payout will be made unless the Company achieves at least median performance. Full vesting will be achieved if the Company is at the upper quartile compared to the peer group. 2. **Group Embedded Value:** This target is commercially sensitive and therefore, not disclosed. Actual targets and results will be disclosed in the Annual Report for the year in which an award vests. The assumptions underpinning the calculations are subject to independent actuarial scrutiny. The Committee may substitute, vary or waive the performance measures in accordance with the Scheme Rules. The maximum award is 100% of basic salary, however the LTI Scheme award for 2014 is limited to 75%.	The Remuneration Committee has undertaken a review of the remuneration policy during 2013. This is a new scheme for which shareholder approval is being sought at the AGM. More information is set out in the notes to this table and in the Resolution on page 199.

Non-executive Directors' remuneration

Purpose and link to strategy	Operation	Performance measures and maximum (where applicable)	Changes to 2013 policy
Fees			
To recruit and retain independent individuals with the skills, experience and qualities relevant to the role and who are also able to fulfil the required time commitment.	Fees for the Chairman are determined and agreed with the Board by the Committee (without the Chairman being party to this). Non-executive Director fees are determined by the Chairman and the Executive Directors. Fees are reviewed periodically and in setting fees consideration is given to market data for similar roles in companies of comparable size and complexity whilst also taking account of the required time commitment. All Non-executive Directors are paid a base fee. Additional fees are paid to the Senior Independent Director, the chair of Board Committees and to other Non-executive Directors to reflect additional time commitments and responsibilities required by their role. Since our last report and following a review of market practice on fees for similar sized organisations, the Chairman's fees have been increased by 11.1% from £90,000 to £100,000 effective from 1 January 2014. The last increase was in 2010. The Remuneration Committee Chairman will be paid an additional fee of £5,000 in 2013 and 2014 to reflect the increased time commitment required to support the changes to the company's remuneration policy and other regulatory requirements.	Fees for the Chairman and Non-executive Directors are not performance related. Reflecting the periodic nature of the fee reviews, increases at the time they are made, may be above those paid to Executives and/or other employees.	There have been no changes to the 2013 policy.

DIRECTORS' REMUNERATION REPORT

REMUNERATION POLICY REPORT (CONTINUED)

Explanatory notes:

1. Why these performance measures were chosen and how performance targets are set

STI Scheme – The performance measures for the STI Scheme reflect the main financial contributors to sustaining returns for shareholders and the Group strategic objectives to ensure that management is incentivised on the important projects needed to support the strategy. The Remuneration Committee determines the measures, their weighting and the targets for each financial year. The measures will be based upon the most relevant taken from a selection of measures which may include costs, IFRS pre-tax profit, EEV operating profit, cash generation, Group strategic objectives and personal performance. The maximum potential award requires significant outperformance of budgeted targets.

LTI Scheme – The performance measures for the LTI Scheme have been selected for their alignment to shareholder interests using an absolute measure (growth in Group EEV) and a comparative measure (TSR). The measures and the targets are set by the Committee. The maximum potential award for the Group EEV measure requires significant outperformance of budgeted targets. The TSR measure uses the FTSE 350 High Yield Index over a 3 year period with averaging during the first and last month. The Committee currently considers this to be an appropriate comparator given Chesnara's strategic aims and focus on dividend payments.

In setting targets for both Schemes, the Committee exercises its judgement to try and ensure that there is a balance between stretch in the targets and the company's risk appetite. Full details of the performance measures, weightings and targets and the corresponding potential awards are set out in the Implementation Plan. (For 2014 see page 66).

The Future Policy table notes that all the financial targets for the STI Scheme are commercially sensitive as is one of the measures for the LTI Scheme. The Committee has considered whether it could reasonably use transparent targets but concluded that transparency should not be sought at the expense of choosing the right ones for the alignment of Executive Director and shareholder interests even if these are not capable of being disclosed up front.

2. Changes to the Executive Directors' incentive schemes

The Committee has undertaken a wide ranging review of the Executive Directors' incentive schemes primarily to better align the interests of Executive Directors and shareholders; and to improve the balance of awards between short-term results and achievement of longer-term strategic initiatives. The review has resulted in two new schemes being put to shareholders for approval at the 2014 AGM.

Short-Term Incentive (STI) scheme

The Committee has made the following changes in relation to its approach to short-term incentives to address concerns that have been expressed about the previous arrangements and to better align the Executive Directors' interests to those of shareholders:-

- **(i)** moved away from a single performance measure (IFRS pre-tax profit) to a broader range of measures – including Group strategic objectives;
- **(ii)** each year, the Committee will determine the measures and their weighting to help ensure there is focus on each of the elements necessary to drive sustainable performance. The main weighting will be given to financial measures (typically 80%);
- **(iii)** replaced a purely cash-based award without any deferral with an award that is part cash and part share award deferred for a further 3 years. For 2014 the award is 65% cash and 35% deferred into shares provided that the total award to a participant is at least £20,000 otherwise the award is 100% cash with no deferral. The Committee may increase the weighting for the share award in future years and adjust the de-minimis amount;
- **(iv)** the period during which unvested awards may be withheld under the terms of the malus provisions has been extended by virtue of the introduction of a 3 year deferred period for part of the award; and
- **(v)** it is the intention of the Committee to make a new award each year.

Further information about the new 2014 STI Scheme can be found in the Scheme Summary on page 79.

Long-Term Incentive (LTI) scheme

Following its review the Committee believes this new scheme provides a more transparent approach to long-term incentives and better aligns the interests of Executive Directors with those of shareholders. More specifically:

- **(i)** replaced a purely cash based award with a performance share plan;
- **(ii)** moved away from a single absolute performance measure (EEV) to use of absolute and comparative measures;
- **(iii)** in making a new award, the Committee will determine the measures, their weighting and targets to maintain a clear focus on longer-term strategic aims;
- **(iv)** performance period at least three years and exactly three years for the awards made in 2014; and
- **(v)** it is the intention of the Committee to make a new award each year.

Consistent with the previous LTIP, malus provisions are included.

Further information about the new 2014 LTI Scheme can be found in the Scheme Summary on page 80.

Changes common to both new incentive schemes

Maximum Potential Awards

Under the existing incentive arrangements, the potential maximum award is 100% of basic salary and is shared between the annual and long-term plans. The maximum is now 75% and applies to each new Scheme independently which has the effect of increasing the Executive Director's overall maximum potential across the two Schemes. The Committee is of the view that independent maxima are preferable in order to remove any potential bias in the Executive Directors' behaviours to favour creation of good short-term results at the expense of creating value over the longer-term. Additionally, the Committee is of the view that the revised quantum (75% of basic salary for each award in 2014) strikes the right balance between being motivational for the Executive Directors and not excessive either in absolute terms or by comparison with the market. The Committee may, in future years, increase the maximum award for the STI Scheme and/or the LTI Scheme up to 100% of basic salary if it considers that the targets justify a higher potential reward.

Minimum shareholding requirement

In order to further align the Executive Directors' interests with those of shareholders, a minimum shareholding requirement has been introduced equal to one times salary. There is no timescale attached and it may be achieved by participating in the Company's share plans. It is a requirement that shares awarded under the STI and LTI schemes (net of shares sold to pay for any income tax and National Insurance) must be retained if the minimum requirement has not been met. Details of Executive Directors' shareholdings and the extent to which the requirements have been met are disclosed on page 79 of the Annual Report on Remuneration.

Existing incentive plans

Vesting of outstanding awards made under existing plans will be dependent on the performance conditions and other rules of the Long-Term Incentive plan under which the awards were granted.

3. Differences in policy compared with other employees:

The following note outlines any differences in the Company's policy on Executive Director remuneration from other employees of the Group.

- **Salary and fees:** There are no differences in policy. The Committee takes into account the Company's overall salary budget and percentage increases made to other employees.
- **All taxable benefits:** There are no differences in policy although the benefits available vary by personnel and jurisdiction and with job role. For example cars and health insurance benefits are broadly consistent with the equivalent benefits when offered to UK Non-Director personnel. Executive Directors receive fuel allowances which is a benefit not offered to other grades receiving a car allowance.
- **Annual bonus:** This is an integral part of the Company's philosophy with all UK employees below Board level being eligible to participate in a bonus scheme which is based on service and achievement of financial targets. Senior managers in Sweden participate in annual bonus schemes which reflect the achievement of business targets and personal goals. In line with Swedish regulations part of the payment of this bonus is deferred. Other employees in Sweden participate in a scheme based on the achievement of company-wide business goals.
- **Long-term plans:** Only Executive Directors are entitled to participate in the long-term plans as these are the roles which have most influence on and accountability for the strategic direction of the business and the delivery of returns to shareholders.
- **Pension:** The level of contribution made by the Company to Executive Directors is similar to that offered to the majority of other UK employees. Certain employees do receive lower company pension contributions.

4. Other

The Company currently operates an SAYE scheme which expires in 2014. The Committee has the discretion to renew the SAYE scheme, a tax efficient all employee scheme in which Executive Directors are eligible to participate.

Approach to remuneration on recruitment

The following principles apply when recruiting Executive Directors:

- To offer a remuneration package that is sufficient to attract individuals with the skills and experience appropriate to the role to be filled whilst also being consistent with this Policy. In addition to salary and variable remuneration, this may include pension, taxable benefits and other allowances such as relocation, housing and education.
- Pay levels will be set taking account of remuneration across the company including other senior appointees, and the salary offered for similar roles by other companies of similar size and complexity.
- Each element of remuneration offered will be considered separately and collectively in this context.
- The maximum awards in respect of the STI Scheme and LTI Scheme as set out in the table on pages 79 and 80 apply in recruitment situations, save that exceptionally the Company may award a one-off compensatory bonus or LTI award where the new joiner would lose a bonus or long-term award relating to his or her former role. In the event that such a payment is made, full details will be disclosed in the Annual Report on remuneration for the relevant year.

DIRECTORS' REMUNERATION REPORT

REMUNERATION POLICY REPORT (CONTINUED)

Service contracts and loss of office

Executive Directors

Our policy is for Executive Directors to have service contracts with a rolling twelve-month notice period.

The table below summarises the notice periods and other termination rights of the Executive Directors and the Company. The approach of the Company on any termination is to consider all relevant circumstances and to act in accordance with any relevant rules or contractual provisions. Typically, a leaving employee is classified as a 'Good Leaver' if they depart under 'Special Circumstances' (defined in the table below). An employee leaving under any other circumstances is classified as a 'Bad Leaver'.

The Committee has discretion to classify an employee as a Good Leaver or a Bad Leaver and to determine the treatment of their outstanding awards upon departure.

Typical treatment in relation to salary, benefits and outstanding incentive awards for leavers under each scenario is shown below:

Nature of termination	Notice period	Salary and benefits	Short-Term Incentive scheme	Long-Term Incentive scheme	Pension
By Executive Director or company giving notice (excluding special circumstances see below).	12 months.	Cease on date employment ends. Payment may be made for any unused holiday entitlement.	No grants following service of notice. Right to cash payment and unvested deferred share awards cease on date employment ends. Outstanding options must be exercised within 6 months of date employment ends.	No grants following service of notice. Unvested awards lapse on date employment ends. Outstanding options must be exercised within 6 months of date employment ends.	Cease on date employment ends.
By Company summarily.	None.	Cease on date employment ends.	No further grants. Right to cash payment and unvested deferred share awards cease on date employment ends. Outstanding options must be exercised within 6 months of date employment ends.	No further grants. Unvested awards lapse on date employment ends. Outstanding options must be exercised within 6 months of date employment ends.	Cease on date employment ends.
Special circumstances: leaving by reason of death, injury or disability, redundancy, retirement with the agreement of the Remuneration Committee, the sale of employing business or company, or other special circumstances at the discretion of the Committee.	None prescribed.	Normally cease on date employment ends. Payment may be made for any unused holiday entitlement. Discretion to Company to pay salary and benefits in a single payment or in monthly instalments. Where payments are made monthly the executive is under an obligation to mitigate his or her loss and monthly payments will cease or reduce upon the executive accepting alternative employment.	Discretion to make further grants during a notice period where this is considered to be in the company's interests. Where employment ends before deferred share awards made, at the discretion of the Committee, the award may be retained. If retained, the Committee has discretion to allow the award to vest in accordance with original terms, or determine award is to vest on ceasing to be employed and will also assess the extent to which targets have been met. In either case the award will be pro-rated to reflect period of Performance Period that has been worked and will be paid in cash. Committee has discretion to pro-rate using a longer period. Where employment ends after deferred share awards made, the award will be retained and vest in accordance with original terms. The Committee has discretion to allow the award to vest on ceasing to be employed. All outstanding options must be exercised within 6 months of the date on which employment ends or on which they vest (whichever is later), unless the Committee specifies a longer period.	No further grants. Where employment ends before share awards vest, at the discretion of the Committee the award may be retained. If retained, the Committee has discretion to allow the award to vest in accordance with original terms or, may determine awards to vest on ceasing to be employed and will also assess the extent to which the targets have been met. In either case the award will be pro-rated to reflect the period of the Performance Period that has been worked. Committee has discretion to pro-rate using a longer period. All outstanding options must be exercised within 6 months of the date on which employment ends or on which they vest (whichever is later) unless the Committee specifies a longer period.	Cease on date employment ends.

Non-executive Directors

- Appointments are made under a contract for services for an initial term of three years subject to election by shareholders at the first Annual General Meeting following their appointment and annual re-election thereafter.
- Non-executive Directors are typically expected to serve two three-year terms but may be invited by the Board to serve for an additional period. Any renewal is subject to Board review and AGM re-election.
- The terms of an appointment are set out in a letter of appointment which can be terminated by either party with three months' notice.
- There are no compensation terms regardless of the circumstances that may lead to a contract being terminated.

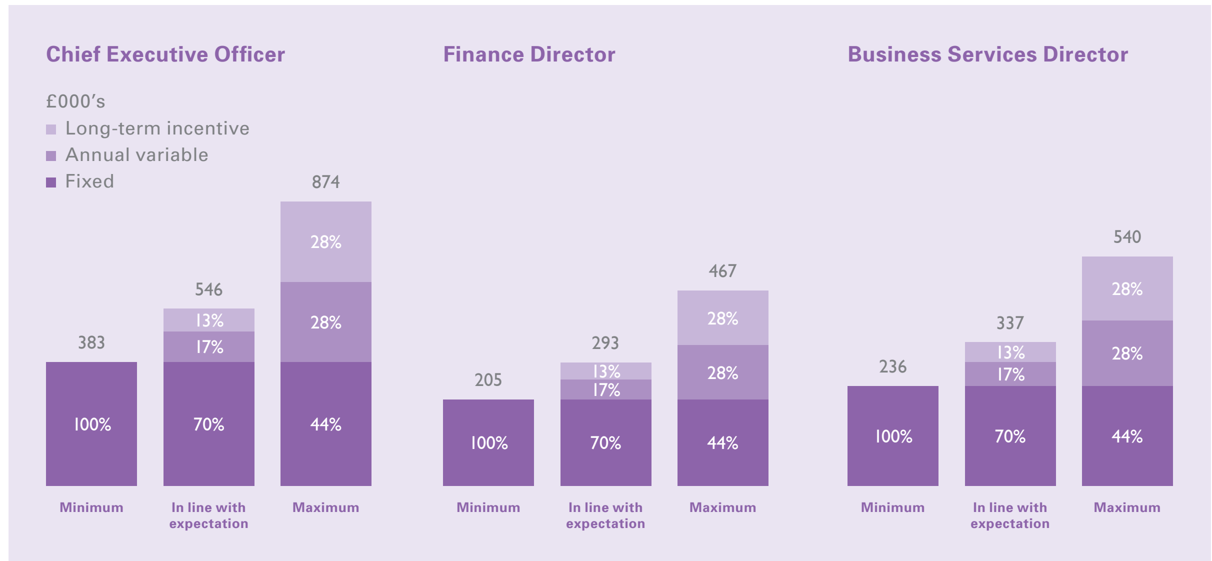
Other Directorships

Executive Directors may, if approved by the Board, accept appointments as non-executive directors of suitable organisations. Normally fees for such positions are paid to the Company, unless the Board determines otherwise.

Illustration of application of Remuneration Policy

The view of the Committee is that there should be balance between fixed and variable pay such that when stretching performance targets have been achieved in full around half of an Executive Directors' earnings are variable and half are fixed. The Committee believes that this is appropriate given the strategy of the Company and its risk appetite.

The charts below provide estimates of the potential future reward opportunities for each Executive Director, and the potential split between the different elements of remuneration under three different performance scenarios: 'Minimum', 'In line with expectation' and 'Maximum'. The illustration assumes that the 2014 Policy applies throughout the period and that the new STI and LTI Schemes are both approved by shareholders.



Minimum

The table below analyses the constitution of the minimum earnings projection for 2014:

Director	Salary and fees £000	Benefits £000	Pension £000	Total fixed pay £000
Chief Executive Officer	326	21	36	383
Finance Director	166	15	24	205
Business Services Director	198	14	24	236

The pension information above includes both employee and employer contributions. Employee pension contributions are funded by way of a salary sacrifice arrangement and as such are reported as part of the pensions value with a corresponding reduction in salary. The employer contribution element of the pension value varies by Director, and is between 7.5% and 9.5% of gross basic salary before salary sacrifice items.

Statement of shareholder views

The review of Executive Director incentives which has been carried out during 2013 by the Remuneration Committee has taken into account views expressed by shareholders in connection with the 2012 Remuneration Report.

DIRECTORS' REMUNERATION REPORT

ANNUAL REMUNERATION REPORT

Single total figure of remuneration for each Director (audited information)

The remuneration of the Executive Directors for the years ended 31 December 2013 and 31 December 2012 is made up as follows:

Executive Directors' remuneration as a single figure – year ended 31 December 2013

Name of Director	Salaries and fees £000	All taxable benefits £000	Annual bonuses £000	LTIP £000	Pension £000	Total for 2013 £000
Graham Kettleborough	302	21	320	–	51	694
Ken Romney (resigned 17 May 2013)	77	5	–	–	17	99
David Rimmington (appointed 17 May 2013)	93	9	98	–	13	213
Frank Hughes	167	14	198	–	50	429
Total	**639**	**49**	**616**	**–**	**131**	**1,435**

Executive Directors' remuneration as a single figure – year ended 31 December 2012

Name of Director	Salaries and fees £000	All taxable benefits £000	Annual bonuses £000	LTIP £000	Pension £000	Total for 2012 £000
Graham Kettleborough	272	18	190	75	49	604
Ken Romney	190	12	130	50	42	424
Frank Hughes	150	14	117	25	45	351
Total	**612**	**44**	**437**	**150**	**136**	**1,379**

The remuneration of the Non-executive Directors for the years ended 31 December 2013 and 31 December 2012 is made as follows:

Non-executive Directors' remuneration as a single figure – year ended 31 December 2013

Name of Director	Salaries and fees £000	All taxable benefits £000	Total for 2013 £000
Peter Mason	90	–	90
Mike Gordon (resigned on 17 May 2013)	17	–	17
Terry Marris (resigned on 17 May 2013)	15	–	15
Peter Wright	60	–	60
Veronica France (appointed 16 January 2013)	46	–	46
David Brand (appointed 16 January 2013)	43	–	43
Mike Evans (appointed 4 March 2013)	37	–	37
Total	**308**	**–**	**308**

Non-executive Directors' remuneration as a single figure – year ended 31 December 2012

Name of Director	Salaries and fees £000	All taxable benefits £000	Total for 2013 £000
Peter Mason	90	–	90
Mike Gordon	45	–	45
Terry Marris	40	–	40
Peter Wright	50	–	50
Total	**225**	**–**	**225**

Salary and fees
Basic salaries are usually reviewed annually by the Remuneration Committee. Assessments are made giving full regard to external factors such as earnings inflation and industry benchmarks and to internal factors such as changes to the role by way of either structural reorganisations or enlargement of the Group. In addition, basic pay levels reflect levels of experience. The single earnings figures demonstrate the application of this assessment process. The year on year increase in the basic salary of Graham Kettleborough and Frank Hughes reflect the findings from a benchmarking exercise undertaken by the Remuneration Committee towards the end of 2012, details of which were included in the 2012 Annual Report & Accounts. David Rimmington has entered the Finance Director position at a lower basic salary then his predecessor and the Remuneration Committee will assess development and performance and reconsider the level of basic pay as appropriate.

Taxable benefits
The taxable benefits relate to the provision of a car, fuel allowance and medical insurance.

Annual bonuses and LTIPs
The 2013 annual bonus scheme is based on a single measure, namely IFRS pre-tax profit. The scheme begins to generate value at 75% of IFRS pre-tax profit target increasing to a value of 15.79% of annual basic salary for achieving 100% of target. Thereafter the value increases on a straight line basis until a maximum award of 100% of basic salary is earned. During 2013 the IFRS pre-tax profit was 398% of the target, which is at a level such that the maximum attainment of 100% of basic salary has been reached. Despite the 100% of basic salary cap the analysis suggests that the annual bonus is actually higher than basic salary. This apparent anomaly is due to the fact that the salary reported is net of employees' pension scheme contributions made by way of salary sacrifice.

During 2013 the incentive arrangements have a combined cap of 100% of basic salary for both the annual bonus plan and the LTIP. Therefore the 2013 LTIP which vests in 2015 has zero value potential.

The 2012 annual bonus scheme was as per the 2013 scheme detailed above. The IFRS pre-tax profit represented an achievement of 178.89% of the target profit and an annual bonus scheme award of 66% of basic salary.

The 2012 LTIP scheme is dependent upon target embedded value criteria being achieved at the end of 2014 and hence has generated zero value at the end of 2012 and 2013. The 100% of basic salary combined annual bonus and LTIP cap means that the maximum potential 2012 LTIP value is 34% of basic salary.

The LTIP value reported in the 2012 single earnings figure analysis relates to the final award under a discretionary scheme set up in 2009 to reflect the value generated by the acquisition of Movestic. The scheme included a fixed bonus value payable in 2013 subject to the embedded value of Movestic at 31 December 2012 being higher than the value on 31 December 2009 and the performance criteria was met.

Pension
The pension component in the single figure table above includes a combination of employer's contributions and a salary sacrifice element. The employer's contribution is based on a fixed percentage of each Executive's salary, and can vary between Executives. With regard to the salary sacrifice element, this is determined at the discretion of each Executive. For the salary sacrifice component the Company contributes the NI saving associated with the amount of salary sacrificed by each Executive.

DIRECTORS' REMUNERATION REPORT

ANNUAL REMUNERATION REPORT (CONTINUED)

Scheme interests awarded during the financial year (audited information)

Up until and including 2011 the LTIP schemes for Executive Directors were effectively based on single year performance measures with payments deferred for three years. As such any amounts due from pre-2012 LTIP schemes are recognised within the single earnings figures for the original performance assessment year. That is, all awards have already crystallised prior to this financial year and have been reported.

The LTIP schemes for 2012 and 2013 depend upon three year EEV projection targets being met or exceeded. As such no value in these schemes has as yet crystallised. The 2012 and 2013 schemes will vest at the end of 2014 and 2015 respectively and will hence be included in the single earning figures in those future vesting years. Note however that for 2012 and 2013 the total maximum combined bonus from the short-term annual incentive plans and long-term incentive plans is capped at 100% of basic salary. In light of the annual bonuses earned in 2012 and 2013, the maximum potential value from the current active LTIPs is relatively limited. Annual bonus payments during 2012 represented 65.48% of the total basic salary and as such only 34.52% remains available from any potential LTIP award. During 2013 the annual bonus represents 100% of basic salary and hence the 2013 LTIP has no potential value on vesting.

The table below sets out potential Long-Term Incentive scheme interests that have accrued during the year:

Name of Executive Director	Name of scheme	Basis of award	Face value (note 1) £	% of award vesting for minimum performance	Length of vesting period	Summary of performance measures and targets (note 2)
Graham Kettleborough	2013 LTIP	Awards in cash are made dependent on the EEV outcome against target EEV projections at the end of a 3 year assessment period.	–	–	3 years – vesting date 31 December 2015.	Based on achievement of a target share price at the end of 2015: Rewards on a sliding scale from 0% of basic annual salary on achievement of 75% of target to 21.05% of basic annual salary on achievement of target, continuing on a straight line basis if target is exceeded. (Note 2)
	2012 LTIP	Awards in cash are made dependent on the EEV outcome against target EEV projections at the end of a 3 year assessment period.	99,775	–	3 years – vesting date 31 December 2014.	Based on achievement of a target share price at the end of 2014: Rewards on a sliding scale from 0% of basic annual salary on achievement of 75% of target to 21.05% of basic annual salary on achievement of target, continuing on a straight line basis if target is exceeded. (Note 2)

Scheme interests awarded during the financial year (audited information)(continued)

Name of Executive Director	Name of scheme	Basis of award	Face value (note 1) £	% of award vesting for minimum performance	Length of vesting period	Summary of performance measures and targets (note 2)
Frank Hughes	2013 LTIP	Awards in cash are made dependent on the EEV outcome against target EEV projections at the end of a 3 year assessment period.	–	–	3 years – vesting date 31 December 2015.	Based on achievement of a target share price at the end of 2015: Rewards on a sliding scale from 0% of basic annual salary on achievement of 75% of target to 21.05% of basic annual salary on achievement of target, continuing on a straight line basis if target is exceeded. (Note 2)
	2012 LTIP	Awards in cash are made dependent on the EEV outcome against target EEV projections at the end of a 3 year assessment period.	61,204	–	3 years – vesting date 31 December 2014.	Based on achievement of a target share price at the end of 2014: Rewards on a sliding scale from 0% of basic annual salary on achievement of 75% of target to 21.05% of basic annual salary on achievement of target, continuing on a straight line basis if target is exceeded. (Note 2)
David Rimmington	2013 LTIP	Awards in cash are made dependent on the EEV outcome against target EEV projections at the end of a 3 year assessment period.	–	–	3 years – vesting date 31 December 2015.	Based on achievement of a target share price at the end of 2015: Rewards on a sliding scale from 0% of basic annual salary on achievement of 75% of target to 21.05% of basic annual salary on achievement of target, continuing on a straight line basis if target is exceeded. (Note 2)

Note 1 – The Face Value is reported as the current estimate of the potential value on vesting less any adjustment to recognise the combined Annual Bonus and LTIP cap of 100% of basic salary.

Note 2 – Any payments, together with the annual bonus, would normally be capped, on award, at 100% of basic salary.

Note 3 – Any amounts vesting will be subject to a pro rata adjustment to reflect scheme entry part way through the year.

DIRECTORS' REMUNERATION REPORT

ANNUAL REMUNERATION REPORT (CONTINUED)

Payments for loss of office (audited information)

On 17 May 2013 Ken Romney resigned as Finance Director of the Group. The total amount that he was paid for loss of office was as follows:

Description	Amount £	Explanation of how calculated
Pay in lieu of notice	125,233	This represents payment of salary and contractual benefits.
Compensation for early termination of employment	75,000	This is a discretionary amount agreed by the Committee as compensation for early termination of employment.
Early payment of performance-vested annual bonus with deferred elements and acquisition-related payments	155,110	This represents early payment of deferred awards where performance conditions have been met, that would have been paid at the end of 2013, and which were paid early at the discretion of the Remuneration Committee as the majority of the deferral period had been served.
Payment in lieu of 2012 LTIP award	41,601	This represents a discretionary early payment of the 2012 LTIP award, based on an assessment of the level of financial performance up to the point of departure.
Total	**396,944**	

As reported in the 2012 Annual Report & Accounts all of the payments in the table above were conditional upon certain personal performance obligations being achieved to the satisfaction of the Board. It can be confirmed that these performance obligations were met and therefore payment of the above items was made in full.

Statement of Directors' shareholding and share interests (audited information)

The Remuneration policy, effective from the 2014 AGM, requires Executive Directors to hold shares to the value of their basic salary. This recognises that it is not practical to impose an immediate requirement and as such Directors are expected to retain all shares received from either short-term or long-term incentive schemes until the requirement is met. Directors may dispose of shares even when the minimum holding level has not been achieved where funds are required to discharge any income tax and National Insurance liabilities arising from awards received from a Chesnara incentive plan.

The table below shows, in relation to each Director, the total number of share interests with and without performance conditions, the total number of share options with and without performance measures, those vested but unexercised and those exercised at 31 December 2013 or the date of resignation.

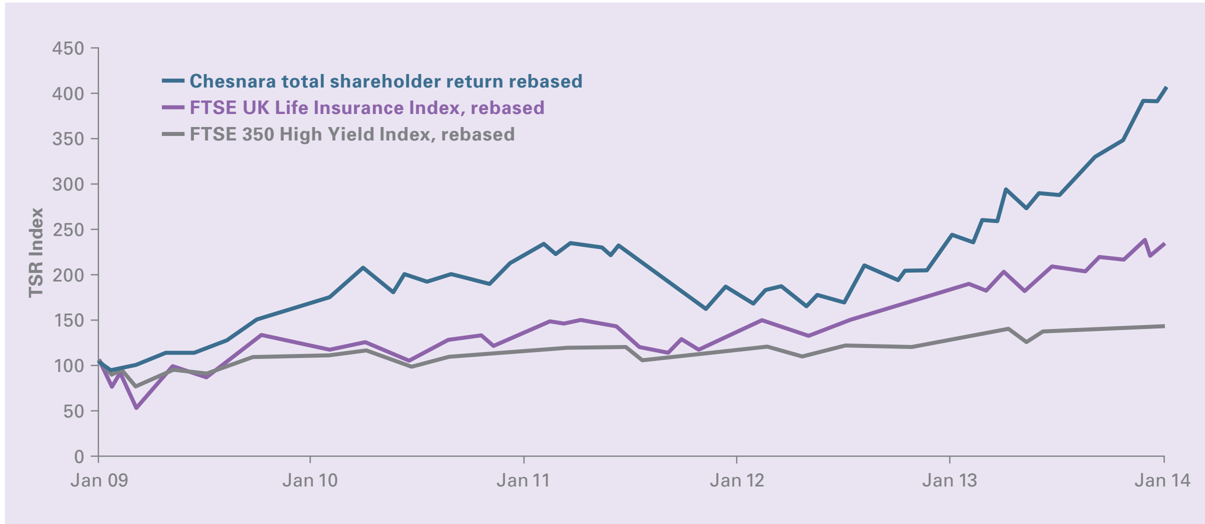
The share options without performance measures relate to amounts invested by the Executive Directors into a "save as you earn" scheme instigated in 2011 which vests in 2014. The number of shares is based on a cumulative investment values of £27,000 divided by an option price of 173.4p per share.

No changes took place in the interests of the Directors between 31 December 2013 and 27 March 2014.

Name of Director	Shares		Options			
	With performance measures	Without performance measures	With performance measures	Without performance measures	Vested but unexercised	Exercised during the year
Graham Kettleborough	–	68,100	–	5,190	–	–
Ken Romney (resigned on 17 May 2013)	–	79,476	–	–	–	–
David Rimmington	–	2,127	–	5,190	–	–
Frank Hughes	–	5,832	–	5,190	–	–
Peter Mason	–	19,768	–	–	–	–
Mike Gordon (resigned on 17 May 2013)	–	–	–	–	–	–
Terry Marris (resigned on 17 May 2013)	–	57,615	–	–	–	–
Peter Wright	–	70,000	–	–	–	–
Veronica France	–	–	–	–	–	–
David Brand	–	–	–	–	–	–
Mike Evans	–	–	–	–	–	–
Total	**–**	**302,918**	**–**	**15,570**	**–**	**–**

Performance graph and CEO remuneration table

The following graph shows the Company's performance, measured by total shareholder return, compared with the performance of the FTSE 350 High Yield Index and the FTSE UK Life Insurance Index, which are also measured by total shareholder return. The FTSE 350 High Yield Index has been selected as a comparison because it is the index used by the Company for the performance criterion for the 2014 Long-Term Incentive scheme, and the FTSE UK Life Insurance Index has been selected due to Chesnara's inclusion within this index.



The table below sets out the details for the Director undertaking the role of Chief Executive Officer.

Year	CEO single figure of total remuneration £000	Annual bonus pay-out against maximum %	Long-term incentive vesting rates against maximum opportunity %	Note
2013	694	100.00%	n/a	1
2012	604	65.48%	100.00%	2
2011	376	17.39%	n/a	3
2010	624	100.00%	n/a	3
2009	502	94.27%	n/a	3

Note 1 – During 2013 no LTIP value as been earned because the annual bonus in isolation has accounted for the full 100% combined bonus cap.

Note 2 – The vesting percentage in 2012 within the Long-term incentive column does not relate to a formal LTIP scheme. It relates to a discretionary supplementary scheme established in 2009 to recognise the value added to the Group from the acquisition of Movestic. The amount vesting has been classified in the LTIP column due to the fact its award was subject to certain future performance criteria being achieved. That scheme has generated the maximum potential value of £75,000 in 2012. The formal 2012 LTIP scheme has contributed no value to the total single remuneration figure as it does not vest until performance criteria have been achieved in 2014.

Note 3 – Prior to 2012 the LTIP schemes were in fact better characterised as deferred annual bonus schemes. As such they are classified within the annual bonus value and any value is included in the annual bonus pay-out against maximum percentage.

DIRECTORS' REMUNERATION REPORT

ANNUAL REMUNERATION REPORT (CONTINUED)

Percentage change in remuneration or Director undertaking the role of Chief Executive Officer

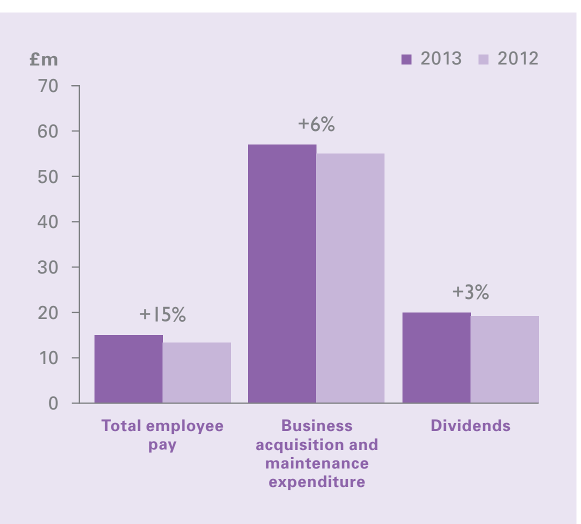
The table below shows the percentage change in remuneration or the Director undertaking the role of Chief Executive Officer and the company's employees as a whole between the years 2013 and 2012.

Percentage change in remuneration in 2013 compared with 2012	CEO	Group employees
Salary and fees	+11.32%	+7.73%
All taxable benefits	+17.48%	+2.64%
Annual bonuses	+68.15%	+11.53%

Relative importance of spend on pay

The graph to the right shows the actual expenditure of the Group and change between the current and previous years.

Due to the fact that Chesnara adopts a strategy of outsourcing much of its activities the level of total employee pay is relatively low in comparison to dividends. In addition, the graph shows a comparison with the Group's total acquisition and maintenance expenditure. As can be seen, the total employee pay is relatively small against our overall cost base.



Statement of Implementation of Remuneration Policy in the following financial year

A Remuneration Policy has been developed during 2013 in accordance with regulatory requirements and, subject to appropriate approvals being received, will take effect from the date of the 2014 AGM.

The following tables and commentary illustrate, in terms of parameters and targets, how the policy will be implemented during 2014:

Salaries and fees

Will be managed in accordance with the Company's Remuneration Policy (see page 65).

2014 Short-Term Incentive (STI) scheme

The table below and accompanying notes set out the performance measures, weightings and the potential outcomes for achieving minimum, on-target and maximum performance. The actual targets for each measure are commercially sensitive and will not be disclosed until 2015 together with the actual performance against those targets.

Measures	Weightings	Ranges and targets			Potential outcomes in terms of % of basic salary		
		Minimum achievement (as % of target)	Target achievement	Max achievement (as % of target)	Minimum achievement	Target achievement	Max achievement
IFRS pre-tax profit	50%	75%	Target	200%	–	11.25%	37.50%
EEV operating profit	30%	90%	Target	150%	–	9.60%	22.50%
Group strategic objectives	20%	75%	Target	125%	–	7.50%	15.00%

Subject to shareholder approval, the 2014 STI Scheme will be implemented and operated by the Remuneration Committee as set out within the Remuneration Policy (see the Future Policy table on page 66 and its accompanying notes).

Measures

The three measures selected by the Remuneration Committee for 2014 ensure a balance between aligning Executive Director remuneration to shareholder returns whilst also recognising measures over which the Directors can exercise more immediate and direct influence. The IFRS pre-tax profit and EEV operating profit are recognised outputs from the audited year end Financial Statements, although it should be noted that the Remuneration Committee is able to make discretionary adjustments if deemed necessary. The Executive Director objectives include major regulatory or business development initiatives that are expected to be progressed during the year. The Remuneration Committee reviewed the Group business plan and identified developments which it considers appropriate for assessing the Executive Directors. Each individual development objective is assigned a "significance weighting" influenced by factors such as business criticality, scale, complexity and level of Executive Director influence. Developments with a higher significance are weighted more heavily when establishing the overall performance target.

Weightings

The weightings have been set by the Remuneration Committee. The financial measures that align most directly to shareholder benefit are generally assigned a higher weighting.

Targets

The IFRS pre-tax profit and EEV operating profit targets are initially based on the 2014 budgets produced as part of the 2014 Group business planning process. The Group business plan is subject to rigorous Chesnara Board scrutiny and approval. The Remuneration Committee can make discretionary adjustments to either the targets or to the actual results for the year if it considers this to be appropriate.

DIRECTORS' REMUNERATION REPORT

ANNUAL REMUNERATION REPORT (CONTINUED)

2014 Long-Term Incentive (LTI) scheme

The table below and accompanying notes set out the performance measures, weightings and the potential outcomes relative to achieving minimum, on-target and maximum performance. The actual EEV target is commercially sensitive and will not be disclosed until 2017 together with the actual performance against those targets.

Measures	Weightings	Ranges and targets			Potential outcomes in terms of % of basic salary		
		Minimum achievement (as % of target)	Target achievement	Max achievement (as % of target)	Minimum achievement	Target achievement	Max achievement
TSR	50%	<Median	Median	Upper quartile	nil	9.4%	37.5%
EEV	50%	≤89%	Target	114%	nil	12.5%	37.5%

Subject to shareholder approval, the 2014 LTI Scheme will be implemented and operated by the Remuneration Committee as set out within the Remuneration Policy (see the Future Policy table on pages 65 to 67 and its accompanying notes).

Measures

The two performance measures for the 2014 LTI Scheme award use performance against an index and internal targets. The external measure compares the 3 year TSR of Chesnara plc against the TSR of the FTSE 350 High Yield Index with averaging over the first and last calendar months. The internal measure assesses Embedded Value growth compared to Board approved target projections. Both measures ensure an alignment between Executive Director reward and shareholder value, with one assessing relative performance to other investment opportunities and the other assessing absolute performance. Both measures are based on a 3 year performance period ending 31 December 2016.

Weightings

For the 2014 award the two measures have been assigned equal weighting.

Targets

The Remuneration Committee proposes that the FTSE 350 High Yield Index represents the most appropriate peer group for assessing the relative TSR performance. Award begins to accrue for median performance with a value of 9.4% of basic salary. This increases on a straight line basis to 37.5% for upper quartile performance. The Embedded Value target is an output from the Chesnara business plan process. The figure is therefore subject to Group Board challenge and approval. The projections assume a realistic expectation for investment returns and incorporate challenging expectation for new business value from Movestic. The Remuneration Committee can make discretionary adjustments to either the target or to the actual result for the year if it considers this to be appropriate.

Consideration by the Directors of matters relating to Directors' remuneration

In accordance with its Terms of Reference, which can be viewed on the Company's website, the Remuneration Committee considered matters relating to Directors' Remuneration at each of its meetings in 2013. Members of the Remuneration Committee during the course of the year were:

Committee members	Notes relating to role/tenure on the Committee
Mike Gordon	Previous Committee Chairman. Resigned 17 May 2013
Veronica France	Appointed 16 January 2013. Committee Chairman from 17 May 2013
Terry Marris	Resigned 17 May 2013
Peter Wright	Stepped down 11 July 2013*
David Brand	Appointed 16 January 2013. Stepped down 11 July 2013*
Mike Evans	Appointed 04 March 2013

*As part of a review of the Company's committee structures undertaken by its Nominations Committee.

By invitation, the Chief Executive, Graham Kettleborough attended the Remuneration Committees held last year, but was not present when matters relating to his own remuneration were discussed.

The Committee does not retain the services of external advisers, however, on a project basis, during the past year, the Committee engaged the services of KPMG for advice on the design of two new incentive schemes. This appointment was made by the Committee Chairman in consultation with the Committee using an appropriate appointment process. The Committee Chairman discussed the Committee's requirements with two potential services providers and invited proposals before making a selection. The Committee has no reason to believe that the advice received from KPMG has been anything other than independent and objective particularly as the firm is a member of the Remuneration Consultants Group. Fees to KPMG in relation to work undertaken last year were £31,000.

Statement of voting at general meeting

Concerns expressed in connection with the 2012 Remuneration Report, and the actions taken in response, are included in the section entitled "2012 shareholder voting – a clear message" within the Remuneration Committee Chairman's Annual Statement on pages 60 to 61.

The Group is committed to on-going shareholder dialogue and takes an active interest in voting outcomes. Where there are substantial votes against resolutions in relation to Directors' remuneration, the reasons for any such vote will be sought. In 2012 a significant percentage of shareholders voted against the Remuneration Report. The reasons and actions taken are covered in the Chairman's Statement on page 61.

The following table sets out actual voting in respect of the approval of the 2012 remuneration report:

Number of votes cast for	Percentage of votes cast for	Number of votes cast for	Percentage of votes cast against	Total votes cast	Number of votes withheld
46,616,431	74.8%	15,703,128	25.2%	62,319,559	54,996

There was no vote over the remuneration policy report as this is being introduced for this first time in the 2013 Annual Report & Accounts. The 2013 remuneration policy report will be subject to shareholder approval at the 2014 AGM and the results will be included in the 2014 Annual Report & Accounts as well as being made available on the Chesnara website.

Approval

This report was approved by the Board of Directors on 27 March 2014 and signed on its behalf by:

Peter Mason Chairman	Graham Kettleborough Chief Executive Officer

AUDIT & RISK COMMITTEE REPORT

The Audit & Risk Committee continues to bring to bear its knowledge and expertise in fulfilling its obligations and in exercising judgement in critical areas.

Role and composition
At the start of the year the Audit & Risk Committee comprised Peter Wright (Chairman), Mike Gordon and Terry Marris, as independent Non-executive Directors and Peter Mason (Group Chairman). Mike Gordon and Terry Marris left the Committee on their retirement from the Chesnara Board on 17 May 2013. Peter Mason left on 17 October 2013 having completed the maximum nine years term as a member. Veronica France and David Brand were appointed as independent Non-executive Directors to the Committee on 16 January 2013. Similarly Mike Evans was appointed to the Committee on 4 March 2013. The qualifications of each member of the Committee are included on page 53. On invitation, the Group Chairman, the Chief Executive, the Finance Director, the Business Services Director (whose role includes risk reporting), the Head of UK Internal Audit, the consulting firm which provides internal audit services to Movestic and the external Auditor attends meetings to assist the Committee in the fulfilment of its duties. The Committee met six times during the year ended 31 December 2013.

The role of the Audit & Risk Committee includes assisting the Board in discharging its duties and responsibilities for financial reporting, corporate governance and internal control. The scope of its responsibilities also includes focus on risk and risk management: accordingly it also assists the Board in fulfilling its obligations in this regard. The Committee is also responsible for making recommendations to the Board in relation to the appointment, re-appointment and removal of the external Auditor. The Committee's duties include keeping under review the scope and results of the audit work, its cost effectiveness and the independence and objectivity of the external Auditor. The full terms of reference of the Audit & Risk Committee are available on our website **www.chesnara.co.uk**

Activity
During the period under review, the Audit & Risk Committee has formally reported to the Board on how it has discharged its responsibilities. This has included:

- reviewing the Group's draft Financial Statements prior to Board approval and reviewing the external Auditor's detailed reports thereon, in respect of the half year ended 30 June 2013 and the year ended 31 December 2013;
- reviewing the appropriateness of the Group's accounting policies;
- provide guidance with respect to the annual financial statements being fair, balanced and understandable;
- reviewing the provision of supplementary reporting of financial information in accordance with European Embedded Value principles, including the methodology undertaken and the assumptions adopted;
- reviewing and approving the audit fee estimates and reviewing and approving the audit and non-audit fees, in conjunction with an assessment of external Auditor performance;
- reviewing the external Auditor plan for the audit of the Group's financial statements which included an assessment of key risks and confirmation of Auditor independence;
- reviewing and approving internal audit plans for the internal audit of the Group's internal controls, embracing operating, financial and business controls;
- reviewing an annual report on the Group's systems of risk management and internal control and their effectiveness and reporting to the Board on the results of the review;
- reviewing regular reports from the internal audit functions;
- overseeing the due diligence and governance process for the acquisition of Protection Life;
- reviewing the internal audit arrangements for, and approving the change in external consultants providing internal audit services to Movestic;
- meeting the Head of UK Internal Audit without an Executive Director or a member of the Company's senior management being present;
- reviewing quarterly reports by Executive Management on the identification, evaluation and management of key risks, embracing the Company, CA plc and Movestic;
- meeting the external Auditor without an Executive Director or a member of the Company's senior management being present;
- reviewing the nature and volume of non-audit services provided by the external Auditor to ensure that a balance is maintained between objectivity and value added; and
- reviewing the Group's policies and procedures relating to fraud, whistle-blowing and employment of ex-employees of the external Auditor.

In addition to the above, Committee members have detailed knowledge of CA plc's risk management processes by virtue of their common membership of the CA plc Risk Committee, which reports to the CA plc Board, CA plc being subject to the PRA/FCA Risk and Responsibility regime.

Key issues

During the period under review the following issues have arisen, which have required careful consideration and exercise of judgement by the Committee:

With-profits guarantees

The ex Save and Prosper segment of business contains some with-profits contracts with guarantees. For EEV reporting the cost of these guarantees is assessed on a market-consistent basis which attempts to reproduce the theoretical cost of hedging out the risks associated with them. This in turn requires stochastic modelling of future equity prices and bond yields based on assumptions for the volatilities of these variables consistent with those which underline option pricing at the valuation date as well as assumptions regarding future investment policy and costs of guarantees charged to policyholders. There is some judgement required in setting these volatilities although they are obtained from an external source. Over the year the rise in bond yields and equity prices has reduced the cost of guarantees by a material amount.

For IFRS reporting a more prudential approach is taken, consistent with the general approach when setting policyholder liabilities under IFRS 4. The cost of with-profits guarantees is set at 110% of the equivalent cost for EEV reporting. The movement in cost over the year is, however, very similar.

Allowance for non-market non-diversifiable risks

In the EEV the rate of interest used to discount shareholder cash flows is subject to an addition to cover non-market risks which are not diversifiable. This addition had been set at 0.5% pa for CA plc and 0.7% pa for Movestic for some years.

One of the investigations presented to the Committee compares the EEV reduction applied with an independent measurement of the relevant non-market risk runs. It was concluded that continuing with the 0.7% pa addition for Movestic was inappropriate as it would have reduced the overall allowance for risk and as a consequence it was decided to raise the allowance to 1% pa. The 0.5% pa was deemed appropriate for UK businesses, including that acquired with Protection Life.

Allowance for credit risk when setting valuation rate of interest

For UK IFRS reporting the valuation rate of interest used for discounting policyholder liabilities makes an explicit allowance for credit risk. The company adopts a formula for determining this based on the credit rating of each asset and its yield spread over an equivalent gilt edged stock. The overall yield on any asset after this formulaic deduction is then subject to a cap which in recent years has been 2% pa over the equivalent gilt edged stock yield.

Over 2013 the yield spread on corporate bonds reduced substantially. In the light of this it was decided that continuing with the existing formula would imply a deduction for default risk which was below general market estimates and hence changes were made to bring CA and PL allowances into line. The overall permitted maximum yield over gilt-edged stock was also reduced to 1.5% pa.

Accounting for the purchase of Protection Life

For the acquisition accounting of Protection Life under IFRS, in determining the fair value of the net assets acquired one of the most prominent assets recognised was an intangible asset that represents the fair value of the acquired value of in-force business (AVIF). The AVIF represents the present value of the cash in-flows and outflows associated with the policies in force at the time of acquisition, and ascribing a value requires professional judgement and expertise.

A paper was prepared by management highlighting the process that was performed in determining the fair value of the net assets acquired. The paper highlighted the key assumptions applied in arriving at these values, including specific focus on the AVIF asset, coupled with commentary articulating the outcome of the process. In valuing the AVIF, the key inputs that were presented to the Audit & Risk Committee were the projected best estimate of the cash inflows and outflows, the assumptions applied in arriving at the projected cash flows, and the discount rate that was applied in valuing these cash flows. The outcome of this assessment resulted in a small gain being recognised on acquisition.

UK administration costs

Some of the outsourcing arrangements within the UK are subject to on-going contract negotiations. As a result of this there is an element of Management judgment surrounding the future costs that are expected to be incurred in administering these components of the UK business. Assumptions made by Management in this regard will impact both the IFRS and statutory positions of these components (as these assumptions affect the valuation of insurance contract provisions) and also the EEV position. Management has prepared papers for the Audit & Risk Committee supporting the expense assumptions that have been applied, which clearly articulate the basis on which its judgments have been made.

Movestic persistency

Over 2013 Movestic management has closely monitored, on a monthly basis, actual persistency experience against that assumed in the EEV as the assumptions set at the end of 2012 did allow for an improvement on the then current experience. Some improvement was observed, but this was less than expected, and as a consequence the Committee agreed strengthening of the EEV assumptions at both the half-year and year-end. The assumptions now for discontinuances of all kinds are in line with current experience.

Higher than expected discontinuance rates have also led to a re-assessment of the pace of amortisation of deferred acquisition cost (DAC) assets for IFRS reporting. Such DAC assets at Group level are established only for business written after Chesnara's acquisition of Movestic and hence the impact of a faster pace of amortisation on historic DAC assets is muted in Chesnara's Group accounts.

AUDIT & RISK COMMITTEE REPORT (CONTINUED)

Key issues (continued)

Impairment of Movestic acquisition VIF intangible asset
The acquisition of Movestic in 2009 resulted in the recognition of a material intangible asset, representing the fair value of the acquired in-force policies at that date. This intangible asset is being amortised over its expected useful life and is subject to annual impairment tests as required by IFRS. The impairment test performed by Management compares the unamortised acquisition VIF at the year end date to an estimate of the year end VIF on policies that were in force at acquisition and continue to remain in force at the year end date. The year end VIF on policies that were in force at acquisition is determined using a cash flow model that includes a number of Management assumptions, such as discount rates, future investment returns and discontinuance rates. A paper was prepared and presented to the Audit & Risk Committee which highlighted the key assumptions applied and the conclusions drawn.

Going concern
The Committee continues to review the periodic reports relating to the continuing appropriateness of preparing Group financial statements on a going concern basis, and gives particular attention to the integrity of the underlying assumptions and to the appropriateness of the different stress scenarios which test the assumptions.

External Auditor

Effectiveness of the audit process
The Committee has assessed the effectiveness of the external audit process. This assessment has had regard to the following factors:

- the quality of the background papers and verbal presentations to the Committee on the audit planning process, interim and final audit findings and compliance with independence criteria. The current audit engagement partner was appointed during 2010;
- the rationale put forward for the materiality limits established and the explanation given of the impact these have had on the work performed;
- the views of the Executive on the way in which the audit has been conducted. For February 2014 the views were collated by means of a formal questionnaire; prior to that time verbal representations were taken;
- the report produced by the Financial Reporting Council dated May 2013 entitled "Deloitte LLP Audit Quality Inspection" in conjunction with the report "Audit Quality Inspection Annual Report 2012/13". The Deloitte specific report was discussed with the auditor although we understand that the Chesnara plc audit was not in the population of those inspected; and
- the audit fees charged and the change in fees from the previous year. Changes in annual fees do, of course, need to reflect change in the nature of the company's business which has expanded over time.

It was concluded that the audit process was effective. In view of the tenure of the current auditor, who were appointed in 2009 following a tendering process, it is recommended that the auditor be re-appointed. The company is committed to putting its audit out to tender at least every ten years. In the past there have been no contractual restrictions on which firms may be invited to tender but the nature of the company's business (life assurance) and its geographical scope do, in practice, limit the choice of firm to those with substantial life actuarial expertise and some international reach.

Provision of non-audit services and independence
The Committee has agreed a policy on the engagement of the audit firm for non-audit services. Automatic approval is granted where the service is clearly related to the process of audit services including the review of embedded value results and regulatory returns. In other cases the approval of the Committee is required, where generally the engagement would result from a tendering process where the audit firm was considered to be clearly superior to any of the other firms invited to tender. Exceptionally, however, in an acquisition process time pressures may make a tendering process impractical and/or conflicts of interest may preclude other suitable firms from being engaged. In these special circumstances the Committee (or its chairman alone where time pressures are very great) may approve the engagement of the auditor.

The Committee regularly monitors the level of fees paid for non-audit services to ensure, over a period of years, that these represent a low proportion of total fees paid. Reports from the auditor on independence are also reviewed annually and discussed with the auditor. It should be noted that total fees paid by the company are not material in the context of the overall business of the auditor.

Details of the fees paid to the external Auditor, and its associates, for both audit and non-audit services during the year are provided in Note 16 to the Financial Statements.

DIRECTORS' REPORT

Chesnara plc — Company No. 4947166
The Directors present their Annual Report and the audited consolidated financial statements of Chesnara plc ('Chesnara') for the year ended 31 December 2013. The Corporate Governance Report on pages 55 to 59 forms part of the Directors' Report.

The following information, that has been included by way of a cross reference to other areas of the Report & Accounts, is required by the Companies Act to be included within the Directors' report:

Requirements/reference

Financial risk management objectives and policies
The "Financial management" section on pages 40 to 43 and the "Risk management" section on pages 44 to 46.

Exposure to price risk, credit risk, liquidity risk and cash flow risk
Note 6 "Management of financial risk" to the IFRS Financial Statements.

Likely future developments
The "Business review" section on pages 18 to 27.

Greenhouse gas reporting
The "Corporate and social responsibility" section on pages 48 and 49.

Environmental, employee and social community matters
The "Corporate and social responsibility" section on pages 48 and 49.

Results and dividends

The Group consolidated statement of comprehensive income for the year ended 31 December 2013, prepared in accordance with International Financial Reporting Standards and set out on page 93, shows:

	2013 £000	2012 £000
Profit for year attributable to shareholders	49,363	27,941

An interim dividend of 6.25p per ordinary share was paid by Chesnara on 14 October 2013. The Board recommends payment of a final dividend of 11.63p per ordinary share on 22 May 2014 to shareholders on the register at the close of business on 11 April 2014.

Directors

Full details of the Directors who served in 2013 and will serve in 2014 is detailed in Corporate Governance Report on pages 55 to 59. Details of the Non-executive Directors who served as Chairmen and members of the Nominations and Audit & Risk Committees of the Board are set out in the Corporate Governance Report and Audit & Risk Committee reports respectively on pages 55 to 59 and 82 to 84. Information in respect of the Chairman and members of the Remuneration Committee and in respect of Directors' service contracts is included in the Remuneration Report on pages 60 to 81, which also includes details of Directors' interests in shares and share options.

All the Non-executive Directors will retire at the Annual General Meeting and, being eligible, offer themselves for re-election. All the Executive Directors have service contracts with the Company of no more than one year's duration and will offer themselves for re-election at least every three years. The service contracts of all the Directors will be available for inspection for 15 minutes prior to the Annual General Meeting. In addition, no Director had any material interest in any significant contract with the Company or with any of the subsidiary companies during the year.

The Directors benefited from qualifying third party indemnity provisions in place during the years ended 31 December 2012 and 31 December 2013 and the period to 27 March 2014.

Share capital

Details of the issued share capital, together with details of movements in the issued share capital of Chesnara plc during the year are shown in Note 44 which is incorporated by reference and deemed to be part of this report.

The Company has one class of ordinary share which carries no right to fixed income. Each share carries the right to one vote at general meetings of the Company. The ordinary shares are listed on the Official List and traded on the London Stock Exchange. As at 31 December 2013, the Company had 115,047,662 ordinary shares in issue, of which 194,183 were held as treasury shares.

In order to retain maximum flexibility, the Company proposes to renew the authority granted by ordinary shareholders at the Annual General Meeting in 2013, to repurchase up to just under 10% of its issued share capital. Further details are provided in the Notice of this year's Annual General Meeting.

At the Annual General Meeting in 2013, shareholders approved resolutions to allot shares up to an aggregate nominal value of £287,619 and to allot shares for cash other than pro rata to existing shareholders. Resolutions will be proposed at this year's Annual General Meeting to renew these authorities.

No person has any special rights of control over the Company's share capital and all issued shares are fully paid. There are no specific restrictions on the size of holding nor on the transfer of shares which are both governed by the general provisions of the Articles of Association and prevailing legislation. The Directors are not aware of any agreements between holders of the Company's shares that may result in restrictions on the transfer of securities or voting rights. The Directors have no current plans to issue shares.

An employee share scheme was introduced during 2011 which vests in 2014. All staff were eligible to join the scheme in which a maximum monthly investment of £250 can be used to buy shares at an option price of 173.4p per share.

Director appointments

With regard to the appointment and replacement of Directors, the Company follows the UK Corporate Governance Code and is governed by its Articles of Association, the Companies Act 2006 and related legislation. The Articles of Association may be amended by special resolution of the shareholders.

DIRECTORS' REPORT (CONTINUED)

Substantial shareholdings

The following substantial interests in the Company's ordinary share capital at 31 December 2013 have been notified to the Company:

Name of substantial shareholder	Total number of ordinary shares held	Percentage of the issued share capital as at 31 December 2013
Amerprise Financial, Inc. (Threadneedle Asset Management)	14,898,826	12.97
Artemis Investment Management LLP	11,423,003	9.95
Standard Life Investments Limited	4,172,345	3.63
Legal and General Group	4,130,698	3.60
Norges Bank	3,434,374	2.99
Hermes Equity Ownership Services	3,401,096	2.96

There have been changes to the position since 31 December 2013 and the revised holding is shown below. No other person holds a notifiable interest in the issued share capital of the Company.

Name of substantial shareholder	Total number of ordinary shares held	Percentage of the issued share capital as at 27 March 2014
Amerprise Financial, Inc. (Threadneedle Asset Management)	13,638,820	11.87
Artemis Investment Management LLP	5,730,793	4.99

There were no significant contracts with substantial shareholders during the year.

Charitable donations made by Group companies during the year ended 31 December 2012 were £nil (2012: £nil). No political contributions were made during the year ended 31 December 2013 (2012: £nil).

Employees

The average number of employees during the year was 146 (2012: 148).

Employee involvement

The Group believes that employee communication and consultation is important in enhancing the Company culture and connectivity, and in motivating and retaining employees. An open communications programme enables all employees to understand key strategies and other matters of interest and importance, quickly and efficiently. The communication includes face-to-face briefings, open discussion forums with senior management and email.

Chesnara plc currently operates a SAYE share scheme for its UK employees.

Going concern statement

After making appropriate enquiries, the Directors confirm that they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future. Accordingly, they continue to adopt the going concern basis in the preparation of the financial statements as stated in Note 2(c) to the financial statements. Detailed analysis of relevant risks and other factors is included within the Risk Management section on pages 44 to 46, within the Financial Management Section on pages 40 to 43 and within Notes 5 and 6 to the IFRS financial statements.

Disclosure of information to Auditor

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's Auditor is unaware; and each Director has taken all the steps that he ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's Auditor is aware of that information. This information is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Auditor

A resolution for the re-appointment of Deloitte LLP as Auditor of the Company is to be proposed at the forthcoming Annual General Meeting.

Approved by the Board on 27 March 2014 and signed on its behalf by:

David Rimmington
Finance Director

DIRECTORS' RESPONSIBILITIES STATEMENT

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors are required to prepare the group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Article 4 of the IAS Regulation and have also chosen to prepare the parent company financial statements under IFRSs as adopted by the EU. Under company law the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, International Accounting Standard 1 requires that directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the company's ability to continue as a going concern.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole;
- the strategic report includes a fair review of the development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the annual report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the company's performance, business model and strategy.

Peter Mason	Graham Kettleborough
Chairman	Chief Executive Officer
27 March 2014	27 March 2014

SECTION D

IFRS FINANCIAL STATEMENTS

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INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CHESNARA PLC

Opinion on financial statements of Chesnara plc

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2013 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

The financial statements comprise the Consolidated Statement of Comprehensive Income, the Consolidated and Company Balance Sheets, the Consolidated and Company Statements of Cash Flows, the Consolidated and Company Statements of Changes in Equity and the related notes 1 to 54. The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Going concern

As required by the Listing Rules we have reviewed the directors' statement contained within the Directors' Report on page 87 that the Group is a going concern. We confirm that:

- we have not identified material uncertainties related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern which we believe would need to be disclosed in accordance with IFRSs as adopted by the European Union; and
- we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's ability to continue as a going concern.

Our assessment of risks of material misstatement

The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team:

Risk	How the scope of our audit responded to the risk
Save and Prosper cost of guarantees The assessment of the cost of guarantee reserves in respect of policies written by Save and Prosper is complex and material, including the use of a stochastic model based on a variety of possible economic scenarios.	We have challenged the appropriateness of assumptions used in the model by benchmarking to external actuarial data. Where appropriate, sensitivity analysis was also performed to assess potential management bias. We developed an independent expectation of how the assumptions would impact the model and corroborated management's explanation and analysis to support such variations. We use actuarial specialists within our audit team to assist us in this challenge.
Policy administration expense assumptions The UK operations are largely outsourced and the appropriateness of assumptions relating to policy administration expenses can have a significant impact on the overall technical provisions held.	We have obtained legal contracts relating to outsourced activity, whether signed or in negotiation (i.e. in respect of any contracts reaching expiry) and compared these contracts to the estimated future expense assumptions applied in the calculation of technical provisions. We have also assessed the completeness of all expenses included within the provision.
Valuation rate of interest adjustments The determination of the valuation rate of interest applied in discounting the actuarial liabilities requires significant judgment particularly in relation to credit risk adjustments applied to non-government bond yields.	We evaluated the appropriateness of the principal assumptions used in the calculation of the valuation rate of interest for discounting the technical provisions including any credit risk adjustments. This involved benchmarking the assumptions used against those obtained from external data, including a comparison to those adopted by Industry peers, where available.

Risk	How the scope of our audit responded to the risk
Fair value accounting for the Protection Life acquisition The Group's assessment of the fair values of assets and liabilities recognised as part of the Protection Life acquisition is a judgemental process which will impact the quantum of profit relating to the transaction.	We have assessed the completeness of identified assets and liabilities, including any contingent liabilities, acquired as part of the transaction. In assessing the fair value of tangible and intangible assets acquired we have used internal actuarial specialists to assist in our challenge of the key assumptions relating to the estimated future cash flows, growth rates and the discount rate applied to the business acquired.
Valuation of the acquired in-force business intangible The recoverable value of the intangible acquired in-force business requires significant judgment in relation to estimation of the net present value of cash flows arising from pre-acquisition policies acquired in past business combinations.	We evaluated the recoverability of the acquired in-force business intangible assets by reviewing the mechanical accuracy of the net present value calculation, the level of headroom this calculation generated by reference to the carrying value of the asset and by challenging the appropriateness of the key assumptions used within the model. This included verifying that the cash flows used were the latest available cash flows and were used consistently throughout the business; assessment of key assumptions such as persistency rates for reasonableness; and performance of sensitivity analysis, for example in relation to discount rates applied in the calculation.

The Audit & Risk Committee's consideration of these risks is set out on pages 83 to 84.

Our audit procedures relating to these matters were designed in the context of our audit of the financial statements as a whole, and not to express an opinion on individual accounts or disclosures. Our opinion on the financial statements is not modified with respect to any of the risks described above, and we do not express an opinion on these individual matters.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

We determined materiality for the Group to be £6.3 million, which is below 3% of net assets.

We agreed with the Audit & Risk Committee that we would report to the Committee all audit differences in excess of £118,000, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit & Risk Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our Group audit scope focused primarily on the audit work at the 5 principal locations where the Group's policies are administered and which are underwritten by Countrywide Assured plc, Protection Life Company Limited and Movestic Livförsäkring AB the underwriting entities within the Group. All of these were subject to a full audit. Statutory audits were also performed for the legal entities referred to above and the statutory audits were executed at levels of materiality applicable to each individual entity which were lower than Group materiality.

The UK based audit teams performed the audit work directly at 4 of the 5 locations and at the remaining location continued to direct the work of the overseas audit team and to follow a programme of planned visits that has been designed so that the Senior Statutory Auditor or his designate visits this location at least once a year.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CHESNARA PLC (CONTINUED)

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records
Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' Remuneration
Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made or the part of the Directors' Remuneration Report to be audited is not in agreement with the accounting records and returns. Under the Listing Rules we are required to review certain elements of the Directors' Remuneration Report. We have nothing to report arising from these matters or our review.

Corporate Governance Statement
Under the Listing Rules we are also required to review the part of the Corporate Governance Statement relating to the company's compliance with nine provisions of the UK Corporate Governance Code. We have nothing to report arising from our review.

Our duty to read other information in the Annual Report
Under International Standards on Auditing (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- otherwise misleading.

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the Audit & Risk Committee which we consider should have been disclosed. We confirm that we have not identified any such inconsistencies or misleading statements.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent 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 financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

David Heaton (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Manchester, United Kingdom
27 March 2014

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December	Note	2013 £000	2012 £000
Insurance premium revenue		109,938	115,520
Insurance premium ceded to reinsurers		(35,469)	(35,336)
Net insurance premium revenue		**74,469**	**80,184**
Fee and commission income	**10**	69,990	66,658
Net investment return	**11**	567,463	332,053
Total revenue net of reinsurance payable		**711,922**	**478,895**
Other operating income	**12**	22,270	19,645
Total income net of investment return		**734,192**	**498,540**
Insurance contract claims and benefits incurred			
Claims and benefits paid to insurance contract holders	**13**	(281,800)	(272,479)
Net increase in insurance contract provisions	**13**	(62,249)	(20,732)
Reinsurers' share of claims and benefits	**13**	57,004	47,865
Net insurance contract claims and benefits		(287,045)	(245,346)
Change in investment contract liabilities	**14**	(320,132)	(156,663)
Reinsurers' share of investment contract liabilities	**14**	5,568	2,810
Net change in investment contract liabilities		(314,564)	(153,853)
Fees, commission and other acquisition costs	**15**	(19,450)	(17,967)
Administrative expenses	**16**	(38,761)	(37,029)
Other operating expenses			
Charge for amortisation of acquired value of in-force business	**17**	(7,530)	(7,863)
Charge for amortisation of acquired value of customer relationships	**17**	(301)	(391)
Other	**17**	(6,483)	(9,205)
Total expenses net of change in insurance contract provisions and investment contract liabilities		**(674,134)**	**(471,654)**
Total income less expenses		**60,058**	**26,886**
Share of profit of associate	**25**	1,252	1,244
Profit recognised on business combination	**7**	2,807	–
Exceptional item	**8**	–	(4,778)
Financing costs	**18**	(3,527)	(3,670)
Profit before income taxes	**9**	**60,590**	**19,682**
Income tax (expense)/credit			
Before exceptional item	**19**	(11,227)	3,481
Exceptional item	**8**	–	4,778
After exceptional item		(11,227)	8,259
Profit for the year	**9**	**49,363**	**27,941**
Foreign exchange translation differences arising on the revaluation of foreign operations		(516)	741
Total comprehensive income for the year		**48,847**	**28,682**
Basic earnings per share (based on profit for the year)	**49**	42.98p	24.33p
Diluted earnings per share (based on profit for the year)	**49**	42.98p	24.33p

The notes and information on pages 100 to 175 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

31 December	Note	2013 £000	2012 £000
Assets			
Intangible assets			
Deferred acquisition costs	20	28,162	22,555
Acquired value of in-force business	21	88,615	76,118
Acquired value of customer relationships	22	1,583	1,884
Software assets	23	5,004	5,712
Property and equipment	24	673	369
Investment in associates	25	4,088	2,902
Investment properties	26	20,387	100,167
Deferred tax assets	38	–	2,295
Reinsurers' share of insurance contract provisions	33	379,894	278,692
Amounts deposited with reinsurers	34	34,293	30,245
Financial assets			
Equity securities at fair value through income	27	479,617	427,303
Holdings in collective investment schemes at fair value through income	27	3,440,992	3,009,799
Debt securities at fair value through income	27	370,666	363,377
Policyholders' funds held by the Group	27	130,237	61,171
Insurance and other receivables	27/28	46,382	24,313
Prepayments	27/28	4,889	3,160
Derivative financial instruments	27/29	2,956	3,095
Total financial assets		4,475,739	3,892,218
Reinsurers' share of accrued policyholder claims	40	11,399	4,489
Income taxes	30	2,608	4,299
Cash and cash equivalents	31	184,263	228,676
Total assets		**5,236,708**	**4,650,621**
Liabilities			
Insurance contract provisions	33	2,362,063	2,207,078
Other provisions	37	5,348	5,161
Financial liabilities			
Investment contracts at fair value through income	34	2,283,403	2,022,314
Liabilities relating to policyholders' funds held by the Group	35	130,237	61,171
Borrowings	36	94,377	48,324
Derivative financial instruments	29	387	286
Total financial liabilities		2,508,404	2,132,095
Deferred tax liabilities	38	11,007	5,894
Reinsurance payables	39	11,539	16,610
Payables related to direct insurance and investment contracts	40	47,137	38,894
Deferred income	41	7,865	8,884
Income taxes	42	8,012	–
Other payables	43	27,104	17,057
Bank overdrafts	31	1,127	602
Total liabilities		**4,989,606**	**4,432,275**
Net assets	9	**247,102**	**218,346**
Shareholders' equity			
Share capital	44	42,024	42,024
Share premium	44	42,526	42,523
Treasury shares	45	(212)	(217)
Other reserves	46	7,203	7,719
Retained earnings	47	155,561	126,297
Total shareholders' equity		**247,102**	**218,346**

The notes and information on pages 100 to 175 form part of these financial statements.

Approved by the Board of Directors on 27 March 2014 and signed on its behalf by:

Peter Mason
Chairman

Graham Kettleborough
Chief Executive Officer

COMPANY BALANCE SHEET

31 December	Note	2013 £000	2012 £000
Assets			
Non-current assets			
Financial assets			
Investment in subsidiaries	**27**	199,111	146,699
Current assets			
Receivables and prepayments	**28**	636	585
Income taxes	**30**	2,194	1,394
Cash and cash equivalents	**31**	37,489	32,412
Total current assets		**40,319**	**34,391**
Total assets		**239,430**	**181,090**
Current liabilities			
Borrowings	**36**	8,897	7,844
Other provisions	**37**	591	399
Other payables	**43**	2,434	2,725
Total current liabilities		**11,922**	**10,968**
Non-current liabilities			
Borrowings	**36**	64,143	21,818
Other provisions	**37**	2,715	3,405
Total non-current liabilities		**66,858**	**25,223**
Total liabilities		**78,780**	**36,191**
Net assets		**160,650**	**144,899**
Shareholders' equity			
Share capital	**44**	5,752	5,752
Share premium	**44**	42,526	42,523
Treasury shares	**45**	(212)	(217)
Other reserves	**46**	50	50
Retained earnings	**47**	112,534	96,791
Total shareholders' equity		**160,650**	**144,899**

The notes and information on pages 100 to 175 form part of these financial statements.

The financial statements of Chesnara plc (registered number 4947166) were approved by the Board of Directors on 27 March 2014 and signed on its behalf by:

Peter Mason
Chairman

Graham Kettleborough
Chief Executive Officer

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December	2013 £000	2012 £000
Profit for the year	**49,363**	**27,941**
Adjustments for:		
Depreciation of property and equipment	177	128
Amortisation of deferred acquisition costs	9,386	7,657
Amortisation of acquired value of in-force business	7,530	7,864
Amortisation of acquired value of customer relationships	301	391
Amortisation of software assets	2,580	2,188
Tax paid/(recovered)	11,227	(8,259)
Interest receivable	(19,256)	(25,961)
Dividends receivable	(19,049)	(46,774)
Interest expense	3,527	3,670
Change in fair value of investment properties	6,197	5,650
Fair value gains on financial assets	(523,938)	(254,457)
Profits on sale of property and equipment	(10)	(2)
Profit arising on business combination	(2,807)	–
Share of profit of associate	(1,252)	(1,244)
Interest received	18,701	26,357
Dividends received	19,252	46,738
Increase in intangible assets related to insurance and investment contracts	(19,397)	(10,255)
Changes in operating assets and liabilities		
Decrease in financial assets	46,539	145,971
Increase in reinsurers' share of insurance contract provisions	(14,596)	(14,138)
Increase in amounts deposited with reinsurers	(4,048)	(2,214)
(Increase)/decrease in insurance and other receivables	(5,267)	402
(Increase)/decrease in prepayments	(1,792)	96
Increase in insurance contract provisions	51,570	15,271
Increase in investment contract liabilities	351,630	140,360
(Decrease)/increase in provisions	(1,829)	2,336
(Decrease)/increase in reinsurance payables	(5,182)	88
Increase/(decrease) in payables related to direct insurance and investment contracts	2,110	(1,795)
Increase/(decrease) in other payables	3,690	(3,251)
Cash (utilised by)/generated from operations	**(34,643)**	**64,758**
Income tax received/(paid)	1,405	(1,152)
Net cash (utilised by)/generated from operating activities	**(33,238)**	**63,606**
Cash flows from investing activities		
Business combinations	(31,924)	–
Development of software	(1,882)	(1,094)
Purchases of property and equipment	(485)	(109)
Net cash utilised by investing activities	**(34,291)**	**(1,203)**
Cash flows from financing activities		
Proceeds from issue of share capital	3	–
Proceeds from/(repayment of) borrowings	46,728	(6,406)
Sale treasury shares	5	–
Dividends paid	(20,099)	(19,525)
Interest paid	(3,975)	(3,949)
Net cash generated by/(utilised by) financing activities	**22,662**	**(29,880)**
Net (decrease)/increase in cash and cash equivalents	**(44,867)**	**32,523**
Cash and cash equivalents at beginning of year	228,074	195,086
Effect of exchange rate changes on cash and cash equivalents	(71)	465
Cash and cash equivalents at end of the year	**183,136**	**228,074**

The notes and information on pages 100 to 175 form part of these financial statements.

COMPANY STATEMENT OF CASH FLOWS

Year ended 31 December	2013 £000	2012 £000
Profit for the year	**35,841**	**39,668**
Adjustments for:		
Tax recovery	(800)	(1,420)
Interest expense	1,383	1,218
Dividends receivable	(40,000)	(44,000)
Changes in operating assets and liabilities		
Increase in loans and receivables	(80)	(310)
Increase in prepayments	29	21
(Decrease)/increase in provisions	(498)	2,304
(Decrease)/increase in other payables	(317)	669
Cash utilised by operating activities	**(4,442)**	**(1,850)**
Income tax received	–	1,223
Net cash utilised by operating activities	**(4,442)**	**(627)**
Cash flows from investing activities		
Acquisition of subsidiary company	(52,412)	–
Dividends received from subsidiary company	40,000	44,000
Net cash (utilised by)/generated from investing activities	**(12,412)**	**44,000**
Cash flows from financing activities		
Net proceeds from the issue of share capital	3	–
Net proceeds from/(repayment of) borrowings	43,800	(6,000)
Dividends paid	(20,099)	(19,525)
Interest paid	(1,778)	(1,073)
Sale of Treasury Shares	5	–
Net cash generated from/(utilised by) financing activities	**21,931**	**(26,598)**
Net increase in cash and cash equivalents	**5,077**	**16,775**
Cash and cash equivalents at beginning of year	32,412	15,637
Cash and cash equivalents at end of the year	**37,489**	**32,412**

The notes and information on pages 100 to 175 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2013	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2013	**42,024**	**42,523**	**7,719**	**(217)**	**126,297**	**218,346**
Profit for the year	–	–	–	–	49,363	49,363
Dividends paid	–	–	–	–	(20,099)	(20,099)
Foreign exchange translation differences	–	–	(516)	–	–	(516)
Sale of treasury shares	–	3	–	5	–	8
Equity shareholders' funds at 31 December 2013	**42,024**	**42,526**	**7,203**	**(212)**	**155,561**	**247,102**

Year ended 31 December 2012	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2012	**42,024**	**42,523**	**6,978**	**(217)**	**117,881**	**209,189**
Profit for the period	–	–	–	–	27,941	27,941
Dividends paid	–	–	–	–	(19,525)	(19,525)
Foreign exchange translation differences	–	–	741	–	–	741
Equity shareholders' funds at 31 December 2012	**42,024**	**42,523**	**7,719**	**(217)**	**126,297**	**218,346**

The notes and information on pages 100 to 175 form part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2013

	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2013	**5,752**	**42,523**	**50**	**(217)**	**96,791**	**144,899**
Profit for the year	–	–	–	–	35,841	35,841
Dividends paid	–	–	–	–	(20,098)	(20,098)
Sale of treasury shares	–	3	–	5	–	8
Equity shareholders' funds at 31 December 2013	**5,752**	**42,526**	**50**	**(212)**	**112,534**	**160,650**

Year ended 31 December 2012

	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2012	**5,752**	**42,523**	**50**	**(217)**	**76,648**	**124,756**
Profit for the year	–	–	–	–	39,668	39,668
Dividends paid	–	–	–	–	(19,525)	(19,525)
Equity shareholders' funds at 31 December 2012	**5,752**	**42,523**	**50**	**(217)**	**96,791**	**144,899**

The notes and information on pages 100 to 175 form part of these financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 General information

Chesnara plc (Registered Number 4947166) (the Company) is a limited liability company incorporated and domiciled in England and Wales and has a primary listing on the London Stock Exchange. The address of the registered office is Harbour House, Portway, Preston, PR2 2PR, UK.

The Company and its subsidiaries, together forming the Group, comprise UK and Swedish life and pensions businesses.

The UK businesses, which comprise the CA, S&P and PL segments described in Note 9, the activities of which are performed entirely in the UK, underwrite life risks such as those associated with death, disability and health and provide a portfolio of investment contracts for the savings and retirement needs of customers through asset management. They are substantially closed to new business, such that new insurance contracts are only issued to existing customers, dependent on their changing needs.

The Swedish business, which comprises the Movestic segment, described in Note 9, the activities of which are performed predominantly in Sweden, underwrites life, accident and health risks and provides a portfolio of investment contracts. It is open to new business, securing distribution of its products principally through independent financial advisers.

These financial statements are presented in pounds sterling, which is the functional currency of the Parent Company. Foreign operations are included in accordance with the policies set out in Note 2. The financial statements were authorised for issue by the Directors on 27 March 2014.

2 Significant accounting policies

In the information which follows distinction is made, where necessary, in respect of the applicability of certain policies, or as to their clarification:

(i) as between the UK businesses and the Swedish business, which comprises the Movestic segment; and

(ii) as between the CA, S&P and PL segments of the UK businesses.

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (`IFRSs') as adopted by the European Union ('Adopted IFRSs') and therefore comply with Article 4 of the EU IAS Regulation. Both the Parent Company financial statements and the Group financial statements have been prepared and approved by the Directors in accordance with Adopted IFRSs.

Adoption of new and revised standards

In the current year the following new and revised Standards and Interpretations have been adopted that affected the 2013 Group Financial Statements:

- Amendments to IFRS 7: Disclosures – Offsetting financial assets and financial liabilities: This requires disclosure of the effect or potential effects of netting arrangements on an entity's financial position. The amendments have been applied retrospectively, with associated disclosures in Note 27.
- IFRS 13 Fair Value measurement: IFRS 13 provides comprehensive guidance on how to calculate the fair value of financial and non-financial assets. The adoption of IFRS 13 did not have a material financial impact on the Group.

At the date of authorisation of these financial statements the following Standards and Interpretations, which are applicable to the Group and which have not been applied in these financial statements, were in issue but not yet effective (and in some cases have not been adopted by the EU):

Title	Subject
Annual Improvements to IFRSs: 2011-13 Cycle (Dec 2013)	Annual Improvements to IFRSs: 2011-13 Cycle
Annual Improvements to IFRSs: 2010-12 Cycle (Dec 2013)	Annual Improvements to IFRSs: 2010-12 Cycle
Amendments to IAS 19 (Nov 2013)	Defined Benefit Plans: Employee Contributions
Amendments to IAS 39 (Jun 2013)	Novation of Derivatives and Continuation of Hedge Accounting
Amendments to IAS 36 (May 2013)	Recoverable Amount Disclosures for Non-Financial Assets
IFRIC 21	Levies
Amendments to IFRS 10, IFRS 12 and IAS 27 (Oct 2012)	Investment Entities
Amendments to IAS 32 (Dec 2011)	Offsetting Financial Assets and Financial Liabilities
IFRS 9	Financial Instruments
IFRS 12	Disclosure of Interests in Other Entities
IFRS 11	Joint Arrangements
IFRS 10	Consolidated Financial Statements
IAS 28 (revised May 2011)	Investments in Associates and Joint Ventures
IAS 27 (revised May 2011)	Separate Financial Statements

The Directors do not expect that the adoption of the standards listed above will have a material impact on the financial statements of the Group in future periods, except as follows:

- IFRS 9 will impact both the measurement and disclosures of Financial Instruments; and
- IFRS 12 will impact the disclosures of interests Chesnara plc has in other entities.

Beyond the information above, it is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

In publishing the Parent Company financial statements together with the Group financial statements the Company has taken advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements. The Parent Company profit for the year has been disclosed in Note 47.

(b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and of entities controlled by the Company (its subsidiaries), made up to 31 December each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities. The Parent Company financial statements present information about the Company as a separate entity and not about its Group.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling interest's share of changes in equity since the date of the combination.

Profit or loss and each component of other comprehensive income are attributed to the Company and to the non-controlling interests. Total comprehensive income is attributed to the Company shareholders and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

The results of subsidiaries acquired or disposed of during the year are included in the Consolidated Statement of Comprehensive Income from the effective date of acquisition or up to the effective date of disposal. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

(c) Basis of preparation

The Consolidated and Parent Company financial statements have been prepared on a going concern basis. The Directors believe that they have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. In making this assessment, the Directors have taken into consideration the points as set out in the Financial Management section under the heading 'Going Concern'.

The financial statements are presented in pounds sterling, rounded to the nearest thousand and are prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments, financial instruments at fair value through income, assets and liabilities held for sale, investment property and investment contract liabilities at fair value through income.

Assets and liabilities are presented on a current and non-current basis in the notes to the financial statements. If assets are expected to be recovered or liabilities expected to be settled within a year, they are classified as current. If they are expected to be recovered or settled in more than one year, they are classified as non-current.

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years. Judgements made by management in the process of applying the Group's accounting policies that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are set out in Note 3.

The accounting policies set out below, unless otherwise stated, have been applied consistently to all years presented in these consolidated financial statements.

These financial statements have also been prepared in accordance with the disclosure provisions of FRS 27 'Life Assurance', which was issued by the UK's Accounting Standards Board (ASB) in December 2004. FRS 27 adds to the requirements of IFRS but does not vary them in any way.

(d) Business combinations

The Group uses the purchase method of accounting to account for the acquisition of subsidiaries. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Expenses directly attributable to the acquisition are expensed as incurred. The acquiree's identifiable assets, liabilities, and contingent liabilities, which meet the conditions for recognition under IFRS 3, are measured initially at their fair values at the acquisition date. Gains arising on a bargain purchase, where the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquiree exceeds the cost of acquisition, is recognised in the Consolidated Statement of Comprehensive Income at the acquisition date.

The non-controlling interest in the acquiree is initially measured at the non-controlling interest's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

(e) Investments in associates

An associate is an entity over which the Group is in a position to exercise significant influence, but not control or joint control, through participation in the financial and operating policy decisions of the investee. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting. Investments in associates are carried in the balance sheet at cost as adjusted by post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments.

Where a Group company transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the associate. Losses may provide evidence of an impairment of assets transferred, in which case appropriate provision is made for impairment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(f) Foreign currencies

The individual financial statements of each Group company are presented in the currency of the primary economic environment in which it operates, being its functional currency. For the purpose of these consolidated financial statements, the results and financial position of each Group company are expressed in pounds sterling, which is the functional currency of the Parent Company and the presentation currency of the consolidated financial statements.

In preparing the financial statements of the individual companies, transactions in currencies other than the entity's functional currency, being foreign currencies, are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities which are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value, which are denominated in foreign currencies, are translated at the rates prevailing when the fair value was determined. Exchange differences are recognised in the Consolidated Statement of Comprehensive Income in the period in which they arise, except when they relate to items for which gains and losses are recognised in equity.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during the period, in which case the exchange rates at the dates of transactions are used. Exchange differences arising are classified as equity and are recognised in the Group's foreign currency translation reserve. Such translation differences are recognised as income or as expense in the period in which the operation is disposed of.

Transactions relating to business combinations denominated in foreign currencies are translated into sterling at the exchange rates prevailing on the transaction date.

(g) Product classification

The Group's products are classified at inception as either insurance or investment contracts for accounting purposes. Insurance contracts are contracts which transfer significant insurance risk and remain as insurance contracts until all rights and obligations are extinguished or expire. They may also transfer financial risk. Investment contracts are contracts which carry financial risk, with no significant insurance risk. Where contracts contain both insurance and investment components and the investment components can be measured reliably, the contracts are unbundled and the components are separately accounted for as insurance contracts and investment contracts respectively.

In some insurance contracts and investment contracts the financial risk is borne by the policyholders. Such contracts are usually unit-linked contracts.

With-profits contracts, which subsist only within the UK businesses, all contain a discretionary participation feature (''DPF'') which entitles the holder to receive, as a supplement to guaranteed benefits, additional benefits or bonuses, which may be a significant portion of the total contractual benefits.

In respect of S&P the amount and timing of such contractual benefits are at the discretion of the Group and are contractually based on realised and/or unrealised investment returns on a specified pool of assets held by the Group. The terms and conditions of these contracts, together with UK regulations, set out the bases for the determination of the amounts on which the additional discretionary benefits are based and within which the Group may exercise its discretion as to the quantum and timing of their payment to contract holders.

In respect of CA all such contracts are wholly reinsured with Guardian Assurance Limited ('Guardian'), and the amount or timing of the additional payments are contractually at the discretion of the reinsurer and are contractually based on:

(i) the performance of a specified pool of contracts or a specified type of contract;

(ii) realised and/or unrealised investment returns on a specified pool of assets held by the reinsurer; or

(iii) the profit or loss of the reinsurer.

All contracts with discretionary participation features are classified as insurance contracts.

PL does not have any contracts containing discretionary participation features.

(h) Insurance contracts

There are fundamental differences between the nature of the insurance contracts subsisting in the UK and Swedish businesses, including inter alia contract longevity: the related product characteristics are set out for the separate UK and Swedish businesses in Note 5. As a consequence, the alignment of income and expense recognition with the underlying assumption of risk leads to the adoption of separate accounting policies appropriate to each business, as follows:

(h) Insurance contracts (continued)

UK businesses

(i) Premiums

Premiums are accounted for when due, or in the case of unit-linked insurance contracts, when the liability is recognised, and exclude any taxes or duties based on premiums. Outward reinsurance premiums are accounted for when due.

(ii) Claims and benefits

Claims are accounted for in the accounting period in which they are due or notified. Surrenders are accounted for in the accounting period in which they are paid. Claims include policyholder bonuses allocated in anticipation of a bonus declaration. Reinsurance recoveries are accounted for in the same period as the related claim.

(iii) Acquisition costs

Acquisition costs comprise all direct and indirect costs arising from the conclusion of insurance contracts. They are initial fees amortised at a rate based on the pattern of anticipated margins in respect of the related policies. An explicit deferred acquisition cost asset is established in the balance sheet to the extent that acquisition costs exceed initial fees deducted. At 31 December each year, such costs that are deferred to future years are reviewed to ensure they do not exceed available future margins.

Renewal commission and other direct and indirect acquisition costs arising on enhancements to existing contracts are expensed as incurred.

(iv) Measurement of insurance contract provisions

Insurance contract provisions are measured using accounting policies having regard to the principles laid down in Council Directive 2002/83/EC.

Insurance contract provisions are determined following an annual actuarial investigation of the long-term funds and are calculated initially on a statutory solvency basis in order to comply with the reporting requirements of the Prudential Sourcebook for Insurers. This valuation is then adjusted to remove certain contingency reserves and to remove excess prudence from other reserves. In accordance with this, the provisions are calculated on the basis of current information, using the specific valuation methods set out below.

Unit-linked provisions are measured by reference to the value of the underlying net asset value of the Group's unitised investment funds, determined on a bid value basis, at the balance sheet date.

For immediate annuities in payment the provision is calculated as the discounted value of the expected future annuity payments under the policies, allowing for mortality, including projected improvements in future mortality, interest rates and expenses. For certain temporary annuities in payment no allowance for mortality has been made.

In respect of S&P, for those classes of non-linked business with a discretionary participation feature, a gross premium method has been used to value the liability, whereby expected income and costs have been projected, allowing for mortality, interest rates and expenses.

For the other classes of non-linked business the provision is calculated on a net premium basis, being the level of premium consistent with a premium stream, the discounted value of which, at the outset of the policy, would be sufficient to cover exactly the discounted value of the original guaranteed benefits at maturity, or at death if earlier, on the valuation basis. The provision is then calculated by subtracting the present value of future net premiums from the present value of the benefits guaranteed at maturity, or death if earlier, as a result of events up to the balance sheet date. Negative provisions do not arise under the net premium method, which makes no allowances for voluntary discontinuances by policyholders, and which only implicitly allows for future policy maintenance costs.

In respect of CA for those classes of non-linked and unit-linked business where policyholders participate in profits the liability is wholly reassured to Guardian. The liability is calculated on a net premium basis, but is then increased to the realistic liability as a result of the liability adequacy test.

In respect of PL, this segment does not carry any contracts with discretionary participation features.

Insurance contract provisions are tested for adequacy by discounting current estimates of all contractual cash flows and comparing this amount to the carrying value of the provision and any related assets: this is known as the liability adequacy test. Where a shortfall is identified, an additional provision is made and the Group recognises the deficiency in income for the year.

Insurance contract provisions can never be definitive as to their timing or the amount of claims and are therefore subject to subsequent reassessment on a regular basis.

Swedish business – life

(i) Premiums

Premiums are accounted for when received, and exclude any taxes or duties based on premiums. Outward reinsurance premiums are accounted for when due.

(ii) Claims and benefits

Claims are accounted for in the accounting period in which they are due or notified. Reinsurance recoveries are accounted for in the same period as the related claim.

(iii) Acquisition costs

Acquisition costs comprise expenditure incurred arising from the completion of insurance contracts. They are initial fees amortised at a rate based on the pattern of anticipated margins in respect of the related policies. An explicit deferred acquisition cost asset is established in the balance sheet to the extent that acquisition costs exceed initial fees deducted. At the end of each year, such costs that are deferred to future years are reviewed to ensure they do not exceed available future margins.

Renewal commission and other direct and indirect acquisition costs arising on enhancements to existing contracts are expensed as incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(h) Insurance contracts (continued)

Swedish business – life (continued)

(iv) Measurement of insurance contract provisions

Provision is made at the year-end for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported. The estimated cost of claims includes expenses to be incurred in settling claims. Outstanding claim provisions are not discounted other than for income protection and waiver of premium benefits, where payments may be made for a considerable period of time.

All reasonable steps are taken to ensure that there is appropriate information regarding claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

Insurance contract provisions are tested for adequacy by discounting current estimates of all contractual cash flows and comparing this amount to the carrying value of the provision and any related assets: this is known as the liability adequacy test. Where a shortfall is identified, an additional provision is made and the deficiency in income for the year is recognised.

Swedish business – non-life

(i) Premiums

Written premiums for non-life (general) insurance business comprise the premiums on contracts incepting in the financial year. Written premiums are stated gross of commission payable to intermediaries and exclusive of taxes and duties paid on premiums.

Unearned premiums are those proportions of the premium which relate to periods of risk after the balance sheet date. Unearned premiums are calculated on a straight-line basis according to the duration of the policy underwritten.

(ii) Acquisition costs

Acquisition costs, which represent commission payable, incurred in writing written premiums, are deferred and amortised over the period in which the related premiums are earned.

(iii) Claims

Claims incurred

Claims incurred comprise claims and related expenses paid in the year and changes in provisions for outstanding claims, including provisions for claims incurred but not yet reported and related expenses, together with any adjustments to claims from previous years.

Outstanding claims provisions

Provision is made at the year-end for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported. The estimated cost of claims includes expenses to be incurred in settling claims. Outstanding claims provisions are not discounted. Provisions are calculated gross of any reinsurance recoveries.

All reasonable steps are taken to ensure that there is appropriate information regarding claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

The estimation of outstanding claims provisions is described in Note 33.

(i) Investment contracts

(i) Amounts collected

Amounts collected on investment contracts, which primarily involve the transfer of financial risk such as long-term savings contracts, are accounted for using deposit accounting, under which the amounts collected, less any initial fees deducted, are credited directly to the balance sheet as an adjustment to the liability to the investor.

(ii) Amounts deposited with reinsurers

Amounts deposited with reinsurers under reinsurance arrangements, which primarily involve the transfer of financial risk, are entered directly to the balance sheet as amounts deposited with reinsurers. These assets are designated on initial recognition as at fair value through income.

(iii) Benefits

For investment contracts, benefits paid are not included in the income statement but are instead deducted from investment contract liabilities in the accounting period in which they are paid.

(iv) Acquisition costs

Acquisition costs relating to investment contracts comprise directly attributable incremental acquisition costs, which vary with, and are related to, securing new contracts, and are recognised as an asset to the extent that they represent the contractual right to benefit from the provision of investment management services. The asset is presented as a deferred acquisition cost asset and is amortised over the expected term of the contract, as the fees relating to the provision of the services are recognised. All other costs are recognised as expenses when incurred.

(v) Liabilities

All investment contract liabilities are designated on initial recognition as held at fair value through income. The Group has designated investment contract liabilities at fair value through income as this more closely reflects the basis on which the businesses are managed.

The financial liability in respect of unit-linked contracts is measured by reference to the value of the underlying net asset value of the unitised investment funds, determined on a bid value, at the balance sheet date.

For the UK businesses, deferred tax on unrealised capital gains and for the Swedish business a yield tax in respect of an estimate of the investment return on the underlying investments in the unitised funds are also reflected in the measurement of the respective unit-linked liabilities.

In respect of the UK businesses guaranteed income and guaranteed growth bond liabilities and other investment contract liabilities are managed together with related investment assets on a fair value basis as part of the documented risk management strategy.

The fair value of other investment contracts is measured by discounting current estimates of all contractual cash flows that are expected to arise under contracts.

(j) Reinsurance

The Group cedes reinsurance in the normal course of business for the purpose of avoiding the retention of undue concentration of risk on any one life, policyholder or loss event (for example multiple losses under a Group Life contract). Assets, liabilities and income and expense arising from ceded reinsurance contracts are presented separately from the related assets, liabilities, income and expenses from the related insurance contracts because the reinsurance arrangements do not relieve the Group from its direct obligations to its policyholders.

Only rights under contracts that give rise to a significant transfer of insurance risk are accounted for as reinsurance assets, which comprise amounts due from insurance companies for paid and unpaid losses and ceded life policy benefits. Rights under contracts that do not transfer significant insurance risk are accounted for as financial instruments and are presented as amounts deposited with reinsurers.

The net premiums payable to a reinsurer may be more or less than the reinsurance assets recognised by the Group in respect of the reinsurance cover purchased. Any gain or loss is recognised in the income statement in the period in which the reinsurance premiums are payable.

Rights under reinsurance contracts comprising the reinsurers' share of insurance contract provisions and accrued policyholder claims are estimated in a manner that is consistent with the measurement of the provisions held in respect of the related insurance contracts and in accordance with the terms of the reinsurance contract. Such assets are deemed impaired if there is objective evidence, as a result of an event that occurred after its initial recognition, that the Group may not recover all amounts due and the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer. Impairment losses reduce the carrying value of the related reinsurance assets to their recoverable amount and are recognised as an expense in the income statement.

The Group enters into certain financing arrangements, which are established in the form of a reinsurance contract, but which are substantively in the form of a financial instrument. Such arrangements are classified and presented as borrowings within financial liabilities.

(k) Fee and commission income

Fees charged for investment management services provided in connection with investment contracts are recognised as revenue as the services are provided. Initial fees which exceed the level of recurring fees and relate to the future provision of services are deferred and amortised over the anticipated period in which services will be provided.

Initial fees charged for investment management services provided in connection with insurance contracts are recognised as revenue when earned.

For both insurance and investment contracts, initial fees, annual management charges and contract administration charges are recognised as revenue on an accruals basis. Surrender charges are recognised as a reduction to policyholder claims and benefits incurred when the surrender benefits are paid.

Benefit-based fees comprising charges made to unit-linked insurance and investment funds for mortality and morbidity benefits are recognised as revenue on an accruals basis.

For insurance and investment contracts, commissions received or receivable which do not require the Group to render further services are recognised as revenue by the Group on the effective commencement or renewal dates of the related contract. However, when it is probable that the Group will be required to render further services during the life of the contract, the commission, or part thereof, is deferred and recognised as revenue over the period in which services are rendered.

(l) Investment income

Investment income comprises income from financial assets and rental income from investment properties.

Income from financial assets comprises dividend and interest income, net fair value gains and losses (both unrealised and realised) in respect of financial assets classified as fair value through income, and realised gains on financial assets classified as loans and receivables.

Dividends are accrued on an ex-dividend basis. Interest received and receivable in respect of interest-bearing financial assets classified as at fair value through income is included in net fair value gains and losses. For loans and receivables and cash and cash equivalents interest income is calculated using the effective interest method.

Rental income from investment properties under operating leases is recognised in the Consolidated Statement of Comprehensive Income on a straight-line basis over the term of each lease. Lease incentives are recognised in the Consolidated Statement of Comprehensive Income as an integral part of the total lease income.

(m) Expenses

(i) Operating lease payments

Leases where a significant proportion of the risks and rewards of ownership is retained by the lessor are classified as operating leases. Payments made under operating leases are recognised in the Consolidated Statement of Comprehensive Income on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

(ii) Financing costs

Financing costs comprise interest payable on borrowings and on reinsurance claims deposits included within reinsurance payables, calculated using the effective interest rate method.

(n) Income taxes

Income tax on the profit or loss for the year comprises current and deferred tax and is recognised in the Consolidated Statement of Comprehensive Income. Tax that relates directly to transactions reflected within equity is also presented within equity.

(i) Current tax

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(n) Income taxes (continued)

(ii) Deferred tax

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(iii) Policyholders' fund yield tax

Certain of the Group's policyholders within the Swedish business are subject to a Swedish yield tax which is calculated based on an estimate of the investment return on underlying investments within their unitised funds. The Group is under an obligation to deduct the yield tax from the policyholders' unitised funds and to remit these deductions to the tax authorities. The remittance of this tax payment is included in other operating expenses as it does not comprise a tax charge on Group profits.

(o) Acquired value of in-force business

Acquired in-force insurance and investment contracts arising from business combinations are measured at fair value at the time of acquisition.

The difference between the fair value of insurance contracts and the liability measured in accordance with the Group's accounting policies for the contracts is recorded as acquired present value of in-force business. Present value of in-force business is carried gross of tax and is amortised against income on a time profile which, it is intended, will broadly match the profile of the underlying emergence of surplus as anticipated at the time of acquisition. The present value of in-force insurance contracts is tested for recoverability/impairment as part of the liability adequacy test.

The present value of in-force investment contracts is stated at cost less accumulated amortisation and impairment losses. The initial cost is deemed to be the fair value of the contractual customer relationships acquired. The acquired present value of the in-force investment contracts is carried gross of tax and is amortised against income on a time profile which, it is intended, will broadly match the profile of the underlying emergence of profit from the contracts. The recoverable amount is estimated at each balance sheet date. If the recoverable amount is less than the carrying amount, an impairment loss is recognised in the Consolidated Statement of Comprehensive Income and the carrying amount is reduced to its recoverable amount.

(p) Acquired value of customer relationships

The acquired value of customer relationships arising from business combinations is measured at fair value at the time of acquisition. This comprises the discounted cash flows relating to new insurance and investment contracts which are expected to arise from existing customer relationships. These are carried gross of tax, are amortised in accordance with the expected emergence of profit from the new contracts and are tested periodically for recoverability.

(q) Software assets

An intangible asset in respect of internal development software costs is only recognised if all of the following conditions are met:

(i) an asset is created that can be identified;

(ii) it is probable that the asset created will generate future economic benefits; and

(iii) the development costs of the asset can be measured reliably.

Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred. Software assets, including internally developed software, are amortised on a straight-line basis over their estimated useful life, which typically varies between 3 and 5 years.

(r) Property and equipment

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses.

Depreciation is charged to the Consolidated Statement of Comprehensive Income on a straight-line basis over the estimated useful economic lives of the property and equipment on the following basis:

Computers and similar equipment	3 years
Fixtures and other equipment	5 years

Assets held under finance leases are depreciated over their useful economic lives on the same basis as owned assets, or where shorter, over the term of the relevant lease.

(s) Investment property

Investment properties are properties which are held either to earn rental income or for capital appreciation or for both. On initial recognition investment properties are measured at cost including attributable transaction costs, and are subsequently measured at fair value. Independent external valuers, having an appropriate recognised professional qualification and recent experience in the location and category of property being valued, value the portfolio every twelve months.

The fair values reflect market values at the balance sheet date, being the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

Any gain or loss arising from a change in fair value is recognised in the Consolidated Statement of Comprehensive Income. Rental income from investment property is accounted for as described in accounting policy (l).

(t) Financial assets

Investments in subsidiaries are carried in the Company balance sheet at cost less impairment.

Financial assets are classified into different categories depending on the type of asset and the purpose for which it is acquired. Currently two different categories of financial assets are used: 'financial assets at fair value through income' and 'loans and receivables'. Financial assets classified as at fair value through income comprise financial assets designated as such on initial recognition and derivative financial instruments.

All financial assets held for investment purposes other than derivative financial instruments are designated as at fair value through income on initial recognition since they are managed, and their performance is evaluated, on a fair value basis in accordance with documented investment and risk management strategies. This designation is also applied to the Group's investment contracts, since the investment contract liabilities are managed together with the investment assets on a fair value basis as part of the documented risk management strategy.

Purchases and sales of 'regular way' financial assets are recognised on the trade date, which is when the Group commits to purchase, or sell, the assets.

All financial assets are initially measured at fair value plus, in the case of financial assets not classified as fair value through income, transaction costs that are directly attributable to their acquisition.

Subsequent to initial recognition, financial assets classified as fair value through income are measured at their fair value without any deduction for transaction costs that may be incurred on their disposal.

The fair values of financial assets quoted in an active market are their bid prices at the balance sheet date.
Financial assets classified as loans and receivables are stated at amortised cost less impairment losses. A provision for the impairment of loans and receivables is established when there is objective evidence that the Group will not be able to collect all the amounts due according to the original contract terms after the date of the initial recognition of the asset and when the impact on the estimated cash flows of the financial asset can be reliably measured.

Financial assets classified as prepayments are held at cost and are amortised over the relevant time period.

Financial assets not recognised at fair value through income are regularly reviewed for objective evidence of impairment. In determining whether objective evidence exists, the Group considers, among other factors, the financial stability of the counterparty, current market conditions and fair value volatility.

Financial assets are derecognised when contractual rights to receive cash flows from the financial assets expire, or where the financial assets have been transferred together with substantially all the risks and rewards of ownership.

(u) Derivative financial instruments

Derivative financial instruments are recognised at fair value. The gain or loss on re-measurement to fair value is recognised immediately in profit or loss. Hedge accounting has not been applied.

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties. The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

Embedded derivatives which are not closely related to their host contracts and which meet the definition of a derivative are separated and fair valued through income.

(v) Policyholders' funds held by the Group and liabilities relating to policyholders' funds held by the Group

Policyholders' funds held by the Group and liabilities relating to policyholders' funds held by the Group are recognised at fair value.

(i) Policyholders' funds held by the Group

The policyholders' funds held by the Group represent the assets associated with an Investment product in the Swedish business, where the assets are held on behalf of the policyholder and where all the risks and rewards associated with the assets are the policyholders' not the Group's.

The policyholders' funds held by the Group are held for investment purposes on behalf of the policyholders and are designated as at fair value through income. The fair values of the policyholders' funds held by the Group are the accumulation of the bid prices of the underlying assets at the balance sheet date. Transactions in these financial assets are recognised on the trade date, which is when the Group commits (on behalf of the policyholder) to purchase, or sell the assets.

(ii) Liabilities relating to policyholders' funds held by the Group

The liability relating to policyholders' funds held by the Group represents the liability that matches the asset policyholders' funds held by the Group. As stated previously, the risk and rewards associated with the investment product (and its underlying assets and matching liability) lie with the policyholders, not the Group.

(w) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks and other short-term highly liquid investments. Highly liquid is defined as having a short maturity of three months or less at their acquisition.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(x) Assets held for sale and liabilities held for sale

Assets and liabilities are classified as held for sale if their carrying amount is to be recovered principally through a sale transaction that is highly likely to complete within one year from the date of classification, rather than through continuing use. Such assets are measured at the lower of carrying amount and fair value and are classified separately from other assets in the balance sheet. Assets and liabilities are not netted. In the period where a non-current asset or disposal group is recognised for the first time, the balance sheet for the comparative prior period is not restated.

(y) Impairment

The carrying amounts of the Group's assets other than reinsurance assets (refer to (j) above) and assets which are carried at fair value are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets' recoverable amount is estimated in order to determine the extent of the impairment loss, if any. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount and impairment losses are recognised in the Consolidated Statement of Comprehensive Income. The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money.

Impairment losses are reversed through the Consolidated Statement of Comprehensive Income if there is a change in the estimates used to determine the recoverable amount. Such losses are reversed only to the extent that the assets' carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation where applicable, if no impairment loss had been recognised.

(z) Provisions

Provisions are recognised when the Group has a present, legal or constructive obligation as a result of past events such that it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Where the effect of the time value of money is material, the amount of the provision is the present value of the expenditure expected to be required to settle the obligation. The Group recognises provisions for onerous contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

(aa) Borrowings

Borrowings are recognised initially at fair value, less transaction costs, and are subsequently measured at amortised cost using the effective interest rate method, with interest expense recognised in the Consolidated Statement of Comprehensive Income on an effective yield basis. The effective interest rate method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts future cash payments through the expected life of the financial liability.

(bb) Employee benefits

(i) Pension obligations

UK businesses

Group companies operate defined contribution pension schemes, which are funded through payments to insurance companies, to which Group companies pay fixed contributions. There are no legal or constructive obligations on Group companies to pay further contributions if the fund does not hold sufficient assets to pay employee benefits relating to service in current and prior periods. Accordingly, Group companies have no further payment obligations once the contributions have been paid. Contributions to defined contribution pension schemes are recognised in the Consolidated Statement of Comprehensive Income when due.

Swedish business

The Group participates in a combined defined benefit and defined contribution scheme for the benefit of its employees. However, the scheme is a multi-employer scheme, with the associated assets and liabilities maintained on a pooled basis. There is limited information available to the Group to allow it to account for the scheme as a defined benefit scheme and, in accordance with IAS19 Employee Benefits, it is, therefore, accounted for as a defined contribution scheme. Contributions paid to the scheme are recognised in the Consolidated Statement of Comprehensive Income when due.

(ii) Bonus plans

The Group recognises a liability and an expense for bonuses based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The expense is recognised in the Consolidated Statement of Comprehensive Income on an accruals basis.

(cc) Share capital and shares held in treasury

(i) Share capital

Shares are classified as equity when there is no obligation to transfer cash or other assets. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax. Incremental costs directly attributable to the issue of equity instruments, as consideration for the acquisition of a business, are included in the cost of acquisition.

(ii) Shares held in treasury

Where the Company purchases its own equity share capital, the consideration paid, including directly attributable costs, is deducted from total shareholders' equity and shown separately as `treasury shares' until they are cancelled. Where such shares are subsequently sold, any consideration received is credited to the share premium account.

(dd) Dividends

Dividend distributions to the Company's shareholders are recognised in the period in which the dividends are paid, and, for the final dividend, when approved by the Company's shareholders at the Annual General Meeting.

(ee) Other payables and payables related to direct insurance and investment contracts

Insurance and investment contract payables and other payables are recognised when due and are measured on initial recognition at the fair value of the consideration paid. Subsequent to initial recognition, payables are measured at amortised cost using the effective interest rate method.

3 Critical accounting judgements and key sources of estimation and uncertainty

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities and also makes critical accounting judgements in applying the Group's accounting policies. Such estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable. The more critical areas, where accounting estimates and judgements are made, are set out below. Each item identifies the business segments, as described in Note 9, to which it is relevant.

(a) Classification of long-term contracts (CA, S&P, PL and Movestic)

The Group has exercised judgement in its classification of long-term business between insurance and investment contracts, which fall to be accounted for differently in accordance with the policies set out in Note 2 Significant Accounting Policies. Insurance contracts are those where significant risk is transferred to the Group under the contract and judgement is applied in assessing whether the risk so transferred is significant, especially with regard to pensions contracts, which are predominantly, but not exclusively, created for investment purposes.

(b) Acquired value of in-force business (CA, S&P, PL and Movestic)

The Group applies accounting estimates and judgements in determining the fair value, amortisation and recoverability of acquired in-force business relating to insurance and investment contracts. In the initial determination of the acquired value of in-force business, the Group uses actuarial models to determine the expected net cash flows (on a discounted basis) of the policies acquired. The key assumptions applied in the models are driven by the expected behaviour of policyholders on termination rates, expenses of management and age of individual contract holders as well as global estimates of investment growth, based on recent experience at the date of acquisition. The assumptions applied within the models are considered against historical experience of each of the relevant factors.

The acquired value of in-force business has been amortised on a basis that reflects the expected profit stream arising from the business acquired at the date of acquisition. Acquired value of in-force business is tested for recoverability by reference to expected future income and expense levels. Such impairment testing requires a degree of estimation and judgement. In particular the value is sensitive to the rate at which future cashflows are discounted and to the rates of return on invested assets. Analysis shows that no impairment adjustments are required for a realistic range of discount rates ranging from those used in the EEV models to a higher and more onerous estimate based on the Weighted Average Cost of Capital (WACC) for Chesnara. The rates used for the purpose of the impairment testing were 6%, 8%, 10% and 12%.

As at 31 December 2013, the carrying value of acquired in-force business, net of amortisation, was £12.0m in respect of CA (as at 31 December 2012: £14.6m), £6.5m in respect of S&P (as at 31 December 2012: £7.2m), £20.0m in respect of PL and £49.9m in respect of Movestic (as at 31 December 2012: £54.3m).

(c) Deferred acquisition costs and deferred income – investment contracts (CA and Movestic)

The Group applies judgement in deciding the amount of direct costs that are incurred in acquiring the rights to provide investment management services in connection with the issue of investment contracts. Judgement is also applied in establishing the amortisation of the assets representing these contractual rights and the recognition of initial fees received in respect of these contracts. The assets are amortised over the expected lifetime of the investment management service contracts and deferred income, where applicable, is amortised over the expected period over which it is earned. Estimates are applied in determining the lifetime of the investment management service contracts and in determining the recoverability of the contractual rights assets by reference to expected future income and expense levels. This test for recoverability is performed using best estimates of future cash flows, using a market consistent estimate of future investment returns.

As at 31 December 2013, the carrying values of deferred acquisition costs, net of amortisation, and of deferred income, in respect of CA, were £4.4m and £7.9m respectively (as at 31 December 2012: £5.1m and £8.9m respectively). The impact on the above numbers of a one year movement in the estimated lifetime of the management services contract or amortisation period is not material.

As at 31 December 2013, the carrying values of deferred acquisition costs, net of amortisation, in respect of Movestic, was £23.8m (as at 31 December 2012: £17.5m). An increase in the length of the amortisation period by one year would have increased profit before tax for the year ended 31 December 2013 by £0.6m and shareholders' equity as at 31 December 2013 by £0.4m.

(d) Fair value of financial assets and unit-linked investments (CA, S&P, and Movestic)

Fair value measurement has been adopted to reduce volatility in reported earnings in the Consolidated Statement of Comprehensive Income as the liabilities so determined are measured in a way which is consistent with the fair value of the underlying invested financial assets.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between willing, knowledgeable parties in an arm's length transaction. Fair values are determined by reference to observable market prices where available and reliable.

(e) Estimates of future benefits payments arising from long-term insurance contracts (CA, S&P and PL)

The Group makes estimates of the expected number of deaths for each of the years that it is exposed to risk. These estimates are based on either standard mortality tables or reinsurers' rate tables as appropriate, adjusted to reflect the Group's own experience. For contracts without fixed terms the Group has assumed that it will be able to increase charges to policyholders in future years, in line with emerging mortality experience.

The Group has offered guaranteed annuity options within certain contracts. Estimates have been made of the number of contract holders who will exercise these options, in order to measure their value. Changes in investment conditions could result in significantly more contract holders exercising their options than the Group has assumed in determining the liabilities arising from these contracts.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

3 Critical accounting judgements and key sources of estimation and uncertainty (continued)

(e) Estimates of future benefits payments arising from long-term insurance contracts (CA, S&P and PL) (continued)

The Group makes estimates of future deaths, voluntary contract terminations, investment returns and administration expenses at the inception of long-term insurance contracts with fixed and guaranteed terms. These estimates, which are reconsidered annually, form the assumptions used to calculate the liabilities arising from these contracts.

When assessing assumptions relating to future investment returns the Group makes estimates of the impact of defaults on the related financial assets. The estimates are reassessed annually. The assumptions used to establish insurance contract liabilities and appropriate sensitivities relating to variations in critical assumptions are disclosed in Note 33.

(f) Estimates of future maintenance expenses (CA)

Future expense levels are a key variable that influence the value of insurance contract provisions. Under normal circumstances the nature of the cost base underpinning our UK regulated entities means that future expenses are relatively predictable and hence assumptions made for actuarial reserving purposes not are subject to material levels of judgement. This is because asset management and policy administration in the UK are outsourced and hence the future costs are defined in contractual arrangements. In addition, governance overheads are by their nature relatively stable and predictable. The outsource contract for the CA book expires in 2015 and hence is currently under negotiation. This creates a short-term level of uncertainty and hence a level of judgement has been applied to reflect Management's best estimate of the outcome from the negotiations, and the most likely impact on future expense levels. Management has assessed that any revised terms are likely to be more expensive than the existing contract and as such expense levels are assumed to increase.

(g) Contracts which contain discretionary participation features (S&P)

All S&P with-profits contracts contain a discretionary participation feature ('DPF') which entitles the holder to receive, as a supplement to guaranteed benefits, additional benefits or bonuses:

- that may be a significant portion of the total contractual benefits;
- whose amount or timing is contractually at the discretion of the Group; and
- that are contractually based on realised and/or unrealised investment returns on a specified pool of assets held by the Group.

The terms and conditions of these contracts, together with UK regulations, set out the bases for the determination of the amounts on which the additional discretionary benefits are based and within which the Group may exercise its discretion as to the quantum and timing of their payment to contract holders.

As at 31 December 2013, the carrying value of insurance contract liabilities which contain S&P discretionary participation features was £310.5m (31 December 2012: £346.7m).

As stated in Note 33 'Insurance contract provisions', the cost to shareholders of guarantees in respect of S&P contracts with discretionary participation features is estimated, based on a constant margin of 10% above a market-consistent evaluation of such costs. An increase in the margin to 20% would reduce profit before tax for the year ended 31 December 2013, by £2.1m and shareholder equity as at 31 December 2013 by £1.7m.

(h) Insurance claim reserves (Movestic)

Provisions are determined by Management based on experience of claims settled and on statistical models which require certain assumptions to be made regarding the timing, incidence and amount of claims. In order to calculate the total provision required, the historical development of claims is analysed using statistical methodology to extrapolate, within acceptable parameters, the value of outstanding claims.

For more recent underwriting years the provisions will make more use of techniques that incorporate expected loss ratios. As underwriting years mature, the reserves are increasingly driven by methods based on actual claims experience. The data used for statistical modelling is internally generated. Actual claims experience may differ from the historical pattern on which the estimate is based and the cost of individual claims may exceed that assumed.

Liabilities carried in respect of waiver of premium and income protection policies are sensitive to the Group's assessment of the length of period in which benefits will be paid to policyholders (which can be significant). Estimates are made based on the sex, age and occupation of the claimant as well as the length of time the claimant has been claiming on the policy.

As at 31 December 2013, the carrying value of the insurance claim reserves, gross of reinsurance, was £66.1m (as at 31 December 2012: £68.6m). The key sensitivities in respect of insurance claim reserves are considered in Note 33.

(i) Insurance claim reserves – reinsurance recoverable (Movestic)

A significant proportion of the insurance claims arising within Movestic are ceded to reinsurers. In preparing the financial statements the Directors have made an assessment as to whether claims ceded to reinsurers are recoverable. As at 31 December 2013, such claims ceded to reinsurers and reflected on the balance sheet were £44.4m (31 December 2012: £46.2m). The application of a 10 per cent bad debt provision on the reinsurance balance would reduce 2013 profit before tax by £4.4m and shareholders' equity by £3.3m.

(j) Accounting for pension plans (Movestic)

The Group participates in a defined benefit pension scheme on behalf of its Swedish employees. The scheme is a multi-employer plan to which a number of third party employers also contribute. The underlying assets and liabilities of the scheme are pooled and are not allocated between the contributing employers. As a result, information is not available to account for the scheme as a defined benefit scheme and the Group has accounted for the scheme as a defined contribution scheme.

4 Exchange rates

The Group's principal overseas operations during the year were located within Sweden.

The results and cash flows of these operations have been translated into Sterling at an average rate for the year of £1 = SEK 10.1901 (2012: £1 = SEK 10.7326).

Assets and liabilities have been translated at the year end rate of £1 = SEK 10.5919 (31 December 2012: £1 = SEK .10.5247).

Total foreign currency exchange rate movements for the year ended 31 December 2013 resulted in a loss recognised in the Consolidated Statement of Comprehensive Income of £516,000 (year ended 31 December 2012: £741,000 gain).

5 Management of insurance risk

The Group's management of insurance risk is a critical aspect of its business. The primary insurance activity carried out by the Group comprises the assumption of the risk of loss from persons that are directly subject to the risk. Such risks in general relate to life, accident, health and financial perils that may arise from an insurable event. As such, the Group is exposed to the uncertainty surrounding the timing and severity of claims under the related contracts. The principal risk is that the frequency and severity of claims is adverse to that expected. The theory of probability is applied to the pricing and provisioning for a portfolio of insurance contracts. Insured events are, by their nature, random, and the actual number and size of events during any one year may vary from those estimated using established statistical techniques. The risk under assurance policies is partly naturally hedged by risks under annuity policies where the exposure is to the risk of longevity.

The Group manages its insurance risk through adoption of underwriting strategies, the aim of which is to avoid the assumption of undue concentration of risk, approval procedures for new products, pricing guidelines and adoption of reinsurance strategies, the aim of which is to reinforce the underwriting strategy by avoiding the retention of undue concentration of risk on any one life.

Notwithstanding that the Group pursues common overarching objectives and employs similar techniques in managing these risks, the disparate characteristics of the products and of the market and regulatory environments of the UK and Swedish businesses are such that insurance risk is managed separately for the separate businesses. Accordingly, the information which follows differentiates these businesses. The UK businesses, which are substantially closed to new business, comprise the CA, S&P and PL segments and these are further differentiated in the information provided below, where necessary. The Swedish business, which is open to new business, comprises the Movestic segment.

UK businesses

Terms and conditions of insurance contracts

The terms and conditions of insurance contracts that have a material effect on the amount, timing and uncertainty of future cash flows arising from insurance contracts are set out in the product analyses below, which give an assessment of the main products of the UK businesses and of the ways in which the associated risks are managed.

Sums assured/benefits per annum – gross and net of reinsurance
31 December

	2013		2012	
	Gross £000	Net £000	Gross £000	Net £000
Long-term unit-linked without DPF (sums assured) – CA, S&P	3,431,526	2,649,724	3,847,002	2,942,430
Long-term non-linked without DPF (sums assured) – CA, S&P, PL	13,942,405	1,863,653	133,566	119,713
Immediate annuities (benefits per annum) – CA	5,890	5,817	6,224	6,120
Deferred annuities with DPF (benefits per annum) – S&P	2,375	2,375	2,599	2,599
Long-term with DPF (sums assured) – CA	52,589	120	56,441	120
Long-term with DPF (sums assured) – S&P	411,718	394,269	434,750	416,760

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5 Management of insurance risk (continued)

UK businesses (continued)

Long-term unit-linked and non-linked insurance contracts – without discretionary participation features

Product features

The UK businesses have written both unit-linked and non-linked contracts, which include death and morbidity benefits on a whole life, endowment and term assurance basis. In addition there are immediate annuities primarily written from vesting pensions.

For contracts where death is the insured risk, the most significant factors that could increase risk are epidemics (such as AIDS, SARS or a flu pandemic) or widespread changes in lifestyle, such as eating, smoking and exercise habits, resulting in earlier or more claims than expected.

Management of risks

Unit-linked insurance contracts are contracts where charges are made for insurance risk and administration charges and the primary purpose of which is to provide an investment return to policyholders. In addition, the policyholder is insured against death and serious injury. Unit-linked contracts operate by investing the policyholders' premiums into pooled investment funds of the UK businesses, the policyholders' share of the fund being represented by units. The benefit is payable on death, or maturity if earlier, the amount payable on death being subject to a guaranteed minimum amount. For these contracts, all of the investment risk is borne by the policyholder as investment performance directly affects the value of the unit fund and hence the benefits payable. Therefore, there is exposure to insurance risk only insofar as the value of the unit-linked fund is lower than the guaranteed minimum death benefit. For a material portion of the business, the charges taken for mortality and morbidity costs are reviewable, which allows the company to mitigate some of its insurance risk.

Non-linked business contains three distinct groups of products:

(i) A number of products representing approximately 78% of sums assured, provide fixed and guaranteed benefits and have fixed future premiums. For these there are no mitigating terms and conditions that reduce the insurance risk accepted.

(ii) Immediate annuities provide regular income payments generally during the outstanding life of the policyholder, and in some cases that of a surviving spouse or partner. In certain cases payments may be guaranteed for a minimum period. These expose the business to longevity risk, though to some extent this provides a hedge to the mortality risk taken on other products; and

(iii) For the remainder of the business, which is operated on a quasi-linked basis, charges are made for mortality risk on a monthly basis and these charges may be altered based on mortality experience, thereby minimising the exposure to mortality risk. In the light of charges made for insurance risk and administration services and of the investment performance of the assets notionally backing these contracts, the premium payable may be altered at regular intervals. A number of these contracts also include Permanent Health Insurance (PHI) benefits which have reviewable charges, which may be altered based on morbidity experience, thereby minimising the exposure to morbidity risk. Delays in implementing increases in charges and market or regulatory restraints over the extent of the increases may reduce this mitigating effect.

Reinsurance is used extensively on the business described above to mitigate concentrations of insurance risk. The insurance risk is further managed through pricing, product design and, for non-linked and quasi-linked contracts, appropriate investment strategy.

Concentration of insurance risk

Through the use of reinsurance exposures to material insurance risks on individual cases are avoided, with 97.0% of the business having retained sums assured of less than £250,000.

Long-term insurance contracts – with discretionary participation features – CA

Product features

CA historically wrote with-profits business in the UK, where the policyholder benefits comprise a guaranteed sum assured payable on death or at maturity, to which may be added a discretionary annual bonus and a discretionary terminal bonus.

Management of risks

This business is wholly reassured to Guardian and hence the only risk retained by CA for this business is the risk of default by the reinsurer. This risk is detailed in the Credit Risk Management section of Note 6.

UK businesses (continued)
Long-term insurance contracts – with discretionary participation features – S&P

Product features
At retirement the with-profits deferred annuity contracts provide for guaranteed minimum pensions and the with-profits endowments provide for guaranteed minimum lump sums. With-profits whole of life policies guarantee a minimum amount payable on death. The guaranteed annuities or lump sums represent investment returns on contributions mainly at 5% p.a. A terminal bonus may be paid at maturity or retirement, and on death, depending on the investment performance of the with-profits policyholder assets when the policyholder receives the higher of the asset share and the minimum guaranteed amount. The asset share is based on the contributions invested plus an allocation of investment return less costs and expenses. In accordance with the Principles and Practices of Financial Management for its with-profits business S&P may make a deduction of up to 1.5% per annum from the asset shares of with-profits policyholders to meet the future cost of guarantees. The amount deducted remains part of the assets in the with-profits policyholder funds. The size of the deduction is reassessed at least annually. In the event of a policyholder choosing to transfer out, the amount payable is not guaranteed and is based on the asset share.

Management of risks
For life endowment and whole of life policies mortality risk is material. This risk is mitigated to some extent by the use of reinsurance. The risk is to increases in mortality rates, which are most likely to be from epidemics (such as AIDS, SARS or a flu pandemic) or widespread changes in lifestyle, such as eating, smoking and exercise habits, resulting in earlier or more claims than expected.

For deferred annuity contracts, the risk is to improving mortality. The risk is managed through the initial pricing, and technical provisions are assessed allowing for future mortality improvements based on industry available information on mortality experience.

Concentration of insurance risk
Through the use of reinsurance exposures to material insurance risks on individual cases are avoided, with 99.0% of the business having retained sums of less than £250,000.

Other risks on insurance contracts
Apart from financial risks relating to the financial assets, which support life assurance contracts, as set out in Note 6, there are other significant types of risk pertaining to life insurance contracts written by the UK businesses, as follows:

Expense risk
The strategy of the UK businesses is to outsource all operational activities to third party administrators in order to reduce the significant expense inefficiencies that would arise with fixed and semi-fixed costs on a diminishing policy base. There are, however, risks associated with the use of outsourcing. In particular, there will be a need in future to renegotiate the terms of the outsourcing arrangements as the existing agreements expire. There is also a risk that, at some point in the future, third party administrators could default on their obligations. The UK businesses monitor the financial soundness of third party administrators and have retained step-in rights on the more significant of these agreements. There are also contractual arrangements in place which provide for financial penalties in the event of default by the administration service provider.

Mortgage endowment misselling complaints
The UK businesses have experienced a significant level of complaints from mortgage endowment policyholders since their first regulatory mailing programme in 2000. In response to this, the UK businesses hold mortgage endowment complaints redress provisions. The UK businesses continue to monitor closely, among other factors, the volume of complaints and the value of compensation paid to policyholders in order to assess the continuing adequacy of the provisions.

There remains however a residual risk that at some point in future the levels of complaints received may prove to be higher than those anticipated within the provision.

Persistency risk
Persistency risk is the risk that the investor cancels the contract or discontinues paying new premiums into the contract, thereby exposing the UK businesses to a loss resulting from an adverse movement in the actual experience compared to that expected in the product pricing. Although changes in the levels of persistency would not adversely affect the result in the short-term they would reduce future profits available from the contract.

Assumptions and sensitivities
The assumptions and sensitivities relating to insurance contract provisions for the UK businesses are set out in Note 33 Insurance Contract Provisions.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5 Management of insurance risk (continued)

Swedish business

The terms and conditions of insurance contracts which have a material effect on the amount, timing and uncertainty of future cash flows arising from insurance contracts are set out in the product analyses below, which give an assessment of the main products of Movestic and of the ways in which the associated risks are managed. The breakdown of the insurance products of Movestic, by gross and net premiums written and by claims outstanding, which reflects the scale of business written, is as follows:

Premiums
Year ended 31 December

	Before reinsurance		After reinsurance	
	2013 £000	2012 £000	2013 £000	2012 £000
Group				
Sweden	22,351	20,369	8,742	7,704
Norway	634	2,378	105	282
Individual				
Death	3,587	3,127	1,705	1,512
Waiver of premium	3,140	3,096	797	906
Income protection	9,566	10,266	5,437	6,009
	39,278	**39,236**	**16,786**	**16,413**

Claims outstanding
As at 31 December

	Before reinsurance		After reinsurance	
	2013 £000	2012 £000	2013 £000	2012 £000
Group				
Sweden	22,020	24,214	4,372	5,445
Norway	4,455	4,474	720	679
Individual				
Death	950	1,604	359	678
Waiver of premium	6,396	6,007	1,694	1,739
Income protection	29,235	32,282	11,485	13,869
	63,056	**68,581**	**18,630**	**22,410**

Swedish business (continued)
Terms and conditions
Product features – Group Contracts
Group Contracts insure policyholders in respect of death with the option to include additional accident and disability benefits. Policyholders may also include their spouse and children (up to the age of 25) on the policy.

Policies are sold in both Sweden and Norway and all sales are intermediated. Group Contracts sold in Sweden allow the policyholder to choose the sum assured level. Contracts sold in Norway have sum assured levels that are normally determined by the policyholders' employer and apply to all members of that company scheme.

The Swedish product provides a maximum coverage of insured benefits up to 40 times a base amount (as at 31 December 2013 SEK 44,500 being approximately £4,201) although most policies are between 6 to 15 times the base amount.

The Norwegian product provides a maximum coverage of insured benefits up to 80 times a base amount (as at 31 December 2013 NOK 85,245, being approximately £8,490) although most policies are between 5 to 10 times the base amount.

All contracts are for an annual period and premium payments are made usually on either an annual or quarterly basis.

Product features – Individual Contracts
In relation to Individual Contracts, Movestic writes contracts, which include death and morbidity benefits on term assurance with disability, waiver of premium and income protection options. Policies are sold in Sweden and all sales are intermediated.

In relation to the income protection and the waiver of premium benefits within the Individual Contracts, the monthly benefits upon a claim may be payable to the policyholders over a long period up to their retirement.

The contracts have been unbundled as between insurance and investment contracts. Risk in respect of investment contracts is described in Note 6. All insurance contracts are for an annual period and payments are made on a monthly basis.

Management of risk
The main risk associated with the Group and Individual Contracts is the frequency of claims (for either death or accident or sickness). Claims experience can be variable, with the main factors being the age, sex and occupation of the policyholder.

In addition, for the Group Contracts, Movestic is exposed to a single loss event that covers a number of employees of an organisation.

The key risks are managed through appropriate product design and pricing of the policies to ensure that the potential cost to Movestic of these events (and associated expenses of underwriting and administration) are reflected in the price charged to the policyholder. Key controls implemented include a defined pricing structure based on the characteristics of the policyholder and the regular review of management information on the type and frequency of accidents.

Group Contracts are issued on an annual basis which means that Movestic's exposure runs for a period of 12 months, after which Movestic has the option to decline to renew or can increase the price on renewal.

Individual Contracts are long-term contracts but Movestic has the option to review the premiums on an annual basis.

For both the Group and Individual Contracts, between 30% to 90% of the premiums and claims relating to this product are ceded to a reinsurer which reduces the overall insurance risk exposure to Movestic. The policies and products from the Aspis acquisition are reinsured for approximately 80% of the claims amount.

In addition, for the majority of the Group Contracts, the loss arising from a single event to multiple employees is reinsured. The reinsurance provides indemnity for a single loss between SEK 5m (approximately £0.5m) and SEK 140m (approximately £13.2m).

Concentration of insurance risk
Concentration of insurance risk is determined by reference to benefits assured for Individual Contracts and by estimated maximum loss for Group Contracts.

Regarding benefits assured for individual contracts, the combined effect of reinsurance and the fact that the vast majority of the total benefit assured relates to numerous small value contracts, limit the level of concentration risk.

Through the use of reinsurance exposures to material insurance risks on individual cases are avoided, with 99.8% of the business having retained sums assured of less than £250,000.

In respect of Group Contracts, the business is exposed to multiple employees of the same organisation being involved in a single loss event. Movestic estimates that its largest such exposures arise in Norway, where the Group Contracts sold tend to cover all employees within that organisation (whereas in Sweden employees may opt in to the Group Contract). Movestic forecasts that its maximum loss would be approximately SEK 44m (approximately £4.2m) gross of reinsurance and SEK 143m (approximately £13.5m) after reinsurance.

Assumptions and sensitivities for Group Contract and Individual Contract insurance contract provisions
Information relating to insurance contract provisions assumptions and sensitivities for the Swedish business is set out in Note 33 Insurance Contract Provisions.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk

The Group is exposed to a range of financial risks, principally through its insurance contracts, financial assets, including assets representing shareholder assets, financial liabilities, including investment contracts and borrowings, and its reinsurance assets. In particular, the key financial risk is that, in the long-term, proceeds from financial assets are not sufficient to fund the obligations arising from its insurance and investment contracts and borrowings. The most important components of this financial risk are market risk (interest rate risk, equity and property price risk, foreign currency exchange risk and liquidity risk), and credit risk, including the risk of reinsurer default. Further, the Group has significant foreign currency exchange rate risk in relation to movements between the Swedish Krona and Sterling arising from its ownership of Movestic.

The terms and conditions of insurance contracts that have a material effect on the amount, timing and uncertainty of future cash flows arising from insurance contracts are set out in Note 5. The terms and conditions of investment contracts that have a material effect on the amount, timing and uncertainty of future cash flows arising from investment contracts are as follows:

The Group provides three types of investment contract: unit-linked savings, unit-linked pensions predominantly written in the UK and Sweden and guaranteed income and growth bonds predominantly written in the UK.

(i) Unit-linked savings are single or regular premium contracts, with the premiums invested in a pooled investment fund, where the policyholder's investment is represented by units or trust accounts where the policyholder decides where to invest. On certain contracts there is a small additional benefit payable on death which is deemed not to transfer significant insurance risk to the business for these contracts. The benefits payable at maturity or surrender of the contracts are the underlying value of the investment in the unit-linked funds or trust accounts, less surrender penalties where applicable.

(ii) Unit-linked pensions are single or regular premium contracts with features similar to unit-linked savings contracts. Benefits are payable on transfer, retirement or death.

(iii) Guaranteed income bonds are mainly single premium contracts for a fixed term offering fixed-income payments plus a return of capital at maturity. A guaranteed growth bond offers no income, but a higher guaranteed payment at maturity date.

Market risk management

(i) General

The Group businesses manage their market risks within asset liability matching (ALM) frameworks that have been developed to achieve long-term investment returns at least equal to their obligations under insurance and investment contracts, with minimal risk. Within the ALM frameworks the businesses periodically produce reports at legal entity and asset and liability class level, which are circulated to the businesses' key management. The principal technique of the ALM frameworks is to match assets to the liabilities arising from insurance and investment contracts by reference to the type of benefits payable to policyholders, with separate portfolios of assets being maintained for each distinct class of liability.

For unit-linked contracts the Group's objective is to match the liabilities, both insurance and investment contract liabilities, with units in the assets of the funds to which the value of the liabilities is linked, such that the policyholder bears the market risk. This minimises the impact of market risks on these contracts, such that the remaining primary exposure to market risk is the risk of volatility in asset-related fees due to the impact of interest rate, equity price and foreign currency movements on the fair value of the unit-linked assets, on which asset-related fees are based.

For non unit-linked business, the Group's objective is to match the timing of cash flows from insurance and investment contract liabilities with the timing of cash flows from assets subject to identical or similar risks. By matching the cash flows of liabilities with those of suitable assets, market risk is managed effectively, whilst liquidity risk is minimised. These processes to manage the risks, which the Group has not changed from previous periods, ensure that the Group is able to meet its obligations under its contractual liabilities as they fall due.

With respect to S&P there is significant additional risk insofar as investment returns on policyholder with-profits assets supporting the with-profits business may result in insufficient policyholder assets to meet contractual obligations to with-profits policyholders, because of the impact of contract guarantees, as explained further on the next page.

The notes below explain how market risks are managed using the categories utilised in the businesses' ALM (Asset Liability Matching) frameworks. In particular, the ALM frameworks require the management of interest risk, equity price risk, and liquidity risk at the portfolio level, so that the appropriate risks for each portfolio may be managed in an effective way. The following tables reconcile the classes and portfolios used in the businesses' ALM frameworks to relevant items in the consolidated balance sheet and are followed by a portfolio-by-portfolio description of the nature of the related market risk and how that risk is managed.

31 December 2013

	Unit-linked contracts £000	Insurance* contracts with DPF £000	Annuities in payment £000	Guaranteed bonds £000	Other non-linked contracts and other shareholder funds £000	Total £000
Assets						
Property and equipment	–	–	–	–	673	673
Investment in associates	–	–	–	–	4,088	4,088
Investment properties	13,692	6,215	–	–	480	20,387
Reinsurers' share of insurance contract provisions	135,324	108,458	–	–	136,112	379,894
Amounts deposited with reinsurers	34,293	–	–	–	–	34,293
Financial assets						
Equity securities at fair value through income	479,615	2	–	–	–	479,617
Holdings in collective investment schemes at fair value through income	3,063,716	308,869	–	–	68,407	3,440,992
Debt securities at fair value through income	154,576	55,214	100,790	836	59,250	370,666
Insurance and other receivables	15,268	819	–	33	30,262	46,382
Prepayments	301	225	–	–	4,363	4,889
Derivative financial instruments	548	318	–	–	2,090	2,956
Total financial assets	3,714,024	365,447	100,790	869	164,372	4,345,502
Reinsurers' share of accrued policyholder claims	6,459	119	–	–	4,821	11,399
Income taxes	–	–	–	–	2,608	2,608
Cash and cash equivalents	73,274	2,206	1,044	544	107,195	184,263
Total assets	**3,977,066**	**482,445**	**101,834**	**1,413**	**420,349**	**4,983,107**
Liabilities						
Insurance contract provisions	1,619,473	423,611	100,865	–	218,114	2,362,063
Other provisions	3	–	–	–	5,345	5,348
Financial liabilities						
Investment contracts at fair value through income	2,276,135	–	–	866	6,402	2,283,403
Borrowings	–	–	–	–	94,377	94,377
Derivative financial instruments	387	–	–	–	–	387
Total financial liabilities	2,276,522	–	–	866	100,779	2,378,167
Deferred tax liabilities	–	–	–	–	11,007	11,007
Reinsurance payables	1,412	10	–	–	10,117	11,539
Payables related to direct insurance and investment contracts	14,925	4,849	567	61	26,735	47,137
Income taxes	–	–	–	–	8,012	8,012
Other payables	4,637	637	–	–	21,830	27,104
Bank overdrafts	61	4	–	–	1,062	1,127
Total liabilities	**3,917,033**	**429,111**	**101,432**	**927**	**403,001**	**4,851,504**

*Insurance contract with DPF include shareholder funds within the S&P with-profits funds.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

31 December 2012

	Unit-linked contracts £000	Insurance* contracts with DPF £000	Annuities in payment £000	Guaranteed bonds £000	Other non-linked contracts and other shareholder funds £000	Total £000
Assets						
Property and equipment	–	–	–	–	369	369
Investment in associates	–	–	–	–	2,902	2,902
Investment properties	77,338	22,349	–	–	480	100,167
Deferred tax assets	2,186	–	–	–	109	2,295
Reinsurers' share of insurance contract provisions	131,266	102,237	–	–	45,189	278,692
Amounts deposited with reinsurers	30,245	–	–	–	–	30,245
Financial assets						
Equity securities at fair value through income	427,294	2	–	–	7	427,303
Holdings in collective investment schemes at fair value through income	2,619,000	313,497	–	–	77,302	3,009,799
Debt securities at fair value through income	151,201	61,652	112,943	1,512	36,069	363,377
Insurance and other receivables	12,758	855	–	89	10,611	24,313
Prepayments	137	–	–	–	3,023	3,160
Derivative financial instruments	310	206	–	–	2,579	3,095
Total financial assets	3,210,700	376,212	112,943	1,601	129,591	3,831,047
Reinsurers' share of accrued policyholder claims	3,806	–	–	–	683	4,489
Income taxes	–	–	–	–	4,299	4,299
Cash and cash equivalents	99,253	4,039	164	337	124,883	228,676
Total assets	**3,554,794**	**504,837**	**113,107**	**1,938**	**308,505**	**4,483,181**
Liabilities						
Insurance contract provisions	1,506,770	453,421	113,107	–	133,780	2,207,078
Other provisions	4	–	–	–	5,157	5,161
Financial liabilities						
Investment contracts at fair value through income	2,012,983	–	–	1,790	7,541	2,022,314
Borrowings	–	–	–	–	48,324	48,324
Derivative financial instruments	278	8	–	–	–	286
Total financial liabilities	2,013,261	8	–	1,790	55,865	2,070.924
Deferred tax liabilities	–	–	–	–	5,894	5,894
Reinsurance payables	1,422	–	–	–	15,188	16,610
Payables related to direct insurance and investment contracts	23,405	4,204	–	148	11,137	38,894
Other payables	3,874	565	–	–	12,618	17,057
Bank overdrafts	10	–	–	–	592	602
Total liabilities	**3,548,746**	**458,198**	**113,107**	**1,938**	**240,231**	**4,362,220**

*Insurance contract with DPF include shareholder funds within the S&P with-profits funds.

Unit-linked contracts
For unit-linked contracts, which may be insurance or investment contracts, the Group matches the financial liabilities, with units in the financial assets of the funds to which the value of the liabilities is linked, such that the policyholders bear the principal market risk (being interest rate, equity price and foreign currency risks) and credit risk. Accordingly, this approach results in the Group having no significant direct market or credit risk on these contracts. Its primary exposure to market risk is the risk of volatility in asset-related fees due to the impact of interest rate, equity price and foreign exchange rate movements on the fair value of the assets held in the linked funds, on which asset-related fees are based.

There is residual exposure to market risk on certain unit-linked contracts where the Group provides to policyholders guarantees as to fund performance or additional benefits which are not dependent on fund performance. This exposure is mitigated to the extent that the Group matches the obligations with suitable financial assets external to the unit-linked funds, such that the residual exposure is not considered to be material.

Insurance contracts with discretionary participation features
Insurance contracts with discretionary participation features subsist entirely within the UK businesses in the form of with-profits policies.

For the CA business, where the policyholder benefits comprise a discretionary annual bonus and a discretionary terminal bonus, the with-profits business is wholly reinsured to Guardian and hence there is no market risk for this class of business. Policyholders have the option, for a small element of the with-profits business, to invest a portion of their investment in unit-linked funds as an alternative to the with-profits fund. In this case, a portion of the business is retained, with the management of financial risks of this portion being the same as described under 'Unit-linked Contracts' above.

For the S&P business the primary investment objective of the with-profits policyholder funds is that the guaranteed minimum benefits of the with-profits policyholders should be met entirely from the policyholder funds. The secondary investment objective is, where possible, to provide a surplus in excess of the guaranteed minimum benefits. The entire surplus in the policyholder fund accrues to the with-profits policyholders. Any deficit in the policyholder fund is ultimately borne by shareholders. Therefore the Group has a significant exposure to market risk in relation to with-profits business should the with-profits policyholder assets be unable to fully meet the cost of guarantees. To achieve the investment objectives, the funds may invest in a range of asset classes including property, equities, fixed interest securities, convertibles, cash and derivatives, both in UK and overseas investments. Such exposure may be achieved by investment in collective investment schemes (including such schemes with total or absolute return objectives or which include investments in commodities). Investment guidelines restrict the level of exposure for certain asset categories. In respect of derivatives, these may only be used for the purposes of reduction of investment risks and efficient portfolio management.

The PL segment does not include any products that contain discretionary participation features.

Annuities in payment
These are contracts which pay guaranteed financial benefits, generally monthly, for the lifetime of the policyholder, and in some cases of their spouse. The financial component of these contracts is a guaranteed fixed interest rate: accordingly the Group's primary financial risk on these contracts is the risk that interest income and capital redemptions from the fixed interest debt securities backing the liabilities are insufficient to fund the benefits payable. The Group manages the interest rate risk by matching closely new contracts written with fixed interest debt securities of a suitable duration and quality. Regular monitoring of the interest rate risk is carried out by analysis of expected cash flows from the financial assets held with those for the liabilities, which are determined by means of projecting expected cash flows from the contracts using prudent estimates of mortality.

Guaranteed bonds
These contracts are for a fixed term with financial benefits that are fixed and guaranteed at the inception of the contract. The Group manages its market risk on these products, by closely matching contracts written with fixed interest debt securities of a suitable duration and quality. Accordingly, the Group's primary financial risk is the risk that interest income and capital redemptions from the financial assets backing the liabilities are insufficient to fund the guaranteed benefits payable. Regular monitoring of the interest rate risk is carried out by analysis of expected cash flows from the financial assets held with those for the liabilities, which are determined assuming all contracts continue until their expected maturity date. This analysis also enables the Group to control its liquidity risk for this portfolio. The liabilities at 31 December 2013 associated with these products amounted to £866,000 (31 December 2012: £1,790,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

Other non-linked contracts and shareholder funds

These categories, in which market risk is borne by shareholders, consist of non-linked insurance contracts without DPF and of net shareholder assets representing shareholders' equity. The Group manages market risks by setting investment guidelines which restrict market exposures.

Non-linked contracts without DPF include contracts which pay guaranteed benefits on death or other insured events, the terms being fixed at the inception of the contract. Exposure to market price risk is minimised by generally investing in fixed-interest debt securities, while interest rate risk is generally managed by closely matching contracts written with financial assets of suitable yield and duration. To the extent that the Group is unable to fully match its interest rate risk, it makes provision in respect of assumed shortfalls on guaranteed returns to policyholders.

Shareholder funds at both Group parent company and operating subsidiary level, in accordance with corporate objectives and, in some instances, in accordance with local statutory solvency requirements, are invested in order to protect capital and to minimise market and credit risk. Accordingly they are generally invested in assets of a shorter-term liquid nature, which gives rise to the risk of lower returns on these investments due to changes in short-term interest rates.

(ii) Liquidity risk

Liquidity risk is the risk that adequate liquid funds are not available to settle liabilities as they fall due and is managed by forecasting cash requirements and by adjusting investment management strategies to meet those requirements. Liquidity risk is generally mitigated by holding sufficient investments which are readily marketable in sufficiently short timeframes to allow the settlement of liabilities as they fall due. Where liabilities are backed by less marketable assets, for example investment properties, there are provisions in contractual terms which allow deferral of redemptions in times of adverse market conditions. The Group's substantial holdings of money market assets also serves to reduce liquidity risk.

The tables below present a maturity analysis of the Group's liabilities, showing balance sheet carrying value and distinguishing between investment contracts and insurance contracts and other liabilities.

31 December 2013

		Contractual cash flows (undiscounted)					
Carrying values and cash flows arising from:	**Carrying value £000**	**0-5 years £000**	**5-10 years £000**	**10-15 years £000**	**15-20 years £000**	**>20 years £000**	**Total £000**
Insurance contract liabilities							
Unit-linked	1,619,473	1,619,473	–	–	–	–	1,619,473
With-DPF							
CA	113,140	113,140	–	–	–	–	113,140
S&P	310,471	100,228	81,984	92,718	74,544	37,127	386,601
Annuities in payment	100,865	27,639	24,366	20,802	16,996	27,023	116,826
Other non-linked	218,114	84,331	82,232	23,014	4,342	5,659	199,578
Investment contract liabilities							
Unit-linked	2,276,135	2,276,135	–	–	–	–	2,276,135
Guaranteed bonds	866	866	–	–	–	–	866
Other	6,402	6,402	–	–	–	–	6,402
Other liabilities	206,038	206,038	–	–	–	–	206,038
Total	**4,851,504**	**4,434,252**	**188,582**	**136,534**	**95,882**	**69,809**	**4,925,059**

Policies arising on the acquisition of Protection Life are all categorised as "Other non-linked" in the table above.

(ii) Liquidity risk (continued)

31 December 2012

Carrying values and cash flows arising from:	Carrying value £000	Contractual cash flows (undiscounted) 0-5 years £000	5-10 years £000	10-15 years £000	15-20 years £000	>20 years £000	Total £000
Insurance contract liabilities							
Unit-linked	1,506,770	1,506,770	–	–	–	–	1,506,770
With-PDF							
CA	106,715	106,715	–	–	–	–	106,715
S&P	346,706	104,576	75,335	88,223	71,820	40,650	380,604
Annuities in payment	113,107	26,883	24,031	20,837	17,353	28,818	117,922
Other non-linked	133,780	57,916	9,182	4,988	3,187	1,873	77,146
Investment contract liabilities							
Unit-linked	2,012,983	2,012,983	–	–	–	–	2,012,983
Guaranteed bonds	1,790	1,790	–	–	–	–	1,790
Other	7,541	7,541	–	–	–	–	7,541
Other liabilities	132,828	132,828	–	–	–	–	132,828
Total	**4,362,220**	**3,958,002**	**108,548**	**114,048**	**92,360**	**71,341**	**4,344,299**

The maturity analysis for unit-linked insurance and investment contracts presents all the liabilities as due in the earliest period in the table because they are repayable or transferable on demand.

Insurance contracts with DPF (with-profits business) can be surrendered before maturity for a cash amount specified in contractual terms and conditions. Accordingly, a maturity analysis based on the earliest contractual repayment date would present all the liabilities as due in the earliest period of the table because this option can be exercised immediately by all policyholders. As stated above, CA insurance contracts with DPF are wholly reinsured to Guardian and hence, in practice, there is no liquidity risk, the only risk retained for this business being the risk of default by the reinsurer, which is detailed under 'Credit Risk Management' below. The maturity analysis in respect of the S&P segment of the business, however, is presented on an estimated basis, in accordance with the anticipated maturity profile and on estimates of mortality.

(iii) Currency risk

Currency risk is the risk that the fair value or future cash flows of an asset or liability will change as a result of movements in foreign exchange rates. The Group's exposure to currency risk is minimised to the extent that the risk on investments denominated in foreign currencies which back unit-linked investment and insurance contracts is borne by policyholders. It is, however, exposed to currency risk through:

(i) its investment in Movestic, the assets and liabilities of which are principally denominated in Swedish Krona;

(ii) the trading operations of Movestic, which include the underwriting of insurance contracts in Norway giving rise to some exposure to the Norwegian Krone: as the Swedish business reinsures 90 per cent of the risk and has some assets denominated in the same currencies as the foreign insurance liabilities, most of the foreign currency exchange rate risk on these operations is eliminated; and

(iii) Movestic's part ownership of Modernac SA, an associated company, the assets and liabilities of which are denominated in Euros.

The Group's currency risk through its ownership of Movestic is reflected in:

(i) foreign exchange translation differences arising on the translation into sterling and consolidation of Movestic's financial statements; and

(ii) the impact of adverse exchange rate movements on cash flows between Chesnara plc and Movestic: in the short-term these relate to capital contributions made to Movestic to support its regulatory solvency capital resource requirements as it develops, while, in the medium-term there is the prospect of cash flows from Movestic to Chesnara by way of dividend payments. The risk on cash flows is managed by closely monitoring exchange rate movements and buying forward foreign exchange contracts, where deemed appropriate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

(iii) Currency risk (continued)

The following tables set out the Group's exposure to assets and liabilities denominated in foreign currencies, expressed in sterling, at the respective balance sheet date:

31 December	2013 £000	2012 £000
Swedish Krona		
Assets	1,833,571	1,515,969
Liabilities	(1,791,390)	(1,475,561)
Net assets	**42,181**	**40,408**
Norwegian Krone		
Assets	5,137	4,164
Liabilities	(4,976)	(4,526)
Net liabilities	**161**	**(362)**
Euro		
Assets	666	1,275
Liabilities	(8)	(33)
Net assets	**658**	**1,242**

(iv) Sensitivities

The table below shows the impact of movements in market risk variables identified above on profit before tax for the year under review and on shareholder equity as at the balance sheet date.

The variables are:

(i) a 10% increase and decrease in the value of assets backing unit-linked insurance and investment contract liabilities;

(ii) a 10% increase and decrease in equity and property values;

(iii) a 100 basis point increase and decrease in per annum market rates of interest; and

(iv) a 10% favourable and adverse movement in foreign currency exchange rates.

As explained above, market risks relating to assets backing unit-linked insurance and investment contract liabilities are borne by policyholders, while there is shareholder exposure to volatility in asset-related fees due to the impact of interest rate, equity price and foreign exchange rate movements on the fair value of the assets held in the linked funds, on which asset-related fees are based. Accordingly, the sensitivities to these risks are presented as generic sensitivities to unit-linked asset movements.

Variation in/arising from	2013		2012	
	Profit before tax £m	Shareholders' equity £m	Profit before tax £m	Shareholders' equity £m
100 bp increase in market rates of interest	9.3	7.3	18.6	14.1
100 bp decrease in market rates of interest	(11.5)	(9.0)	(23.7)	(18.0)
10% increase in equity and property prices	11.8	9.3	10.6	8.1
10% decrease in equity and property prices	(11.8)	(9.3)	(10.6)	8.1
10% favourable movement in SEK: sterling exchange rate	0.3	4.7	0.2	4.5
10% adverse movement in SEK: sterling exchange rate	(0.2)	(3.8)	(0.1)	(3.7)

Credit risk management
The Group has exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Key areas where the Group is exposed to credit risk are:

- Counterparty risk with respect to debt securities and cash deposits;
- Reinsurers' share of insurance liabilities;
- Amounts deposited with reinsurers in relation to investment contracts;
- Amounts due from reinsurers in respect of claims already paid; and
- Insurance and other receivables.

In addition there will be some exposures to individual policyholders, on amounts due on insurance contracts. These are tightly controlled, with contracts being terminated or benefits amended if amounts owed are outstanding for more than a specified period of time, so that there is no significant risk to the results of the businesses.

The Group businesses structure the levels of credit risk they accept by placing limits on their exposure to a single counterparty, or group of counterparties. Such risks are subject to at least an annual review, while watch lists are maintained for exposures requiring additional review.

Although the businesses hold a significant proportion of their financial assets in debt securities and cash deposits the risk of default on these is mitigated to the extent that any losses arising in respect of unit-linked assets backing the insurance and investment contracts which the businesses issue, would effectively be passed on to policyholders and investors through the unit-linked funds backing the insurance and investment contracts.

Reinsurance is used to manage insurance risk in the businesses. This does not, however, discharge the businesses' liability as primary insurers. If a reinsurer fails to pay a claim for any reason, the businesses remain liable for the payment to the policyholder. In respect of Movestic, the current guidelines state that re-insurance should only be effected with counterparties with a credit rating of A or higher, except for the reinsurer which is an associate of Movestic: this credit risk is managed by Movestic being represented on the Board of the reinsurer and, therefore, being able to influence its strategy and operational decisions.

The creditworthiness of major reinsurers is considered on an annual basis by reviewing their financial strength.

The following table presents the assets of the Group which are subject to credit risk and a reconciliation to the balance sheet carrying value of each item:

31 December		2013			2012	
	Amount not subject to credit risk £000	Amount subject to credit risk £000	Balance sheet carrying value £000	Amount not subject to credit risk £000	Amount subject to credit risk £000	Balance sheet carrying value £000
Holdings in collective investment schemes	3,440,542	450	3,440,992	3,008,808	991	3,009,799
Debt securities	137,632	233,034	370,666	139,513	223,864	363,377
Cash and cash equivalents	57,721	126,542	184,263	86,446	142,230	228,676
Derivative financial instruments	2,633	323	2,956	2,889	206	3,095
Reinsurers' share of insurance contract liabilities	–	379,894	379,894	–	278,692	278,692
Amounts deposited with reinsurers	–	34,293	34,293	–	30,245	30,245
Insurance and other receivables	26,970	19,412	46,382	20,620	3,693	24,313
Reinsurers' share of accrued policyholder claims	–	11,399	11,399	–	4,489	4,489
Income taxes	–	2,608	2,608	–	4,299	4,299
Total	**3,665,498**	**807,955**	**4,473,453**	**3,258,276**	**688,709**	**3,946,985**

The amounts presented above as not being subject to credit risk represent unit-linked assets where the risk is borne by the holders of unit-linked insurance and investment contracts, except for (i) reinsurers' share of insurers' contract provisions and (ii) amounts deposited with reinsurers in respect of investment contracts, where the risk of default is borne by shareholders.

Assets held to cover Insurance contracts with DPF, held within a segregated with-profits fund, are included as being subject to credit risk, as such risk will be borne by shareholders where default would result in there being insufficient with-profits policyholder assets to fund minimum guaranteed obligations. However, in normal circumstances (where the asset share is in excess of the minimum guaranteed amount) substantially all the credit risk remains with policyholders.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

Credit risk management (continued)

The Group's exposure to credit risk is summarised as:

Credit rating As at 31 December 2013	AAA £000	AA £000	A £000	Below A £000	Unrated £000	Total £000
Reinsurers share of insurance contract liabilities	–	124,658	3,848	–	251,388	379,894
Holdings in collective investment schemes	–	–	450	–	–	450
Amounts deposited with reinsurers	–	–	–	–	34,293	34,293
Debt securities at fair value through income	143,690	83,560	4,581	–	1,203	233,034
Insurance and other receivables	738	12,774	1,262	–	4,638	19,412
Reinsurers share of accrued policyholder claims	–	4,389	1,030	–	5,980	11,399
Derivative financial instruments	–	–	323	–	–	323
Income taxes	–	2,608	–	–	–	2,608
Cash and cash equivalents	–	36,768	89,724	–	50	126,542
Total	**144,428**	**264,757**	**101,218**	**–**	**297,552**	**807,955**
As at 31 December 2012						
Reinsurers share of insurance contract liabilities	–	38,084	(3,496)	–	244,104	278,692
Holdings in collective investment schemes	–	–	991	–	–	991
Amounts deposited with reinsurers	–	–	–	–	30,245	30,245
Debt securities at fair value through income	218,002	2,006	2,611	–	1,245	223,864
Insurance and other receivables	1,536	–	–	–	2,157	3,693
Reinsurers share of accrued policyholder claims	–	632	203	–	3,654	4,489
Derivative financial instruments	–	–	206	–	–	206
Income taxes	–	–	–	–	4,299	4,299
Cash and cash equivalents	21,024	47,362	73,838	–	6	142,230
Total	**240,562**	**88,084**	**74,353**	**–**	**285,710**	**688,709**

Included within unrated reinsurers' share of insurance contract provisions and unrated amounts deposited with reinsurers, in respect of investment contracts is a total significant exposure of £265.0m as at 31 December 2013 (31 December 2012: £251.4m) to Guardian, which does not have a published credit rating. Of this amount £210.5m (31 December 2012: £207.0m) is in respect of currently guaranteed benefits. This counterparty exposure was mitigated during 2006 when Guardian granted to CA a floating charge over related investment assets, which ranks that company equally with Guardian policyholders. In order to monitor the ongoing creditworthiness of Guardian, CA reviews the financial statements and regulatory returns submitted by Guardian to the PRA on an annual basis.

No credit limits were exceeded during the year ended 31 December 2013.

Financial assets that are past due or impaired

In 2008, a cash deposit with Kaupthing Singer & Friedlander ('KSF') was written down by its full amount of £1,091,000 as a result of KSF entering administration. During 2013, further interim distributions totalling £59,794 (2012: £141,331) were made from the administrators in respect of the deposit.

There are no other Group financial assets that are impaired, would otherwise be past due, or impaired, whose terms have been negotiated or past due but not impaired.

The Group has no significant exposure to Euro-denominated sovereign debt as at 31 December 2013.

7 Business combinations

On 28 November 2013, Chesnara plc acquired the entire issued share capital (100%) of Protection Life Company Limited (previously Direct Line Life Insurance Company Limited) from Direct Line Insurance Group plc for a total consideration of £39,300,000, paid in cash. The Protection Life purchase supports one of our stated strategic aims of acquiring life and pensions businesses.

Protection Life is a UK-based life insurance company. It became substantially closed to new business on 5 July 2011 and has been focused since then on managing the existing portfolio in line with the run-off plan agreed at the time with the then FSA. Prior to closure to new business, Protection Life predominantly offered non-linked products including mortgage life cover, fixed term life cover (both with and without critical illness cover) and over 50's life cover to UK customers distributed under both its own brand and also in recent years, but before the closure to new business, on a white label basis.

The acquisition of this shareholding has given rise to a profit on acquisition of £2.8m calculated as follows:

	Book value £000	Provisional fair value adjustments £000	Fair value £000
Assets			
Intangible assets			
Acquired value of in-force business	–	20,211	20,211
Deferred tax asset	15	–	15
Reinsurers' share of insurance contract provisions	93,826	–	93,826
Financial assets:			
Debt securities at fair value through income	24,940	–	24,940
Insurance and other receivables	13,254	–	13,254
Prepayments	4	–	4
Total financial assets	38,198	–	38,198
Reinsurers' share of accrued policyholder claims	5,284	–	5,284
Cash and cash equivalents	7,375	–	7,375
Total assets	**144,698**	**20,211**	**164,909**
Liabilities			
Insurance contract provisions	103,917	–	103,917
Other provisions	2,000	–	2,000
Reinsurance payables	14	–	14
Payables related to direct insurance contracts	6,163	–	6,163
Deferred tax	–	4,042	4,042
Income taxes	512	–	512
Other payables	6,154	–	6,154
Total liabilities	**118,760**	**4,042**	**122,802**
Net assets	**25,938**	**16,169**	**42,107**
Net assets acquired			**42,107**
Total consideration, paid in cash			**(39,300)**
Profit arising on business combination			**2,807**

The assets and liabilities at the acquisition date in the table above are stated at their provisional fair values and may be amended for 12 months after the date of acquisition in accordance with IFRS 3, Business Combinations.

Acquired receivables

Within the net assets acquired are receivable balances totalling £112.4m, which are held at fair value. For all receivables other than reinsurers' share of insurance contract provisions the gross contractual amounts receivable are equal to fair value. The reinsurers' share of insurance contract provisions receivable balance of £93.0m is discounted as a result of the long-term nature of this asset. Gross contractual amounts receivable are estimated as being £255.0m.

Acquired value of in-force business

The acquisition has resulted in the recognition of net of tax intangible asset amounting to £16.2m, which represents the present value of the future post-tax cash flows expected to arise from policies that were in force at the point of acquisition. The asset has been valued using a discounted cash flow model that projects the future surpluses that are expected to arise from the business. The model factors in a number of variables, of which the most influential are; the policyholders' ages, mortality rates, expected policy lapses, expenses that are expected to be incurred to manage the policies and future investment growth, as well as the discount rate that has been applied. This asset will be amortised over its expected useful life.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

7 Business combinations (continued)

Gain on acquisition

As shown on the previous page a gain of £2.8m has been recognised on acquisition. Under IFRS 3, a gain on acquisition is defined as being a "bargain purchase". In the opinion of the Directors a gain on acquisition arises as a result of the following key factors:

- The previous owners of Protection Life, Direct Line Group (DLG) are a predominantly general insurance group. Protection Life is therefore, in the context of the previous owners, a small non-core business that does not fit into the wider Direct Line Group strategy. DLG Management's areas of expertise are focused on general insurance as opposed to life insurance;
- A consequence of the above is that the implementation of Solvency II to a non-core element of the Direct Line Group could be both time consuming and expensive, especially given that Management's areas of expertise are more focused on general insurance rather than life insurance. Applying Solvency II to Protection Life could be a management distraction that is alleviated as a result of a disposal; and
- The IFRS valuation of insurance contract liabilities at acquisition is based on expense assumptions that are applicable to the Chesnara Group. Future expenses under Chesnara ownership are expected to be lower than under the previous owners, and therefore the price that DLG was willing to sell for could feasibly be reduced as a result of this dynamic.

Acquisition-related costs

The costs in respect of the transaction amounted to £2.4m. £1.6m of these costs have been included in Administration Expenses within the Consolidated Statement of Comprehensive Income. The remainder of the costs are loan arrangement fees, which have been netted off against the proceeds of the loan used to fund the acquisition, and will be reflected in the Consolidated Statement of Comprehensive Income as an interest cost as the loan runs its course, using an Effective Interest Rate model.

Results of Protection Life

The results of PL have been included in the consolidated financial statements of the Group with effect from 28 November 2013, and have contributed total net revenue of £1.0m over this period, whilst contributing £0.2m profit to the overall consolidated profit before tax, before the amortisation of the AVIF intangible asset. Had PL been consolidated from 1 January 2013 the Consolidated Statement of Comprehensive Income would have included net revenue of £17.0m, and would have contributed £5.3m profit before tax to the overall consolidated profit before tax.

8 Exceptional item

On 1 January 2012 S&P policyholder liabilities to taxation were, with effect from 1 January 2012, re-classified within the Consolidated Balance Sheet from deferred tax liabilities to insurance contract provisions. The purpose of this was to align the classification with that adopted by the CA operating segment. As a consequence of this there were:

(i) as at 1 January 2012 a reduction of £4.8m in deferred tax liabilities and an equal and opposite increase of £4.8m in insurance contract provisions; and

(ii) in the 2012 Consolidated Statement of Comprehensive Income a pre-tax charge of £4.8m and a deferred tax release to income tax of £4.8m, both of these amounts being presented as exceptional items, by virtue of their size and incidence. The net-of-tax result in the Consolidated Statement of Comprehensive Income attributable to these exceptional items is, accordingly, £nil.

9 Operating segments

The Group considers that it has no product or distribution-based business segments. It reports segmental information on the same basis as reported internally to the Chief Operating Decision Maker, which is the Board of Directors of Chesnara plc.

The segments of the Group as at 31 December 2013 comprise:

CA

This segment is part of the Group's UK life insurance and pensions run-off portfolio and comprises the original business of Countrywide Assured plc, the Group's principal UK operating subsidiary, and of City of Westminster Assurance Company Limited which was acquired in 2005 and the long-term business of which was transferred to Countrywide Assured plc during 2006. It is responsible for conducting unit-linked and non-linked business.

S&P

This segment, which was acquired on 20 December 2010, comprises the business of Save & Prosper Insurance Limited and its subsidiary Save & Prosper Pensions Limited. It is responsible for conducting both unit-linked and non-linked business, including a with-profits portfolio, which carries significant additional market risk, as described in Note 6 'Management of financial risk'. On 31 December 2011 the whole of the business of this segment was transferred to Countrywide Assured plc under the provisions of Part VII of the Financial Services and Markets Act 2000.

PL

This segment represents the business of Protection Life, which was purchased on 28 November 2013. PL is included within the Group's UK business.

Movestic

This segment comprises the Group's Swedish life and pensions business, Movestic Livförsäkring AB ('Movestic') and its subsidiary and associated companies, which are open to new business and which are responsible for conducting both unit-linked and non-linked business.

Other Group Activities

The functions performed by the parent company, Chesnara plc, are defined under the operating segment analysis as Other Group Activities. Also included therein are consolidation and elimination adjustments.

Other than the addition of the PL segment as a result of the purchase of Protection Life Company Limited during the year there were no changes to the basis of segmentation during the year ended 31 December 2013.

The accounting policies of the segments are the same as those for the Group as a whole. Any transactions between the business segments are on normal commercial terms in normal market conditions. The Group evaluates performance of operating segments on the basis of the profit before tax attributable to shareholders and on the total assets and liabilities of the reporting segments and the Group. There were no changes to the measurement basis for segment profit during the year ended 31 December 2013.

(i) Segmental income statement for the year ended 31 December 2013

Year ended 31 December	CA £000	S&P £000	PL £000	UK Total £000	Movestic £000	Other Group Activities £000	Total £000
Net insurance premium revenue	49,331	7,325	1,183	57,839	16,630	–	74,469
Fee and commission income	31,893	2,499	–	34,392	35,598	–	69,990
Net investment return	198,807	152,413	(143)	351,077	216,182	204	567,463
Total revenue (net of reinsurance payable)	**280,031**	**162,237**	**1,040**	**443,308**	**268,410**	**204**	**711,922**
Other operating income	6,484	11,761	–	18,245	4,025	–	22,270
Segmental income	**286,515**	**173,998**	**1,040**	**461,553**	**272,435**	**204**	**734,192**
Net insurance contract claims and benefits incurred	(159,179)	(120,333)	(249)	(279,761)	(7,284)	–	(287,045)
Net change in investment contract liabilities	(92,878)	(6,163)	–	(99,041)	(215,523)	–	(314,564)
Fees, commission and other acquisition costs	(738)	(32)	(92)	(862)	(18,588)	–	(19,450)
Administrative expenses							
Amortisation charge on software assets	–	–	–	–	(2,188)	–	(2,188)
Depreciation charge on property and equipment	(22)	–	–	(22)	(187)	–	(209)
Other	(7,663)	(9,878)	(114)	(17,655)	(14,870)	(3,839)	(36,364)
Other operating expenses							
Charge for amortisation of acquired value of in-force business	(2,358)	(774)	(169)	(3,301)	(4,229)	–	(7,530)
Charge for amortisation of acquired value of customer relationships	–	–	–	–	(301)	–	(301)
Other	(924)	(1,143)	(391)	(2,458)	(4,085)	60	(6,483)
Segmental expenses	**(263,762)**	**(138,323)**	**(1,015)**	**(403,100)**	**(267,255)**	**(3,779)**	**(674,134)**
Segmental income less expenses	**22,753**	**35,675**	**25**	**58,453**	**5,180**	**(3,575)**	**60,058**
Share of profit from associates	–	–	–	–	1,252	–	1,252
Profit arising on business combinations	–	–	–	–	–	2,807	2,807
Financing costs	–	(4)	–	(4)	(2,140)	(1,383)	(3,527)
Profit/(loss) before tax	**22,753**	**35,671**	**25**	**58,449**	**4,292**	**(2,151)**	**60,590**
Income tax credit/(expense)				(11,604)	(423)	800	(11,227)
Profit/(loss) after tax				**46,845**	**3,869**	**(1,351)**	**49,363**

(ii) Segmental balance sheet as at 31 December 2013

31 December	CA £000	S&P £000	PL £000	Movestic £000	Other Group Activities £000	Total £000
Total assets	1,899,700	1,263,269	181,059	1,853,374	40,319	5,237,721
Total liabilities	(1,824,706)	(1,169,406)	(125,783)	(1,791,943)	(78,781)	(4,990,619)
Net assets/(liabilities)	**74,994**	**93,863**	**55,276**	**61,431**	**(38,462)**	**247,102**
Investment in associates	–	–	–	4,088	–	4,088
Additions to non-current assets	–	–	20,211	17,787	–	37,998

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

9 Operating segments (continued)

(iii) Segmental income statement for the year ended 31 December 2012

Year ended 31 December	CA £000	S&P £000	UK Total £000	Movestic £000	Other Group Activities £000	Total £000
Net insurance premium revenue	54,785	8,987	63,772	16,412	–	80,184
Fee and commission income	35,191	2,776	37,967	28,691	–	66,658
Net investment return	128,009	105,936	233,945	97,846	262	332,053
Total revenue (net of reinsurance payable)	**217,985**	**117,699**	**335,684**	**142,949**	**262**	**478,895**
Other operating income	3,484	11,114	14,598	5,047	–	19,645
Segmental income	**221,469**	**128,813**	**350,282**	**147,996**	**262**	**498,540**
Net insurance contract claims and benefits incurred	(140,502)	(97,787)	(238,289)	(7,057)	–	(245,346)
Net change in investment contract liabilities	(52,679)	(4,134)	(56,813)	(97,040)	–	(153,853)
Fees, commission and other acquisition costs	(947)	(62)	(1,009)	(16,958)	–	(17,967)
Administrative expenses						
Amortisation charge on software assets	–	–	–	(2,188)	–	(2,188)
Depreciation charge on property and equipment	(22)	–	(22)	(187)	–	(209)
Other	(8,105)	(11,000)	(19,105)	(13,053)	(2,474)	(34,632)
Other operating expenses						
Charge for amortisation of acquired value of in-force business	(2,892)	(852)	(3,744)	(4,119)	–	(7,863)
Charge for amortisation of acquired value of customer relationships	–	–	–	(391)	–	(391)
Other	(625)	(1,212)	(1,837)	(5,046)	(2,322)	(9,205)
Segmental expenses	**(205,772)**	**(115,047)**	**(320,819)**	**(146,039)**	**(4,796)**	**(471,654)**
Segmental income less expenses	**15,697**	**13,766**	**29,463**	**1,957**	**(4,534)**	**26,886**
Share of profit from associates	–	–	–	1,244	–	1,244
Exceptional item	–	(4,778)	(4,778)	–	–	(4,778)
Financing costs	–	(1)	(1)	(2,451)	(1,218)	(3,670)
Profit/(loss) before tax	**15,697**	**8,987**	**24,684**	**750**	**(5,752)**	**19,682**
Income tax credit/(expense)						
Income tax credit/(expense) – before exceptional item			2,384	(323)	1,420	3,481
Exceptional item			4,778	–	–	4,778
After exceptional item			7,162	(323)	1,420	8,259
Profit/(loss) after tax			**31,846**	**427**	**(4,332)**	**27,941**

(iv) Segmental balance sheet as at 31 December 2012

31 December	CA £000	S&P £000	Movestic £000	Other Group Activities £000	Total £000
Total assets	1,815,021	1,266,946	1,534,263	34,391	4,650,621
Total liabilities	(1,728,523)	(1,191,376)	(1,476,185)	(36,191)	(4,432,275)
Net assets/(liabilities)	**86,498**	**75,570**	**58,078**	**(1,800)**	**218,346**
Investments in associates	–	–	2,902	–	2,902
Additions to non-current assets	230	–	11,353	–	11,583

10 Fees and commission income

Year ended 31 December Fee income	2013 £000	2012 £000
Policy-based fees	14,910	14,143
Fund management-based fees	31,117	25,324
Benefit-based fees	16,962	21,614
Change in deferred income – gross	1,019	1,116
Change in deferred income – reinsurers' share	(66)	(45)
Total fee income	63,942	62,152
Commission income	6,048	4,506
Total fee and commission income	**69,990**	**66,658**

11 Net investment return

Year ended 31 December	2013 £000	2012 £000
Dividend income	19,049	46,774
Interest income	19,256	25,961
Rental income from investment properties	4,604	7,612
Net fair value gains and losses		
Equity securities designated as at fair value through income on initial recognition	503,258	224,848
Debt securities designated as at fair value through income on initial recognition	20,679	29,609
Derivative financial instruments	6,814	2,899
Investment properties	(6,197)	(5,650)
Net investment return	**567,463**	**332,053**

Net fair value gains and losses in respect of holdings in collective investment schemes are included in the line that is most appropriate taking into account the nature of the underlying investments.

No amounts included in net fair value gains and losses of financial instruments were estimated using a valuation technique (year ended 31 December 2012: £nil).

12 Other operating income

Year ended 31 December	2013 £000	2012 £000
Release of unused provisions	409	629
Administration fees charged to reinsurers	87	95
Professional indemnity insurance recoveries	35	52
Investment management fee rebate	17,550	13,483
HMRC interest on tax refund	16	–
Charges to policyholder funds for yield tax	4,020	5,046
Other	153	340
Total other operating income	**22,270**	**19,645**

All of the income streams set out in Notes 10, 11 and 12 equate to revenue as defined by IAS 18.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

13 Insurance contract claims and benefits

Year ended 31 December	2013 £000	2012 £000
Claims and benefits paid to insurance contract holders	281,800	272,479
Net increase in insurance contract provisions	62,249	20,732
Total insurance contract claims and benefits	**344,049**	**293,211**
Recoveries from reinsurers	(57,004)	(47,865)
Net insurance contract claims and benefits incurred	**287,045**	**245,346**

14 Change in investment contract liabilities

Year ended 31 December	2013 £000	2012 £000
Net changes in the fair value of investment contracts designated on initial recognition as fair value through income	309,130	114,468
Net changes in the fair value of policyholders' funds held by the Group designated on initial recognition as fair value through income	11,002	42,195
Reinsurers' share	(5,568)	(2,810)
Net increase in investment contract liabilities	**314,564**	**153,853**

Investment contract benefits comprise benefits accruing to holders of investment contracts issued by the Group.

15 Fees, commission and other acquisition costs

Year ended 31 December	2013 £000	2012 £000
Directly expensed costs:		
Insurance contracts		
Commission	6,577	5,806
New business and renewal costs	2,693	4,357
Investment contracts		
Commission	12,349	7,579
New business and renewal costs	3,861	2,851
Additions to deferred acquisition costs:		
Insurance contracts	(6,344)	(5,654)
Investment contracts	(9,029)	(4,604)
Amortisation of deferred acquisition costs:		
Insurance contracts	6,820	5,991
Investment contracts	2,565	1,667
Investment contracts-reinsurance	(42)	(26)
Total	**19,450**	**17,967**

16 Administrative expenses

Year ended 31 December	2013 £000	2012 £000
Personnel-related costs (Note 48)	14,906	12,910
Investment management fees	10,901	9,848
Amortisation charge on software assets	2,580	2,188
Depreciation charge on property and equipment	216	209
Costs paid to third-party administrators	7,903	8,201
Other goods and services	2,255	3,673
Total	**38,761**	**37,029**

Included in Other goods and services above are the following amounts payable to the Auditor and its associates, exclusive of VAT.

Year ended 31 December	2013 £000	2012 £000
Fees payable to the Company's Auditor for the audit of the Company's annual accounts	48	94
Fees payable to the Company's Auditor and its associates for other services to the Group:		
The audit of the Company's subsidiaries pursuant to legislation	429	386
Audit-related assurance services*	401	192
Taxation compliance services	–	27
All other services	8	18
Total	**886**	**717**

*Includes the audit of regulatory returns submitted to the UK regulator in both years. 2013 includes fees associated with the acquisition of Protection Life and the S&P capital extraction.

17 Other operating expenses

Year ended 31 December	2013 £000	2012 £000
Charge for amortisation of acquired value of in-force business	**7,530**	**7,863**
Charge for amortisation of acquired value of customer relationships (AVCR)	**301**	**391**
Other		
Increase in other provisions	–	2,546
Direct operating expenses of investment properties		
Revenue-generating properties	1,142	1,212
Non revenue-generating properties	105	233
Recovery of cash deposit	(60)	(141)
Payment of yield tax relating to policyholder funds	4,020	5,046
Other	1,276	309
Total	**6,483**	**9,205**

The recovery of cash deposit represents interim distributions received from the administrators of Kaupthing Singer & Friedlander relating to a cash deposit, previously written down and charged to operating expenses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

18 Financing costs

Year ended 31 December	2013 £000	2012 £000
Interest expense on bank borrowings	1,387	1,219
Interest expense on financial reinsurance	1,965	2,313
Other interest	175	138
Total financing costs	**3,527**	**3,670**

Interest expense on bank borrowings is calculated using the effective interest rate method and is the total interest expense for financial liabilities that are not designated at fair value through income.

19 Income tax before exceptional item

Total income tax before exceptional item comprises: Year ended 31 December	2013 £000	2012 £000
CA, S&P and Other Group Activities – net (expense)/credit	(10,804)	3,804
Movestic – net expense	(423)	(323)
Total net (expense)/credit	**(11,227)**	**3,481**

CA, S&P and Other Group Activities Year ended 31 December	2013 £000	2012 £000
Current tax		
Current year	(7,294)	(2,939)
Overseas tax	(541)	(582)
Adjustment to prior years	–	(29)
Net expense	(7,835)	(3,550)
Deferred tax		
Origination and reversal of temporary differences excluding exceptional item	(2,969)	7,354
Total income tax (expense)/credit	**(10,804)**	**3,804**

Reconciliation of effective tax rate on profit before tax Year ended 31 December	2013 £000	2012 £000
Profit before tax and exceptional item	**56,299**	**23,710**
Income tax using the domestic corporation tax rate of 23.25% (2012: 24.5%)	(13,090)	(5,809)
Non-taxable profit on acquisition of subsidiary	653	–
Other permanent differences	(352)	(70)
Effect of UK tax bases on insurance profits		
Offset of franked investment income	2,978	3,525
Variation in rate of tax on amortisation of acquired in-force value	366	389
Foreign tax	(415)	–
Effect of change in tax rate	(965)	–
Impact of new life tax regime	–	6,129
Other	21	(331)
Over/(under) provided in previous years	–	(29)
Total income tax (expense)/credit	**(10,804)**	**3,804**

A new regime for the taxation of life assurance companies in the UK was introduced with effect from 1 January 2013. The new regime bases the taxable trading profit on IFRS profits rather than on PRA return surplus generated as under the previous rules and also treats pension business separately from life assurance business. The 2012 tax charge reflected a significant deferred tax credit as a result of this change, as the pension losses in the UK life company were ascribed value for the first time in 2012. In addition, as part of the transition to the new regime, accumulated historical profits as at 31 December 2012 were compared between the two bases and the taxable difference is being charged over ten years. This transitional adjustment created a deferred tax charge during 2012, partially offsetting the pension related recovery noted here. In 2013, the deferred tax asset relating to pension losses has been fully utilised creating a deferred tax charge in the year.

Movestic
Year ended 31 December

	2013 £000	2012 £000
Current tax		
Current year expense	–	–
Adjustment to prior years	–	–
Net credits	–	–
Deferred tax		
Origination and reversal of temporary differences	(423)	(323)
Total income tax expense	**(423)**	**(323)**

Reconciliation of effective tax rate on profit before tax
Year ended 31 December

	2013 £000	2012 £000
Profit before tax	**4,292**	**750**
Income tax using the domestic corporation tax rate of 22%	(944)	(197)
Non-taxable income in relation to unit-linked business	366	655
Non-taxable fair value adjustment	423	(215)
Impact of different tax rate for subsidiaries	(95)	(41)
Permanent differences	(201)	(179)
Unrecognised tax recoverable	61	(309)
Non-deductible expenses	(33)	(37)
Total income tax expense	**(423)**	**(323)**

20 Deferred acquisition costs

Year ended 31 December

	CA £000	Movestic £000	2013 Total £000	2012 Total £000
Balance at 1 January	**5,057**	**17,498**	**22,555**	**19,720**
Additions arising from new business	–	15,355	15,355	10,255
Amortisation charged to income	(646)	(6,384)	(7,030)	(7,658)
Impairment losses	–	(2,355)	(2,355)	–
Foreign exchange translation difference	–	(363)	(363)	238
Balance at 31 December	**4,411**	**23,751**	**28,162**	**22,555**
Current	499	2,679	3,178	2,152
Non-current	3,912	21,072	24,984	20,403
Total	**4,411**	**23,751**	**28,162**	**22,555**

The amortisation charged to income is recognised in Fees, Commission and Other Acquisition Costs (see Note 15).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

21 Acquired value of in-force business (AVIF)

31 December	2013 £000	2012 £000
Cost:		
Balance at 1 January	**128,779**	**127,907**
Additions – acquisition of subsidiary	20,211	–
Foreign exchange translation difference	(451)	872
Balance at 31 December	**148,539**	**128,779**
Amortisation and impairment losses:		
Balance at 1 January	**52,661**	**44,561**
Amortisation for the year	7,530	7,863
Foreign exchange translation difference	(267)	237
Balance at 31 December	**59,924**	**52,661**
Carrying amounts		
At 1 January	**76,118**	**83,346**
At 31 December	**88,615**	**76,118**
Current	9,137	7,228
Non-current	79,478	68,890
Total	**88,615**	**76,118**

The amortisation is charged to the Consolidated Statement of Comprehensive Income and is recognised in Other Operating Expenses (see Note 17).

22 Acquired value of customer relationships (AVCR)

31 December	2013 £000	2012 £000
Cost:		
Balance at 1 January	**4,164**	**4,113**
Foreign exchange translation difference	(21)	51
Balance at 31 December	**4,143**	**4,164**
Amortisation and impairment losses:		
Balance at 1 January	**2,280**	**1,858**
Amortisation for the year	301	391
Foreign exchange translation difference	(21)	31
Balance at 31 December	**2,560**	**2,280**
Carrying amounts		
At 1 January	**1,884**	**2,255**
At 31 December	**1,583**	**1,884**
Current	290	291
Non-current	1,293	1,593
Total	**1,583**	**1,884**

The amortisation period of AVCR is based on the underlying returns on the policies expected to be written as a result of customer relationships.

The amortisation is charged to income and is recognised in Other Operating Expenses (see Note 17).

23 Software assets

31 December	2013 £000	2012 £000
Cost:		
Balance at 1 January	**12,483**	**11,229**
Additions	1,882	1,094
Foreign exchange translation difference	(151)	160
Balance at 31 December	**14,214**	**12,483**
Amortisation and impairment losses:		
Balance at 1 January	**6,771**	**4,485**
Amortisation charge for the year	2,580	2,188
Foreign exchange translation difference	(141)	98
Balance at 31 December	**9,210**	**6,771**
Carrying amounts at 31 December	**5,004**	**5,712**
Current	1,921	2,349
Non-current	3,083	3,363
Total	**5,004**	**5,712**

24 Property and equipment

31 December	2013 £000	2012 £000
Cost:		
Balance at 1 January	**1,373**	**1,249**
Additions – acquisitions of subsidiary	158	–
Additions	550	235
Disposals	(55)	(123)
Foreign exchange translation difference	(26)	12
Balance at 31 December	**2,000**	**1,373**
Amortisation and impairment losses:		
Balance at 1 January	**1,004**	**864**
Additions – acquisitions of subsidiary	158	–
Depreciation charge for the year	216	209
Disposals	(39)	(82)
Foreign exchange translation difference	(12)	13
Balance at 31 December	**1,327**	**1,004**
Carrying amounts at 31 December	**673**	**369**
Current	207	138
Non-current	466	231
Total	**673**	**369**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

25 Investment in associate

31 December	2013 £000	2012 £000
Balance at 1 January	**2,902**	**1,613**
Share of profit	1,251	1,244
Foreign exchange translation difference	(65)	45
Balance at 31 December	**4,088**	**2,902**

Associates at 100%	Assets £000	Liabilities £000	Revenues £000	Profit £000
Modernac S.A.	32,093	23,751	10,502	2,554
Total 31 December 2013	**32,093**	**23,751**	**10,502**	**2,554**

Associates at 49%	Equity at 100% £000	Equity at 49% £000	49% share of profit £000
Modernac S.A.	8,342	4,088	1,252
Total 31 December 2013	**8,342**	**4,088**	**1,252**

26 Investment properties

31 December	2013 £000	2012 £000
Balance at 1 January	**100,167**	**132,128**
Additions	966	5,927
Disposals	(74,549)	(32,238)
Fair value adjustments	(6,197)	(5,650)
Balance at 31 December	**20,387**	**100,167**
Current	3,053	–
Non-current	17,334	100,167
Total	**20,387**	**100,167**

Investment properties were bought for investment purposes in line with the investment strategy of the Group. The properties are independently valued in accordance with International Valuation Standards on the basis of determining the open market value of the investment properties on an annual basis. The latest valuations were conducted as at 31 December 2013.

Income arises from investment properties in two streams:

(i) Fair value gains arising as a result of market appreciation in the value of the properties; and

(ii) Rental income arising from leases granted on the properties.

Both of these amounts are disclosed in Net Investment Return (see Note 11). Expenses incurred in the operation and maintenance of investment properties are disclosed in Other Operating Expenses (see Note 17).

27 Financial instruments

Group

Financial assets by measurement category
31 December

	2013 £000	2012 £000
Fair value through income		
Designated at fair-value through income on initial recognition	4,421,512	3,861,650
Derivative financial instruments	2,956	3,095
Insurance and other receivables	46,382	24,313
Prepayments	4,889	3,160
Total	**4,475,739**	**3,892,218**

Fair value is the amount for which an asset could be exchanged between willing parties in an arm's length transaction. The tables below show the determination of fair value according to a three-level valuation hierarchy. Fair values are generally determined at prices quoted in active markets (Level 1). However, where such information is not available, the Group applies valuation techniques to measure such instruments. These valuation techniques make use of market-observable data for all significant inputs where possible (Level 2), but, in some cases it may be necessary to estimate other than market-observable data within a valuation model for significant inputs (Level 3).

Fair value measurement at 31 December 2013 using

	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Equities				
Listed	479,617	–	–	479,617
Holdings in collective investment schemes	3,440,542	450	–	3,440,992
Debt securities – fixed rate				
Government Bonds	294,588	–	–	294,588
Listed	63,104	–	–	63,104
Debt securities – floating rate				
Listed	12,974	–	–	12,974
Total debt securities	370,666	–	–	370,666
Policyholders' funds held by the group	130,237	–	–	130,237
Derivative financial instruments	323	2,633	–	2,956
Total	**4,421,385**	**3,083**	**–**	**4,424,468**
Current				1,798,344
Non-current				2,626,124
Total				**4,424,468**
Financial liabilities				
Investment contracts at fair value through income	2,275,276	8,127	–	2,283,403
Liabilities related to policyholders' funds held by the group	130,237	–	–	130,237
Derivative financial instruments	–	387	–	387
Total	**2,405,513**	**8,514**	**–**	**2,414,027**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

27 Financial instruments (continued)

Fair value measurement at 31 December 2012 using	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Equities				
Listed	427,303	–	–	427,303
Holdings in collective investment schemes	3,008,808	991	–	3,009,799
Debt securities – fixed rate				
Government Bonds	306,623	–	–	306,623
Listed	46,677	–	–	46,677
Debt securities – floating rate				
Listed	10,077	–	–	10,077
Total debt securities	363,377	–	–	363,377
Policyholders' funds held by the group	61,171	–	–	61,171
Derivative financial instruments	310	2,785	–	3,095
Total	**3,860,969**	**3,776**	**–**	**3,864,745**
Current				1,466,685
Non-current				2,398,060
Total				**3,864,745**
Financial liabilities				
Investment contracts at fair value through income	2,010,545	11,769	–	2,022,314
Liabilities related to policyholders' funds held by the group	61,171	–	–	61,171
Derivative financial instruments	8	278	–	286
Total	**2,071,724**	**12,047**	**–**	**2,083,771**

Included within Holdings in collective investment schemes are amounts held with JPMorgan Life Limited through a reinsurance arrangement, under which the Group has reassured certain unit-linked liabilities. The contract does not transfer significant insurance risk and is accounted for as Holdings in collective investment schemes, representing the substance of the arrangement in place. These amounts have been classified as level 2 in the above hierarchy table as the reinsurance contract itself is not quoted but is valued using market-observable data.

Within derivative financial instruments is a financial reinsurance embedded derivative related to our Movestic operation. The Group has entered into a reinsurance contract with a third party that has a section that is deemed to transfer significant insurance risk and a section that is deemed not to transfer significant insurance risk. The element of the contract that does not transfer significant insurance risk has two components and has been accounted for as a financial liability at amortised cost and an embedded derivative asset at fair value.

The embedded derivative represents an option to repay the amounts due under the contract early at a discount to the amortised cost, with its fair value being determined by reference to market interest rate at the balance sheet date. It is, accordingly, determined at Level 2 in the three-level fair value determination hierarchy set out above.

The Investment contract liabilities in Level 2 of the valuation hierarchy represent the fair value of non-linked and guaranteed income and growth bonds liabilities valued using established actuarial techniques utilising market observable data for all significant inputs, such as investment yields.

Except as detailed in the following table, the Directors consider that the carrying value amounts of financial assets and financial liabilities recorded at amortised cost in the financial statements are approximately equal to their fair values:

31 December	Carrying amount		Fair value	
	2013 £000	2012 £000	2013 £000	2012 £000
Financial liabilities:				
Borrowings	94,377	48,324	95,457	50,198

Borrowings consist of bank loans and an amount due in relation to financial reinsurance.

The fair value of the bank loans are taken as the principal outstanding at the balance sheet date.

The amount due in relation to financial reinsurance is fair valued with reference to market interest rates at the balance sheet date.

There were no transfers between levels 1, 2 and 3 during the year.

Company

Year ended 31 December	2013 £000	2012 £000
Balance at 1 January	**146,699**	**146,699**
Acquisition of Protection Life Company Limited	39,300	–
Injection of capital into Protection Life on acquisition	13,112	–
Balance at 31 December	**199,111**	**146,699**
Current	–	–
Non-current	199,111	146,699
Total	**199,111**	**146,699**

A list of investments in subsidiaries held by the Group is disclosed in Note 54.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

28 Insurance and other receivables and prepayments

Group

Insurance and other receivables 31 December	2013 £000	2012 £000
Receivables arising from insurance contracts		
Brokers	–	694
Policyholders	4,895	3,667
Receivables arising from investment contracts		
Policyholders	7	7
Reinsurance receivables	11,835	231
Commission receivables	315	267
Debtor for professional indemnity insurance	78	92
Other receivables		
Loan to associated companies	662	642
Accrued interest income	11,122	4,775
Accrued rent	38	720
Receivables from fund management companies	7,271	3,943
Initial margin payments on derivatives	4,794	6,663
Other	5,365	2,612
Total	**46,382**	**24,313**
Current	44,577	22,548
Non-current	1,805	1,765
Total	**46,382**	**24,313**

The carrying amount is a reasonable approximation of fair value.

31 December	2013 £000	2012 £000
Prepayments	**4,889**	**3,160**
Current	4,039	2,210
Non-current	850	950
Total	**4,889**	**3,160**

The carrying amount is a reasonable approximation of fair value.

Company

Receivables and prepayments 31 December	2013 £000	2012 £000
Amounts due from subsidiary companies	605	510
Other receivables	10	25
Prepayments	21	50
Total	**636**	**585**
Current	636	585
Non-current	–	–
Total	**636**	**585**

The carrying amount is a reasonable approximation of fair value.

29 Derivative financial instruments

The Group does not hold derivatives outside the unit-linked and with-profits funds, except for an option to repay a financial reinsurance contract early, which comprises an embedded derivative.

31 December	2013		2012	
	Asset £000	Liability £000	Asset £000	Liability £000
Exchange-traded futures	866	(387)	516	(286)
Financial reinsurance embedded derivative	2,090	–	2,579	–
Total	**2,956**	**(387)**	**3,095**	**(286)**
Current	820	–	1,118	(286)
Non-current	2,136	(387)	1,977	–
Total	**2,956**	**(387)**	**3,095**	**(286)**

Derivatives within unit-linked funds

As part of its Investment management strategy, the Group purchases derivative financial instruments comprising part of its investment portfolio for unit-linked investment funds, which match the liabilities arising on its unit-linked insurance and investment business.

A variety of equity futures are part of the portfolio matching the unit-linked investment and insurance liabilities. Derivatives are used to facilitate more efficient portfolio management allowing changes in Investment strategy to be reflected by futures transactions rather than a high volume of transactions in the underlying assets.

All the contracts are exchange-traded futures, with their fair value being the bid price at the balance sheet date: They are, accordingly, determined at Level 1 in the three-level fair value determination hierarchy set out in Note 27.

Exchange-traded futures (by geographical investment market)

31 December	2013		2012	
	Asset £000	Liability £000	Asset £000	Liability £000
Australia	16	–	23	–
Switzerland	47	–	–	–
Europe	174	–	–	(26)
UK	101	(387)	140	(260)
Hong Kong	26	–	8	–
Japan	218	–	227	–
South Korea	–	–	16	–
Singapore	–	–	1	–
USA	284	–	101	–
Total	**866**	**(387)**	**516**	**(286)**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

29 Derivative financial instruments (continued)

Financial reinsurance embedded derivative

In respect of Movestic, the Group has entered into a reinsurance contract with a third party that has a section that is deemed to transfer significant insurance risk and a section that is deemed not to transfer significant insurance risk. This assessment has been determined by Management based on the contractual terms of the reinsurance agreement. The element of the contract that does not transfer significant insurance risk has two components and has been accounted for as a financial liability at amortised cost and an embedded derivative asset at fair value.

The embedded derivative represents an option to repay the amounts due under the contract early at a discount to the amortised cost, with its fair value being determined by reference to market interest rates at the balance sheet date. It is, accordingly, determined at Level 2 in the three-level fair value determination hierarchy set out in Note 27.

Derivatives within the S&P with-profits funds

As part of its investment management strategy, S&P enters into a limited range of derivative instruments to manage its exposure to various risks.

S&P uses equity index futures in order to economically hedge equity market risk in the with-profit funds' investments.

The change in fair value of the futures contracts is intended to offset the change in fair value of the underlying equities being hedged. S&P settles the market value of the futures contracts on a daily basis by paying or receiving a variation margin. The futures contracts are not discounted as this daily settlement is equal to the change in fair value of the futures. As a result, there is no additional fair value to recognise in relation to these derivatives on the balance sheet at the period end.

S&P also purchases exchange rate futures to mitigate exchange rate risk within its with-profits funds.

These contracts are exchange-traded contracts in active markets with their fair value being the bid price at the balance sheet date. They are, accordingly, determined at Level 1 in the three-level fair value determination hierarchy set out in Note 27.

30 Income tax assets

Income tax assets, which are all current, comprise:
31 December

	2013 £000	2012 £000
Group		
Corporation tax recoverable	2,608	4,299
Company		
Corporation tax recoverable	2,194	1,394

The carrying amount is a reasonable approximation of fair value.

31 Cash and cash equivalents

Group
31 December

	2013 £000	2012 £000
Bank and cash balances	64,978	76,115
Call deposits due within 1 month	82,692	58,552
Call deposits due after 1 month	36,593	94,009
Total cash and cash equivalents	**184,263**	**228,676**
Bank overdrafts	(1,127)	(602)
Cash and cash equivalents in the statement of cash flows	**183,136**	**228,074**

The effective interest rate on short-term bank deposits was 0.45% (2012: 0.74%), with an average maturity of 22 days (2012: 37 days). All deposits included in cash and cash equivalents were due to mature within 3 months of their acquisition.

Included in cash and cash equivalents held by the Group are balances totalling £73,274,000 (2012: £99,253,000) held in unit-linked policyholders' funds.

Company
31 December

	2013 £000	**2012 £000**
Bank and cash balances	94	389
Cash deposits due within 1 month	25,355	29,015
Cash deposits maturing between greater than 1 month and less than 1 year	12,040	3,008
Total	**37,489**	**32,412**

32 Capital management

(a) Objective

The Group's capital management framework is designed to provide security for all shareholders, while meeting the expectations of policyholders and shareholders. Accordingly it:

1) safeguards policyholders interests by meeting regulatory requirements established by the regulators of the insurance markets in which the Group's regulated companies operate, while not retaining unnecessary excess capital;

2) seeks to meet the dividend expectations of shareholders and to optimise the gearing ratio to ensure an efficient capital base;

3) ensures there is sufficient liquidity to meet obligations to policyholders, debt financiers and creditors as they fall due; and

4) maintains the Group as a going concern so that it continues to provide returns and to meet obligations to all stakeholders.

The Group's subsidiary and associate companies are subject to minimum regulatory capital requirements according to the jurisdictions in which they operate. In addition CA plc is required to prepare and submit a Group-level solvency capital statement in accordance with the EU Insurance Groups Directive (IGD).

The rules are designed to ensure that companies have sufficient assets to meet their liabilities in specified adverse circumstances. As such, there is, in the UK, a restriction on the full transfer of surpluses from the long-term business funds to shareholder funds in CA plc and PL, and on the full distribution of retained earnings from CA plc and PL to Chesnara and, in Sweden, on distributions from Movestic shareholder funds.

The overall capital dynamics of the Group are such that the UK businesses, being substantially in run-off, are net contributors of capital, which is reflected in the medium-term by way of dividend distributions to the parent company, while, in the medium-term, the Swedish business, as it expands, and before it achieves economies of scale, is a net consumer of capital, which is reflected by way of additional capital contributions from the parent company.

(b) Operation of the UK, Swedish and EU regulatory regimes

UK business

The operation of regulation with respect to the UK Businesses is such as to specify the minimum amount of capital that must be held in addition to the insurance liabilities as determined for regulatory purposes. This is established by reference to two calculations, being:

(i) the Pillar 1 calculation, which compares regulatory capital based on the characteristics of the in-force life assurance business with an associated measure of capital as prescribed by regulation; and

(ii) the Pillar 2 calculation, which compares a risk-based assessment of economic capital with an associated measure of capital based on a realistic assessment of insurance liabilities.

For CA plc and PL, for the whole of the period covered by these financial statements, the minimum regulatory capital requirement was determined by the first calculation, as this gave rise to the lesser measure of surplus capital. This calculation is set out below in Section (c) Regulatory Capital Resources and Requirements, together with the CA plc Board's policy in targeting regulatory capital resource cover for total regulatory capital resource requirements.

The long-term insurance business subsisting within CA plc includes with-profits business, for which that acquired from S&P are maintained in separate sub-funds. The scale of such with-profits business remains such that the Company falls outside of the scope of the PRA's "realistic capital" regime. Within these IFRS Financial Statements excess of policyholder assets and liabilities relating to these funds is classified within insurance contract provisions.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

32 Capital management (continued)

(b) Operation of the UK, Swedish and EU regulatory regimes (continued)

Swedish business

Movestic is subject to the Swedish regulatory regime and has to maintain a minimum level of regulatory capital, being the prescribed minimum solvency margin requirements.

The solvency surplus under the Swedish regulatory regime is the excess of the regulatory capital resources over the capital resource requirements which are based on the insurance business. This calculation is set out below in Section (c) Regulatory Capital Resources and Requirements together with the Movestic Board's policy in targeting regulatory capital resource cover for total regulatory capital resource requirements. The Swedish business also includes a 49% interest in an associated company, Modernac S.A. ('Modernac'), a Luxembourg-based reinsurer, which is subject to EU regulatory solvency requirements: its scale of operations are such that its capital resource requirement is the EU regulatory minimum.

Group

In addition to the solvency requirements for the UK and Swedish Businesses, as set out above, the Group is subject to the requirements of the EU Insurance Group Directive, in accordance with which the Group calculates the excess of the aggregate of regulatory capital resources determined on a group-wide basis over the aggregate minimum regulatory capital requirement imposed by local regulators. The requirement is that available Group capital resources, as set out in Section (d) Group Capital Position Statement below, should be at least 100% of capital requirements.

(c) Regulatory capital resources and requirements

UK business

The following summarises the capital resources and requirements of CA plc and PL, as determined for UK regulatory purposes (Pillar 1):

31 December	2013		2012	
	CA plc £m	PL £m	CA plc £m	PL £m
Available capital resources (CR)	96.4	39.2	99.3	53.3
Long-term insurance capital requirement (LTICR)	37.0	25.2	39.5	27.6
Resilience capital requirement (RCR)	7.1	–	10.5	–
Total capital resource requirements (CRR)	44.1	25.2	50.0	27.6
Excess of CR over CRR (solvency surplus)	52.3	14.0	49.3	25.7
Ratio of available CR to CRR	218%	156%	199%	193%
Target capital requirement cover	67.2	37.8	74.7	41.4
Excess of CR over target requirement	29.2	1.4	24.6	11.9

Available capital resources for CA plc as at 31 December 2013 are stated after provision for a dividend of £48.0m which was approved by the CA plc Board subsequent to 31 December 2013 (as at 31 December 2012: £40.0m subsequent to 31 December 2012).

Comparatives for PL have been provided for illustrative purposes only, as the company was purchased on 28 November 2013. Available capital resources for PL as at 31 December 2012 are stated after a dividend of £7.0m in relation to the 2012 financial year, which was paid during 2013. No dividends are proposed for PL in relation to the 2013 financial year.

(c) Regulatory capital resources and requirements (continued)

UK business (continued)

CA plc's Board, as a matter of policy, continues to target CR cover for total CRR at a minimum level of 162.5% of the LTICR plus 100% of the RCR.

Subsequent to the acquisition by Chesnara plc, PL's Board, has introduced a policy such that the CR should be maintained at a minimum of 150.0% of its LTICR.

Individual Capital Assessment (Pillar 2)

The PRA Prudential Sourcebooks require UK insurance companies to make their own assessment of their capital needs to a required standard (a 99.5% probability of being able to meet liabilities to policyholders after one year). In the light of scrutiny of this assessment, the PRA may impose its own additional individual capital guidance. The Individual Capital Assessment (ICA) is based on a realistic liability assessment, rather than on the statutory mathematical reserves, and involves stress testing the resultant realistic balance sheet for the impact of adverse events, including such market effects as significant falls in equity values, interest rate increases and decreases, bond defaults and further widening of bond spreads.

CA plc completed a full annual assessment during 2013 as a result of which it was concluded that the effective current and medium-term capital requirement constraints on distributions to Chesnara will continue to be on the basis set out under 'Regulatory capital resources and requirements' above. This assessment is subject to quarterly high-level updates until the next full annual assessment.

Swedish business

The following summarises the Capital Resources and the Capital Resources Requirements of Movestic as determined for Swedish regulatory purposes and Movestic's 49% proportionate share in the Capital Resources and Capital Resources Requirements of Modernac:

31 December	2013		2012	
	Movestic £m	Modernac £m	Movestic £m	Modernac £m
Available Capital Resources (CR)	34.8	4.7	32.5	3.5
Capital Resource Requirements (CRR)	11.2	1.4	11.6	1.3
Excess of CR over CRR (solvency surplus)	23.6	3.3	20.9	2.2
Ratio of available CR to CRR	311%	336%	280%	269%
Target capital requirement cover	16.9	n/a	17.4	n/a
Excess of CR over target requirement	17.9	n/a	15.1	n/a

The Movestic Board has set a minimum target of 150% of the regulatory capital requirement. Swedish solvency regulation requires that a certain proportion of assets, to be fully admissible, is to be held in the form of cash. The operation of this requirement may, from time to time, act as the operative constraint in determining the level of additional funding requirements, thereby causing the solvency ratio to rise above what it would otherwise have been, had the form of assets matching capital resources not been a constraint. Movestic's solvency ratio declines as the increasing scale of its business requires a higher level of regulatory capital: as the ratio approaches 150%, further planned capital contributions will be made by the Group.

Movestic, in accordance with local regulatory requirements, continues to make quarterly assessments of the risk-based capital requirements of its business: these indicate that capital resources currently provide a comfortable margin over capital resource requirements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

32 Capital management (continued)

(d) Group capital position statement

The following summarises the regulatory capital resources arising in both life and non-life entities, together with a statement of capital resources on a consolidated basis and with a reconciliation to shareholders' net equity established on the IFRS basis:

As at 31 December 2013	UK life businesses with-profits £000	UK life businesses non-participating £000	UK life businesses shareholder £000	UK life businesses total £000	Swedish life and non-life business total £000	Group life insurance businesses total £000
Shareholder funds outside long-term insurance funds – retained earnings	–	–	72,252	72,252	40,255	112,507
Shareholder funds in long-term insurance funds	51,768	21,084	–	72,852	–	72,852
Total shareholder funds	**51,768**	**21,084**	**72,252**	**145,104**	**40,255**	**185,359**
Adjustment onto regulatory basis						
Policyholder funds	14,807	–	–	14,807	–	14,807
Adjustments to net assets	(14,765)	(822)	(8,722)	(24,309)	(5,423)	(29,732)
Total available capital resources	**51,810**	**20,262**	**63,530**	**135,602**	**34,832**	**170,434**

	Group life insurance businesses total £000	Other activities UK business £000	Other activities Swedish business £000	Consolidation adjustments £000	Group total £000	Adjustment for dividend £000	Group total IFRS basis £000
Shareholder funds outside long-term insurance funds – retained earnings	112,507	195,551	1,926	(149,091)	160,893	13,357	174,250
Shareholder funds in long-term insurance funds	72,852	–	–	–	72,852	–	72,852
Total shareholder funds	**185,359**	**195,551**	**1,926**	**(149,091)**	**233,745**	**13,357**	**247,102**
Adjustment onto regulatory basis							
Policyholder funds	14,807	–	–	–	14,807		
Adjustments to net assets	(29,732)	(78,872)	–	18,782	(89,822)		
Total available capital resources	**170,434**	**116,679**	**1,926**	**(130,309)**	**158,730**		

(d) Group capital position statement (continued)

As at 31 December 2012	UK life businesses with-profits £000	UK life businesses non-participating £000	UK life businesses shareholder £000	UK life businesses total £000	Swedish life and non-life business total £000	Group life insurance businesses total £000
Shareholder funds outside long-term insurance funds – retained earnings	–	–	49,110	49,110	38,759	87,869
Shareholder funds in long-term insurance funds	44,456	4,917	–	49,373	–	49,373
Total shareholder funds	**44,456**	**4,917**	**49,110**	**98,483**	**38,759**	**137,242**
Adjustment onto regulatory basis						
Policyholder funds	15,351	–	–	15,351	–	15,351
Adjustments to net assets	(7,312)	(839)	(6,330)	(14,481)	(6,277)	(20,758)
Total available capital resources	**52,495**	**4,078**	**42,780**	**99,353**	**32,482**	**131,835**

	Group life insurance businesses total £000	Other activities UK business £000	Other activities Swedish business £000	Consolidation adjustments £000	Group total £000	Adjustment for dividend £000	Group total IFRS basis £000
Shareholder funds outside long-term insurance funds – retained earnings	87,869	178,839	1,649	(112,304)	156,053	12,920	168,973
Shareholder funds in long-term insurance funds	49,373	–	–	–	49,373	–	49,373
Total shareholder funds	**137,242**	**178,839**	**1,649**	**(112,304)**	**205,426**	**12,920**	**218,346**
Adjustment onto regulatory basis							
Policyholder funds	15,351	–	–	–	15,351		
Adjustments to net assets	(20,758)	(62,960)	3	16,217	(67,498)		
Total available capital resources	**131,835**	**115,879**	**1,652**	**(96,087)**	**153,279**		

The tables presented above illustrate Group total available capital resources as measured for the purposes of inclusion in the related regulatory returns. As at 31 December 2013 they are stated after provision of a final dividend of £13.4m and, as at 31 December 2012, after provision of a final dividend of £12.9m, which were approved by the Chesnara plc Board subsequent to the respective year ends. Provision is not made for such dividends on the IFRS basis: accordingly, it is necessary to make adjustment to shareholder funds outside long-term insurance funds as at 31 December 2013, as reflected above, in order to illustrate the relationship with the total shareholder equity included in the consolidated balance sheet prepared on the IFRS basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

32 Capital management (continued)

(d) Group capital position statement (continued)

The following tables set out the principal forms of capital, which comprise (i) total available capital resources for the total UK Life Businesses, the total Swedish Life and Non-life Business and the total Group for regulatory purposes and (ii) total shareholder funds for the Group on the IFRS basis.

Available Capital Resources for Regulatory Purposes Year ended 31 December 2013	CA plc £000	PL £000	Movestic £000	Group £000
Share capital	40,000	21,000	1,227	42,024
Share premium	–	–	–	42,526
Treasury shares	–	–	–	(212)
Other equity contributions	–	–	40,460	–
Capital redemption reserve	–	–	–	50
Foreign exchange translation reserve	–	–	–	7,153
Surplus in long-term business fund	2,020	18,242	–	–
Surplus in with-profits funds	51,810	–	–	51,810
Retained earnings/(accumulated deficit)	2,530	–	(6,855)	15,379
Total	**96,360**	**39,242**	**34,832**	**158,730**

The following tables summarise the movement in the available capital resources of the constituent funds of the life businesses, as determined under the respective regulatory regimes for the year ended 31 December 2013:

UK businesses

Year ended 31 December 2013	Life business non-profits CA plc £000	Life business non-profits PL £000	With profits CA plc £000	Life business shareholder CA plc £000	Life business shareholder PL £000	Total life business £000
At beginning of year	**4,078**	**–**	**52,495**	**42,780**	**–**	**99,353**
Surplus arising in the year	29,442	191	15,759	–	–	45,392
Net profit arising in shareholder fund	–	–	–	(195)	–	(195)
Arising on acquisition of PL	–	4,938	–	–	21,000	25,938
Capitilisation of PL	–	13,113	–	–	–	13,113
Intrafund transfers	16,445	–	(16,445)	–	–	–
Transfer from long-term business fund to shareholder fund	(47,945)	–	–	47,945	–	–
Proposed dividend	–	–	–	(48,000)	–	(48,000)
At end of year	**2,020**	**18,242**	**51,809**	**42,530**	**21,000**	**135,601**

Year ended 31 December 2012	Life business non-profits CA plc £000	With profits CA plc £000	Life business shareholder CA plc £000	Life business shareholder SPI £000	Total life business £000
At beginning of year	**6,533**	**48,924**	**49,370**	**7,000**	**111,827**
Surplus arising in the year	22,545	4,593	–	–	27,138
Net profit arising in shareholder fund	–	–	388	–	388
Intrafund transfers	–	(1,022)	8,022	(7,000)	–
Transfer from long-term business fund to shareholder fund	(25,000)	–	25,000	–	–
Proposed dividend	–	–	(40,000)	–	(40,000)
At end of year	**4,078**	**52,495**	**42,780**	**–**	**99,353**

There were no changes in available capital resources for the year ended 31 December 2013 due to changes in management policy, regulatory changes or external factors. The effect of new business written in the period on available capital resources is not considered to be significant.

(d) Group capital position statement (continued)
Swedish business

Year ended 31 December	2013 Total £000	2012 Total £000
At beginning of year	**32,482**	**29,605**
Profit arising in the year	2,556	8,787
Change in intangible assets: software assets	–	(6,274)
Change in deferred tax	–	(3)
Change in foreign exchange reserve	(206)	367
At end of year	**34,832**	**32,482**

There were no changes in available capital resources for the period ended 31 December 2013 due to changes in management policy, regulatory changes or external factors.

The capital position of the Swedish business is sensitive to changes in market conditions affecting the asset values and changes in the assumptions for calculating the insurance contract liabilities, as described in Note 33.

Group Capital Adequacy
In accordance with the EU Insurance Groups Directive, the Group calculates the excess of the aggregate of regulatory capital employed over the aggregate minimum solvency requirement imposed by local regulators for all of the constituent members of the Group, all of which are based in Europe. The following sets out these calculations after the recognition of final dividends for the respective financial year, but approved by the Board and paid to Group shareholders after the respective dates:

31 December	2013 £m	2012 £m
Total available capital resources (CR)	158.7	153.3
Capital resources requirement		
CA plc	44.1	50.0
PL	25.2	–
Movestic Liv	11.2	11.6
Modernac SA	1.4	1.3
Total (CRR)	81.9	62.9
Group solvency surplus (CR less CRR)	76.8	90.4
Group solvency ratio	194%	244%

The Group and its individually regulated life assurance businesses have complied with all externally and internally imposed capital requirements during the year.

There has been no material change in the Group's management of capital during the period, except that, notwithstanding that there are no formal intragroup funding arrangements in place, the parent company continues to commit to provide any additional capital contributions to support the target capital requirement of Movestic as set out in Section (c) above.

Subject to the regulatory constraints and capital management policy of the Group as set out above, capital resources are available for use elsewhere in the Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

32 Capital management (continued)

(e) Technical provisions net of reassurance – UK businesses

(i) The technical provisions established to determine the regulatory capital resources as set out on page 145 are:

31 December	CA		SPI/SPP		PL	
	2013 £000	2012 £000	2013 £000	2012 £000	2013 £000	2012* £000
Unit-linked						
Insurance contracts	681,389	662,316	766,458	704,833	–	–
Investment contracts	651,724	592,777	45,924	92,170	–	–
Non-unit (sterling)						
Insurance contracts	26,315	20,128	16,662	19,403	10,055	11,790
Investment contracts	7,448	9,627	116	191	–	–
Non-participating						
Insurance contracts	135,835	149,265	9,195	9,900	–	–
Investment contracts	7,638	9,485		–	–	–
With DPF	–	–	310,429	340,848	–	–
Total	**1,510,349**	**1,443,598**	**1,148,784**	**1,167,345**	**10,055**	**11,790**

*The 2012 technical provisions for PL have been provided for illustrative purposes only.

(ii) Process used to determine assumptions underlying the calculation of technical provisions.

The process used to determine the assumptions underlying the calculation of technical provisions, which are checked to ensure that they are consistent with observed market prices or other published information, is intended to result in conservative estimates of the most likely, or expected, outcome. The assumptions which are considered include the expected number and timing of deaths, other claims and investment returns over the period of risk exposure. A reasonable allowance is made for the level of uncertainty within the contracts.

(iii) The basis for establishing technical provisions is:

The technical provision for S&P with-profits contracts is based on the guaranteed minimum benefits and is calculated on a gross premium basis, by subtracting the present value of future premiums from the present value of future benefits payable under the policy, until it ceases at maturity, or death if earlier. The gross premium method makes explicit allowance for future policy maintenance costs. If the net present value of the future discounted cash flows is positive, no asset is recognised. Provision is not made for future bonuses as all bonuses are terminal bonuses.

For those classes of CA non-linked and unit-linked business where policyholders participate in profits, the liability is wholly reinsured to Guardian. When performing the gross liability adequacy test allowance is made for expected future bonuses paid by Guardian. This is based on the realistic liabilities of the underlying policies reinsured, as provided to CA by Guardian.

For all other classes of unit linked and quasi-linked business, the technical provision consists of a provision equal to the value of the matching unit-linked assets plus an additional reserve calculated on a gross premium basis, by subtracting the present value of future premiums from the present value of future benefits payable under the policy, until it ceases at maturity, or death if earlier. The gross premium method makes explicit allowance for future policy maintenance costs. If the net present value of the future discounted cash flows is positive, no asset is recognised.

For immediate annuities in payment the technical provision is calculated as the discounted value of the expected future annuity payments under the policies, allowing for mortality, interest rates and expenses.

For certain group business within PL the technical provisions are assessed on an unearned premium method considered appropriate for the nature and scale of the liabilities. For the remainder of the PL business, the technical provisions are calculated on a gross premiums basis, by subtracting the present value of future premiums from the present value of future benefits payable under the policy, until it ceases at maturity, or lapse or death if earlier. The gross premiums method makes explicit allowance for future policy maintenance costs. If the net present value of future discounted cash flows is positive no asset is recognised.

For all other classes of non-linked business the technical provision is calculated on a net premium basis, being the level of premium consistent with a premium stream, the discounted value of which, at the outset of the policy, would be sufficient to cover exactly the discounted value of the original guaranteed benefits at maturity, or at death if earlier, on the valuation basis. The provision is then calculated by subtracting the present value of future net premiums from the present value of the benefits guaranteed at maturity, or death if earlier, as a result of events up to the balance sheet date. Negative provisions do not arise under the net premium method, which makes no allowances for voluntary discontinuances by policyholders, and which only implicitly allows for future policy maintenance costs.

(iv) The principal assumptions underlying the calculation of the technical provisions are:

Mortality
A base mortality table is selected which is most appropriate for each type of contract taking into account rates charged to CA by reinsurers. The mortality rates reflected in these tables are periodically adjusted, allowing for emerging experience and changes in reinsurer rates.

Morbidity
Morbidity tables are derived based on reinsurer tables. These are periodically adjusted to take into account emerging experience where appropriate.

Persistency
In general, no allowance is made for lapses or surrenders within the valuation of insurance contract liabilities, which is a prudent assumption.

(e) Technical provisions net of reassurance – UK businesses (continued)

For S&P unit-linked business, when assessing additional reserves for expenses and mortality risk, allowance has been made for lapses at a prudent level of 75% of the expected level as indicated by recent experience, the rates used being:

Rate of lapse 31 December	2013		2012	
	SPI	SPP	SPI	SPP
Assurances:				
Regular premium plans	3.375%	2.625%	3.000%	2.625%
Single premium contracts	3.375%	3.188%	3.375%	3.375%
Linked TIC*	–	5.000%	–	7.50%

*Trustee Investment Contract, a unit-linked contract ('TIC').

For PL the following lapse assumptions have been adopted when calculating technical provisions:

- For critical illness policies a rate of 4.5% per annum is used when net cash flows are negative and a low lapse rate is prudent, or 15.5% per annum otherwise.
- For all other policies excluding PPI and the whole life guaranteed acceptance plan product, a rate of 1.5% per annum is used when net cash flows are negative and a low lapse rate is prudent, or 12.5% per annum otherwise.
- For PPI and the whole life guaranteed acceptance plan products, no lapses are assumed.

Discount rates

CA uses appropriate rates of interest, for different product types, in discounting projected liabilities. As at 31 December 2013 for the material product types, these lay between 2.10% and 3.50% (31 December 2012: between 1.40% and 2.75%).

The rates of interest shown above have been set after consideration of the risk of default on non-government bonds by applying the following adjustments to the earned yield:

(i) Risk reduction of 0.1% for supranational issuers such as the European Investment Bank;

(ii) For other issuers, a portion of the excess yield above that available on government backed bonds, where the portion varies by credit rating; and

(iii) An overall maximum margin over the equivalent term government fixed interest security of 1.5%.

Credit rating	Aaa	Aa	A	Baa	Ba	B	Caa+
Reduction	25%	40%	45%	50%	55%	65%	80%

For many of the life insurance products the interest rate risk is managed through asset/liability management strategies that seek to match the interest rate sensitivity of the assets to that of the underlying liabilities. The overall objective of these strategies is to limit the net change in value of assets and liabilities arising from interest rate movements.

Technical provisions for with-profits contracts are particularly sensitive to the interest rate used when discounting due to the existence of investment guarantees.

Renewal expenses and inflation

The renewal expenses assumed are based on the charges made to CA by its two third party insurance administration services providers, with appropriate margins. These are assumed to inflate at a mix of current inflation rates in the UK, being the Retail Price Index and the National Average Earnings Index. Explicit allowance is also made for those Governance expenses which are charged to the long-term funds.

Taxation

It has been assumed that current tax legislation and tax rates will not change.

The sensitivities of technical provisions and of components of capital to changes in assumptions are materially the same as those detailed in Note 33.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

32 Capital management (continued)

(f) Valuation of options and guarantees – UK businesses

Deterministically-valued options and guarantees

Timed Investment Funds

Certain investment funds, the 'Timed Investment Funds', carry a guarantee that the price at maturity date or death will not be less than the highest price attained between commencement and contract cessation. The cost of the guarantee can be managed by changing the investment policy adopted by each fund.

In respect of this guarantee:

(i) a monthly charge of 1⁄48% of the fund value is made; and

(ii) investment conditions were such as to require the establishment of a reserve of £390,000 as at 31 December 2013 (31 December 2012: £327,000).

The reserve for a given fund is derived as the discounted exposure at fund maturity date, the exposure being the difference between the guaranteed Timed Investment Fund value and the projected fund maturity value, with the latter projected value being derived assuming an immediate fall in value of equities within the fund of 25% and allowing for future investment returns, including presumed future equity investment return of 3.70% per annum.

Guaranteed Growth Fund

The Guaranteed Growth Fund (GGF) is a deposit-based contract which provides a return to policyholders that is linked to the average residential mortgage rate. However, the assets backing the contract are largely held as cash on deposit. There is, therefore, likely to be a shortfall between the return given to policyholders and the return earned on assets, and the value of this shortfall is reserved for.

Reserves for this product comprise a 'unit' reserve of the current value of the benefits held and a non-unit reserve for expenses.

The underlying fund at 31 December 2013 was £5.7m (31 December 2012: £2.0m). 606 policies invested in the fund (31 December 2012: 658), of which 58 (31 December 2012: 67) were paying premiums (for a total of approximately £17,000 per annum (31 December 2012: £23,000)).

For the valuation of contract liabilities the following are projected for each future year: – the benefit outgo from the fund;

- the investment return from the assets backing the fund; and
- the difference between these items.

These differences are then discounted and summed to establish the GGF loss reserve.

The following assumptions are used for calculating the loss reserve:

Rate of growth of liability:	3.62% pa
Rate of return on cash:	0.4% pa
Discount rate:	1.2% pa
Retirement age:	90% of business with policyholders retiring at age 65 10% of business with policyholders retiring at age 70
Terminations before retirement:	3% pa

The reserve for the guarantee as at 31 December 2013 was £0.7m (31 December 2012: £0.5m).

Deferral of retirement ages

Policyholders with a Personal Retirement Account and Guaranteed Plus Retirement Plan may defer their retirement age on terms that may be beneficial to the policyholder. The cost of policyholders exercising this benefit is assessed using a prudent assumption as to the level of take-up of the option and deferral to age 75. The reserve for this option as at 31 December 2013 was £6.1m (31 December 2012: £7.1m).

Increase of premiums on Personal Retirement Account

Policyholders with a Personal Retirement Account may increase their regular premium contribution on terms that can be beneficial to the policyholder. The cost of policyholders exercising this benefit is assessed using a prudent assumption as to the level of take-up of the option. The reserve for this option as at 31 December 2013 was £0.2m (31 December 2012: £0.2m).

Insurability options

Policyholders with certain contracts have the right to increase their sum assured without underwriting, in certain circumstances. The reserve for this option as at 31 December 2013 was £0.3m (31 December 2012: £0.3m).

Guaranteed annuity options

A limited number of pension plans offer guaranteed annuity options at retirement. The cost of this option is assessed assuming a prudent assessment of the take-up of the option and of the cost. The reserve for this option as at 31 December 2013 is £0.4m (31 December 2012: £0.5m).

(g) Management of risk

The Group's approach to the management of risk which may have an impact on the measurement of capital resources and requirements, as measured on a regulatory basis, is set out in Notes 5 and 6 to these financial statements.

33 Insurance contract provisions

(a) Analysis of insurance contract provisions by operating segment

31 December		2013			2012	
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
CA	1,086,369	234,011	852,358	1,058,070	226,649	831,421
S&P	1,102,369	6,167	1,096,202	1,080,427	5,873	1,074,554
PL	103,448	93,393	10,055	–	–	–
Movestic	69,877	46,323	23,554	68,581	46,170	22,411
Total insurance contract provisions	**2,362,063**	**379,894**	**1,982,169**	**2,207,078**	**278,692**	**1,928,386**
Current	215,436	35,913	179,523	408,702	18,551	390,151
Non-current	2,146,627	343,981	1,802,646	1,798,376	260,141	1,538,235
Total	**2,362,063**	**379,894**	**1,982,169**	**2,207,078**	**278,692**	**1,928,386**

(b) Analysis of movement in insurance contract provisions

Year ended 31 December		2013			2012	
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Balance at 1 January	**2,207,078**	**278,692**	**1,928,386**	**2,190,939**	**263,792**	**1,927,147**
Arising on business combination	103,918	93,826	10,092	–	–	–
Premiums received	67,072	9,468	57,604	75,575	10,845	64,730
Fees deducted	(24,174)	(2,751)	(21,423)	(27,467)	(3,140)	(24,327)
Reserves released in respect of benefits paid	(230,963)	(27,862)	(203,101)	(233,017)	(18,356)	(214,661)
Movements in provisions for contracts sold – Movestic						
– in current year	22,521	12,444	10,077	25,363	14,992	10,371
– in prior years	(12,546)	(5,484)	(7,062)	(14,972)	(7,611)	(7,361)
Investment return	256,963	13,598	243,365	159,877	7,983	151,894
Other movements	(27,806)	7,963	(35,769)	30,780	10,187	20,593
Balance at 31 December	**2,362,063**	**379,894**	**1,982,169**	**2,207,078**	**278,692**	**1,928,386**

(c) Process, basis and assumptions for establishing insurance contract provisions

The process, basis and assumptions for establishing insurance contract provisions for the UK businesses are materially the same as those stated in Note 32 (e) (ii), (iii) and (iv) for establishing technical provisions, except as set out in the following.

Provisions for S&P contracts with discretionary participation features ('DPF') provide for the present value of projected payments to policyholders based on guaranteed minimum investment returns, mainly at 5 per cent per annum. When the insurance contract provisions established on this basis are greater than the associated policyholder asset shares, a shareholder charge for the cost of guarantees arises.

The actual cost to shareholders depends principally on the future investment performance of the associated policyholders' assets and on the rate of discontinuance of policies prior to maturity. During 2012 the estimated cost of these guarantees to shareholders was changed from being based on a simplification of the method used for statutory solvency purposes to a method that is based on market consistent evaluation of the cost, the methodology of which is set out on pages 182 to 185 in the EEV Supplementary Information following and is taken as a constant margin of 10% above the amount so determined, in order to allow for an appropriate level of prudence (the 'market-consistent' method).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

33 Insurance contract provisions (continued)

The following sets out the cumulative charge to shareholders for the cost of guarantees on these bases:

Year ended 31 December	2013 £000s	2012 £000s
At beginning of the year	**46,310**	**45,910**
(Credit)/charge to income	(22,990)	400
At the end of year	**23,320**	**46,310**

Swedish business (Movestic)

Group Contracts are sold on an annual basis and the Individual Contracts include an option for Movestic to increase the premium on an ongoing basis. Therefore, for both Group and Individual Contracts, Movestic adopts a reserving approach that is similar to that of a non-life insurance business, with claim reserves projected using an estimated loss ratio with reference to previous loss development for earlier years.

The insurance contract provisions comprise unearned premium provisions, outstanding claims and associated reinsurance recoveries. Except for the income protection and the waiver of premium benefits within the Individual Contracts, provisions for the insurance contracts are not discounted because of the short-term nature of the liabilities, which are generally paid by the fourth year of development for a single accident year. Income protection and waiver of premium contracts are discounted at a rate equivalent to a high quality (i.e. AA rated) corporate bond.

(d) Assumptions used in establishing insurance contract provisions

The assumptions used in establishing insurance contract provisions for the UK businesses are materially the same as those set out in Note 32(e) (iv) for establishing technical provisions.

Swedish business (Movestic)

Unearned premiums

Unearned premiums represent a proportion of the premium relating to policies that expire after the balance sheet date. Unearned premiums are calculated automatically by the underwriting system and are released to income on a straight-line basis over the period of the policy.

Outstanding claims

Outstanding claims include notified claims, claims incurred as at the balance sheet date but not reported and an estimate of the cost of handling the claims.

The key risk in respect of notified claims is that they are paid or handled inappropriately (for example invalid or fraudulent claims are paid). Management information is reviewed on a regular basis to identify unusual trends in the payment of claims.

The estimation of claims incurred but not reported ('IBNR') is generally subject to a greater degree of uncertainty than the estimation of costs of settling claims already notified to Movestic, where more information about the claim event is generally available. In calculating the estimated cost of claims which have not been notified, Movestic uses a variety of estimation techniques, generally based upon statistical analyses of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience.

The most common methods that are used are the chain ladder method and the Bornhuetter-Ferguson method. Chain ladder methods involve the analysis of historical claims development factors and the selection of estimated development factors based on this historical pattern. The selected factors are applied to cumulative claims data for each accident year that is not fully developed to provide an estimated ultimate claims cost. The Bornhuetter-Ferguson method uses a combination of an initial estimate of the expected loss ratio and an estimate based on observed claims experience. The two estimates are combined using a formula that gives more weight to the experience-based estimate as time passes.

(d) Assumptions used in establishing insurance contract provisions (continued)

The use of different approaches assists in giving greater understanding of the trends inherent in the data being projected and also assists in setting the range of possible outcomes. The most appropriate estimation technique is selected taking into account the characteristics of the policies sold. Where deemed appropriate, an allowance is made for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims. Although claim reserves are considered reasonable, on the basis of information available to Movestic, the ultimate liabilities will vary as a result of subsequent information and events.

Income protection and waiver of premium benefits within Individual Contracts

For reported claims, the liabilities are reviewed on a case by case basis. A discounted cash flow model is used to determine the liabilities and the key factors used are:

- the probability of 'recovery' (i.e. return to work). The recovery rates depend on age, sex and length of time the claimant has been claiming the benefits;
- the mortality rate; and
- the discount rate.

For unreported claims, the claims development table is used. The development of insurance liabilities provides a measure of Movestic's ability to estimate the ultimate value of claims. The top half of the table below illustrates how Movestic's estimate of total claims outstanding for each accident year has changed at successive year-ends. The bottom half of the table reconciles the cumulative claims to the amount appearing in the balance sheet. An accident-year basis is considered to be the most appropriate for the business written by Movestic. The information is presented on both a gross and net of reinsurance basis.

Analysis of claims development – gross

	2008 £000	2009 £000	2010 £000	2011 £000	2012 £000	2013 £000
Estimate of ultimates						
End of accident year	18,400	18,350	45,785	28,198	29,172	30,573
One year later	15,338	13,792	37,610	18,241	19,571	–
Two years later	13,988	13,754	36,210	16,609	–	–
Three years later	11,750	13,695	34,524	–	–	–
Four years later	11,332	13,226	–	–	–	–
Five years later	11,767	–	–	–	–	–
Current estimate of ultimate claims	11,767	13,226	34,524	16,609	19,571	30,573
Cumulative payments	(9,842)	(9,565)	(16,136)	(9,663)	(10,357)	(8,906)
In balance sheet	1,925	3,661	18,388	6,946	9,214	21,667
Provision for prior years						4,285
Liability in balance sheet						66,086

Analysis of claims development – net

	2008 £000	2009 £000	2010 £000	2011 £000	2012 £000	2013 £000
Estimate of ultimates						
End of accident year	2,586	2,893	14,469	11,836	10,845	12,184
One year later	2,334	2,097	10,285	6,062	5,637	–
Two years later	2,123	2,427	9,806	4,566	–	–
Three years later	1,704	2,430	8,955	–	–	–
Four years later	1,697	2,321	–	–	–	–
Five years later	1,776	–	–	–	–	–
Current estimate of ultimate claims	1,776	2,321	8,955	4,566	5,637	12,184
Cumulative payments	(1,428)	(1,631)	(3,765)	(2,554)	(2,642)	(2,490)
In balance sheet	348	690	5,190	2,012	2,995	9,694
Provision for prior years						1,046
Liability in balance sheet						21,659

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

33 Insurance contract provisions (continued)

(e) Sensitivity to changes in assumptions

UK businesses (CA, S&P and PL)

Assumptions are adjusted for changes in mortality, investment return, policy maintenance expenses and expense inflation to reflect anticipated changes in market conditions and market experience and price inflation.

CA, S&P and PL re-run their valuation models on various bases. An analysis of sensitivity around various scenarios provides an indication of the sensitivity of the estimates to changes in assumptions in respect of its life assurance contracts. The table presented below demonstrates the sensitivity of assets and insured liability estimates to particular movements in assumptions used in the estimation process. Certain variables can be expected to impact on life assurance liabilities more than others, and consequently a greater degree of sensitivity to these variables may be expected.

Impact on reported net of tax profits and equity to changes in key variables:

	Change in variable %	Change in net of tax profits and equity 2013 £m	Change in net of tax profits and equity 2012 £m
CA business			
Investment return	+1	(3.7)	(3.0)
Investment return	-1	2.7	(1.0)
Mortality/morbidity	+10	2.5	2.4
Mortality alone	+10	3.4	3.5
Morbidity alone	+10	(0.9)	(1.1)
Policy maintenance expenses	+10	(1.3)	(1.7)
S&P business			
Investment return	+1	11.5	16.1
Investment return	-1	(12.1)	(17.6)
Mortality	+10	0.2	0.4
Policy maintenance expenses	+10	(2.0)	(1.8)
PL business			
Investment return	+1	–	N/A
Investment return	-1	(0.2)	N/A
Mortality/morbidity	+10	(3.9)	N/A
Mortality alone	+10	(2.0)	N/A
Morbidity alone	+10	(1.9)	N/A
Policy maintenance expenses	+10	(0.5)	N/A

The above sensitivities are calculated as an expected impact on IFRS-based profits, net of reinsurance and tax and the analysis has been prepared for a change in the stated variable, with all other assumptions remaining constant.

The sensitivities to the changes in investment returns are calculated taking into account the consequential changes to valuation assumptions.

The sensitivities to mortality and morbidity (critical illness) rates shown above are calculated on the assumption that there would be no consequential change in rates to policyholders. In practice, Group policy is to pass costs on to policyholders where it is contractually permitted and where it considers that the impact of the change is significant.

The main expense risk is that of unforeseen changes to third party administration expenses: the impact shown above quantifies a 10% increase in those expenses.

(e) Sensitivity to changes in assumptions (continued)

Swedish business (Movestic)

The key sensitivities in the measurement of the Group and Individual Contracts insurance claim reserves within Movestic are a movement in the loss ratio applied to earned premium and the foreign exchange risk arising on business written in Norway. In addition, for the income protection and the waiver of premium benefits within the Individual Contracts, the claims reserves are impacted by the discount rate used. The impact of these sensitivities is shown below:

	Pre-tax profit 2013 £m	Pre-tax profit 2012 £m	Shareholders' equity 2013 £m	Shareholders' equity 2012 £m
5% increase in loss ratio				
Gross before reinsurance	(2.0)	(2.0)	(1.5)	(1.5)
Net after reinsurance	(1.1)	(1.3)	(0.8)	(1.0)
5% decrease in loss ratio				
Gross before reinsurance	2.0	2.0	1.5	1.5
Net after reinsurance	1.1	1.3	0.8	1.0
10% increase in the Norwegian Krone				
Gross before reinsurance	(0.4)	(0.2)	(0.3)	(0.2)
Net after reinsurance	(0.3)	(0.0)	(0.3)	(0.0)
10% decrease in the Norwegian Krone				
Gross before reinsurance	0.4	0.2	0.3	0.2
Net after reinsurance	0.3	0.0	0.3	0.0
1% increase in discount rate				
Gross before reinsurance	1.2	2.0	0.9	1.5
Net after reinsurance	0.6	0.8	0.4	0.6
1% decrease in discount rate				
Gross before reinsurance	(1.4)	(2.4)	(1.1)	(1.8)
Net after reinsurance	(0.3)	(0.9)	(0.2)	(0.7)

34 Investment contracts at fair value through income and amounts deposited with reinsurer

Analysis by operating segment

31 December	2013 Investment contract liability £000	2013 Amount deposited with reinsurer £000	2013 Net £000	2012 Investment contract liability £000	2012 Amount deposited with reinsurer £000	2012 Net £000
CA	689,359	34,293	655,066	629,882	30,245	599,637
S&P	45,924	–	45,924	92,170	–	92,170
Movestic	1,548,120	–	1,548,120	1,300,262	–	1,300,262
Total	**2,283,403**	**34,293**	**2,249,110**	**2,022,314**	**30,245**	**1,992,069**
Current	76,826	740	76,086	568,222	523	567,699
Non-current	2,206,577	33,553	2,173,024	1,454,092	29,722	1,424,370
Total	**2,283,403**	**34,293**	**2,249,110**	**2,022,314**	**30,245**	**1,992,069**

The fair values of the Groups' investment contract liabilities have been disclosed according to a three-level valuation hierarchy in Note 27.

The table above does not include any analysis with regards to Protection Life as all of its products are classified as insurance contracts under IFRS.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

35 Liabilities relating to policyholders' funds held by the Group

Unit-linked 31 December	2013 £000	2012 £000
Balance at 1 January	**61,171**	**49,080**
Deposits received	66,000	17,869
Fees deducted from account balances	(727)	(277)
Investment yield	11,002	3,314
Foreign exchange translation difference	(3,127)	833
Other movements	(4,082)	(9,648)
Balance at 31 December	**130,237**	**61,171**
Current	14,676	21,356
Non-current	115,561	39,815
Total	**130,237**	**61,171**

The fair values of the 'Liabilities relating to Policyholders' funds held by the Group' are determined according to a three-level valuation hierarchy, which is explained in Note 27.

The fair value of these liabilities is based on the aggregation of prices quoted in active markets of their associated assets (Level 1), as disclosed in Note 27.

36 Borrowings

Group 31 December	2013 £000	2012 £000
Bank loan	73,040	29,662
Amount due in relation to financial reinsurance	21,337	18,662
Total	**94,377**	**48,324**
Current	13,967	12,218
Non-current	80,410	36,106
Total	**94,377**	**48,324**

Company **31 December**	**2013** **£000**	**2012** **£000**
Bank loan	**73,040**	**29,662**
Current	8,897	7,844
Non-current	64,143	21,818
Total	**73,040**	**29,662**

The bank loan subsisting at 31 December 2013, comprises the following:

- on 7 October 2013 tranche one of a new facility was drawn down, amounting to £30.0m. This facility is unsecured and is repayable in five increasing annual instalments on the anniversary of the draw down date. The outstanding principal on the loan bears interest at a rate of 2.25 percentage points above the London Inter-Bank Offer Rate and is repayable over a period which varies between one and six months at the option of the borrower.
- on 27 November 2013 tranche two of the new loan facility was drawn down, amounting to £31.0m. As with tranche one, this facility is unsecured and is repayable in five increasing annual instalments on the anniversary of the draw down date. The outstanding principal on the loan bears interest at a rate of 2.25 percentage points above the London Inter-Bank Offer Rate and is repayable over a period which varies between one and six months at the option of the borrower.
- on 27 November 2013 a short-term loan of £12.8m was drawn down. This is repayable in full on 27 May 2015. The outstanding principal on the loan bears interest at a rate of 2.75 percentage points above the London Inter-Bank Offer Rate.

The fair value of the bank loan at 31 December 2013 was £73,800,000 (31 December 2012: £30,000,000).

The fair value of amounts due in relation to financial reinsurance was £21,657,269 (31 December 2012: £20,197,549). The fair value of other borrowings is not materially different from their carrying value.

Bank loans are presented net of unamortised arrangement fees. Arrangement fees are recognised in profit or loss using the effective interest rate method.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

37 Other provisions

Group

	MECR £000	Other complaints redress £000	Onerous contracts £000	Unit pricing redress £000	Other £000	Total £000
Balance at 1 January 2012	**69**	**202**	**2,090**	**450**	**–**	**2,811**
Provisions made during the year	40	2	2,504	–	712	3,258
Provisions used during the year	(28)	(1)	(263)	(1)	14	(279)
Provisions reversed during the year	–	–	(184)	(445)	–	(629)
Balance at 31 December 2012	**81**	**203**	**4,147**	**4**	**726**	**5,161**
Provisions made during the year	3	2	33	(1)	2,000	2,037
Provisions used during the year	(6)	–	(455)	–	(886)	(1,347)
Provisions reversed during the year	(63)	(198)	(238)	–	(4)	(503)
Balance at 31 December 2013	**15**	**7**	**3,487**	**3**	**1,836**	**5,348**
31 December 2012						
Current	81	203	496	4	726	1,510
Non-current	–	–	3,651	–	–	3,651
Total	**81**	**203**	**4,147**	**4**	**726**	**5,161**
31 December 2013						
Current	15	7	691	3	1,836	2,552
Non-current	–	–	2,796	–	–	2,796
Total	**15**	**7**	**3,487**	**3**	**1,836**	**5,348**

The reversal of provisions during the year was credited to Other Operating Income as disclosed in Note 12.

Company

	Onerous contracts £000
Balance at 1 January 2012	**1,500**
Provisions made during the year	2,463
Provisions used during the year	(159)
Balance at 31 December 2012	**3,804**
Provisions reversed during the year	(94)
Provisions used during the year	(404)
Balance at 31 December 2013	**3,306**
31 December 2012	
Current	399
Non-current	3,405
Total	**3,804**
31 December 2013	
Current	591
Non-current	2,715
Total	**3,306**

(a) Mortgage Endowment Complaints Redress (MECR)

Insurance contract provisions include a mortgage endowment complaints reserve of £3.01m, in respect of the estimate of future redress for future claims by customers in respect of past misselling of mortgage endowment policies.

As part of the redress process if the complaint is upheld an offer of redress is made to the customer where a loss has occurred. These offers are classified as payables for the first 6 months after they are made, subsequent to which they are reclassified as provisions, as the customer loses the right of redress at the level offered, but continues to have a right to enforce a claim, which the Group has the right to reassess. The provision is established at the original offer level.

(b) Other complaints redress

Offers of redress on complaints other than mortgage endowment related are classified in a manner similar to that detailed for MECR above.

(c) Onerous contracts

The Group and Company have a number of onerous operating lease contracts that have been entered into historically, whose activity and current status is described in Note 50 Operating leases. Given the terms of the contracts the Group and company have created onerous contract provisions for anticipated future net costs. Over the terms of the contracts these provisions take account of the contract terms, future payments and future mitigating income from sublets, contract by contract, to create a view as to the Group's and Company's exposure.

These provisions comprise three components: provision for vacant properties, provision for properties due to become empty at the end of their subleases, and provision for future under-recoveries of costs on subleases entered into.

Of the closing provision balance, £3,306,000, relates to the potential cost of vacant space within the Harbour House Head Office in Preston. The Company has a lease arrangement until mid-2019 for the entire building although it only occupies a small proportion. The majority of the building is available for sub-let. The additional provision represents the future contractual costs not expected to be covered by sub-let income when existing tenants vacate the building. During 2012 Chesnara plc received notice from tenants of their intention to vacate Harbour House. In recognition of this, and in light of the excess commercial property capacity in the market, the estimated level of future sub let income was reduced and the provision as at 31 December 2012 was increased accordingly. The critical factor to which the value is sensitive is the assumed level of re-letting income.

(d) Unit pricing redress

A data error in the indexation of the costs of underlying financial assets in certain of the unit-linked funds was identified during 2007. As a result, the amount of capital gains chargeable to tax had been overestimated for unit pricing purposes and greater deductions were made from these funds than would otherwise have been the case. A provision of £2,994,000 was established at 31 December 2007 to cover the estimated cost of redress and the administration costs of performing the review. Associated recoveries from third parties were established at £494,000 as at the same date and these were included in 'Insurance and other receivables' as at 31 December 2007.

The provision established at 31 December 2007 was estimated insofar as it was not based on specific individual calculations for each policyholder, but was established on the basis of generic data relating to the amount of payments to policyholders who exited from the funds in specific periods, of the unit prices ruling in those periods and of an estimate of the extent of the pricing error pertaining to those periods. Subsequently, a revised estimate was established at £2,794,000 based on specific policy-by-policy data, which by 31 December 2011 had reduced to £450,000 as compensation was paid to policyholders. During 2012 the majority of outstanding amounts owed to policyholders, for which the respective policyholders could not be traced, were re-invested into unit-linked funds for the benefit of all remaining policyholders, and only a small balancing residual provision of £3,000 as at 31 December 2013 continues to be held until all of the associated administration procedures are completed.

(e) Sharesave Plan

A Sharesave Plan was launched during October 2011. The level of contributions combined with the closing share price, result in an immaterial level of company liability and hence no provision has been raised.

(f) Other

One of the conditions of the acquisition of Protection Life was to migrate the accounting and policy administration processes from the Direct Line Group to one of our outsource providers. As a result of this requirement a provision of £2.0m was raised during the year, representing Management's best estimate of the costs that will be incurred to fulfill this obligation. £0.37m of this provision has been utilised during 2013.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

38 Deferred tax assets and liabilities

Deferred tax assets and liabilities comprise:

Deferred tax assets 31 December	2013 £000	2012 £000
Net deferred tax assets:		
CA, S&P, PL and Other Group Activities	–	2,295
Movestic	–	–
Total	**–**	**2,295**
Current	–	–
Non-current	–	2,295
Total	**–**	**2,295**

Deferred tax liabilities 31 December	2013 £000	2012 £000
Net deferred tax liabilities		
CA, S&P, PL and Other Group Activities	(9,502)	(4,786)
Movestic	(1,505)	(1,108)
Total	**(11,007)**	**(5,894)**
Current	(1,241)	(1,048)
Non-current	(9,766)	(4,846)
Total	**(11,007)**	**(5,894)**

CA, S&P, PL and Other Group Activities

(a) Recognised deferred tax assets and liabilities

31 December	2012 Assets/ (liabilities) £000	(Charge)/ credit in year £000	Arising on business combinations	2013 Assets/ (liabilities) £000
Profit arising on transition to new tax regime	(2,636)	264	–	(2,372)
Deferred acquisition costs	(1,065)	269	–	(796)
Deferred income	1,889	(437)	–	1,452
Acquired value in force	(4,857)	1,113	(4,042)	(7,786)
Property, plant and equipment	(39)	14	–	(25)
Tax losses on pensions business	4,178	(4,178)	–	–
Unrealised and deferred investment gains	(4,655)	338	–	(4,317)
Excess expenses of management	4,655	(338)	–	4,317
Other	39	(14)	–	25
Total	**(2,491)**	**(2,969)**	**(4,042)**	**(9,502)**
Comprising:-				
Net deferred tax assets	2,295	(2,295)	–	–
Net deferred tax liabilities	(4,786)	(674)	(4,042)	(9,502)
Total	**(2,491)**	**(2,969)**	**(4,402)**	**(9,502)**

31 December	2011 Assets/ (liabilities) £000	(Charge)/ credit in year £000	2012 Assets/ (liabilities) £000
Profit arising on transition to new tax regime	–	(2,636)	(2,636)
Deferred acquisition costs	(1,319)	254	(1,065)
Deferred income	2,322	(433)	1,889
Acquired value in force	(6,159)	1,302	(4,857)
Property, plant and equipment	(79)	40	(39)
Tax losses on pensions business	–	4,178	4,178
Unrealised and deferred investment gains	(4,682)	27	(4,655)
Excess expenses of management	–	4,655	4,655
Insurance contract provisions	(4,706)	4,706	–
Other	–	39	39
Total	**(14,623)**	**12,132**	**(2,491)**
Comprising:-			
Net deferred tax assets	–	2,295	2,295
Net deferred tax liabilities	(14,623)	9,837	(4,786)
Total	**(14,623)**	**12,132**	**(2,491)**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

38 Deferred tax assets and liabilities (continued)

CA, S&P, PL and Other Group Activities (continued)

(a) Recognised deferred tax assets and liabilities (continued)

Note (i) The deferred tax (charge)/credit to the Consolidated Statement of Comprehensive Income for the year is classified as follows:

Year ended 31 December	2013 £000	2012 £000
Income tax (charge)/credit before exceptional item	(2,969)	7,354
Exceptional item (see Note 8 on page 126)	–	4,778
Total	**(2,969)**	**12,132**

A new regime for the taxation of life assurance companies in the UK was introduced with effect from 1 January 2013. The new regime bases the taxable trading profit on IFRS profits rather than on PRA return surplus generated as under the previous rules and also treats pension business separately from life assurance business. The 2012 tax charge reflected a significant deferred tax credit as a result of this change, as the pension losses in the UK life company were ascribed value for the first time in 2012. In addition, as part of the transition to the new regime, accumulated historical profits as at 31 December 2012 were compared between the two bases and the taxable difference is being charged over ten years. This transitional adjustment created a deferred tax charge during 2012, partially offsetting the pension related recovery noted here. In 2013, the deferred tax asset relating to pension loses has been fully utilised creating a deferred tax charge in the year.

(b) Items for which no deferred tax asset is recognised

31 December	2013 £000	2012 £000
BLAGAB transitional amounts	4,286	4,837
Unrelieved expenses	35,735	58,685
Realised and unrealised investment losses	4,350	4,235
Total	**44,371**	**67,757**

A deferred tax asset has not been recognised in respect of unrelieved expenses, because it is not probable that there will be a sufficient level of taxable income arising from income and gains on financial assets, so that the Group can utilise the benefits therefrom.

Movestic

(a) Recognised deferred tax assets and liabilities

31 December	2012 Assets/ (liabilities) £000	(Charge)/ credit in year £000	Foreign exchange translation difference £000	2013 Assets/ (liabilities) £000
Intangible assets				
Fair value adjustment on acquisition	(601)	45	(16)	(572)
Corporation tax recoverable	91	(94)	3	–
Equity accounting for associate	(601)	(371)	18	(954)
Property, plant and equipment	3	(1)	–	2
Total	**(1,108)**	**(421)**	**5**	**(1,524)**
Comprising:				
Net deferred tax assets	94	(95)	3	2
Net deferred tax liabilities	(1,202)	(326)	2	(1,526)
Total	**(1,108)**	**(421)**	**5**	**1,524**

31 December	2011 Assets/ (liabilities) £000	(Charge)/ credit in year £000	Foreign exchange translation difference £000	2012 Assets/ (liabilities) £000
Intangible assets				
Fair value adjustment on acquisition	(561)	(31)	(9)	(601)
Corporation tax recoverable	–	90	1	91
Equity accounting for associate	(222)	(368)	(11)	(601)
Property, plant and equipment	16	(14)	1	3
Total	**(767)**	**(323)**	**(18)**	**(1,108)**
Comprising:				
Net deferred tax assets	16	76	2	94
Net deferred tax liabilities	(783)	(399)	(20)	(1,202)
Total	**(767)**	**(323)**	**(18)**	**(1,108)**

(b) Unrecognised deferred tax assets

31 December	2013 £000	2012 £000
Corporation tax recoverable – not recognised	758	822
Total	**758**	**822**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

39 Reinsurance payables

Payable to reinsurers
31 December

	2013 £000	2012 £000
Payables in respect of insurance contracts	10,860	15,914
Payables in respect of investment contracts	21	22
Reinsurers' share of deferred acquisition costs and claims deposits	658	674
Total	**11,539**	**16,610**
Current	10,491	15,154
Non-current	1,048	1,456
Total	**11,539**	**16,610**

The carrying value of payables to reinsurers is a reasonable approximation of fair value.

40 Payables related to direct insurance and investment contracts

31 December

	2013			2012		
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Accrued claims	40,971	11,399	29,572	32,490	4,489	28,001
Intermediaries' liabilities	2,301	–	2,301	1,447	–	1,447
Policyholder premium liabilities	2,481	–	2,481	2,289	–	2,289
Other	1,384	–	1,384	2,668	–	2,668
Total	**47,137**	**11,399**	**35,738**	**38,894**	**4,489**	**34,405**
Current	47,137	11,399	35,738	38,894	4,489	34,405
Non-current	–	–	–	–	–	–
Total	**47,137**	**11,399**	**35,738**	**38,894**	**4,489**	**34,405**

The carrying value of payables related to the direct insurance and investment contracts is a reasonable approximation of fair value.

41 Deferred income

31 December

	2013 £000	2012 £000
Balance at 1 January	**8,884**	**10,000**
Release to income	(1,019)	(1,116)
Balance at 31 December	**7,865**	**8,884**
Current	906	1,018
Non-current	6,959	7,866
Total	**7,865**	**8,884**

The release to income is included in Fees and Commission Income (see Note 10).

42 Income tax liabilities

31 December	2013 £000	2012 £000
Income tax liabilities, which are all current, comprise:		
Corporation tax – CA, S&P, PL and Other Group Activities	8,012	–
Corporation tax – Movestic	–	–
Total	**8,012**	**–**

The carrying value of income tax liabilities is a reasonable approximation of fair value.

43 Other payables

Group 31 December	2013 £000	2012 £000
Accrued expenses	6,960	4,222
VAT	76	474
Employee tax	452	538
Policyholder property fund creditors	1,317	1,773
Other	18,299	10,050
Total	**27,104**	**17,057**
Current	27,104	17,057
Non-current	–	–
Total	**27,104**	**17,057**

Company 31 December	2013 £000	2012 £000
Accrued expenses	1,746	2,544
Other	688	181
Total	**2,434**	**2,725**
Current	2,434	2,725
Non-current	–	–
Total	**2,434**	**2,725**

The carrying value of other payables is a reasonable approximation of fair value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

44 Share capital and share premium

Group
31 December

	2013		2012	
	Number of shares	Share capital £000	Number of shares	Share capital £000
Share capital	115,047,662	42,024	115,047,662	42,024
		Share premium £000		Share premium £000
		42,526		42,523

The number of shares in issue at the balance sheet date included 194,183 shares held in treasury (31 December 2012: 199,011).

Share capital for the Group includes the impact of "reverse acquisition accounting" associated with Chesnara plc's acquisition of Countrywide Assured Life Holdings Ltd (CALH) from Countrywide plc (Countrywide) on 24 May 2004. As a result of this, included within share capital of the Group is £41,501,000, which represents the amount of issued share capital of Countrywide Assured Life Holding (the legal subsidiary) immediately before the acquisition. As a result of this accounting treatment the Group share capital differs from the Chesnara plc company position, which is set out below.

Company
31 December

	2013		2012	
	Number of shares	Share capital £000	Number of shares	Share capital £000
Authorised				
Ordinary shares of 5p each	201,000,000	10,050	201,000,000	10,050
Issued				
Ordinary shares of 5p each	115,047,662	5,752	115,047,662	5,752
		Share premium £000		Share premium £000
		42,526		42,523

The number of shares in issue at the balance sheet date included 194,183 shares held in treasury (31 December 2012: 199,011).

45 Treasury shares

Group and Company 31 December	2013 £000	2012 £000
Balance at 31 December	**212**	**217**

46 Other reserves

Group 31 December	2013 £000	2012 £000
Capital redemption reserve	50	50
Foreign exchange translation reserve	7,153	7,669
Balance at 31 December	**7,203**	**7,719**

Company 31 December	2013 £000	2012 £000
Capital redemption reserve	**50**	**50**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

47 Retained earnings

Group
Year ended 31 December

	2013 £000	2012 £000
Retained earnings attributable to equity holders of the parent company comprise:		
Balance at 1 January	**126,297**	**117,881**
Profit for the year	49,363	27,941
Dividends		
Final approved and paid for 2011	–	(12,519)
Interim approved and paid for 2012	–	(7,006)
Final approved and paid for 2012	(12,921)	–
Interim approved and paid for 2013	(7,178)	–
Balance at 31 December	**155,561**	**126,297**

The interim dividend in respect of 2012, approved and paid in 2012 was paid at the rate of 6.10p per share. The final dividend in respect of 2012, approved and paid in 2013, was paid at the rate of 11.25p per share so that the total dividend paid to the equity shareholders of the Parent Company in respect of the year ended 31 December 2012 was made at the rate of 17.35p per share.

The interim dividend in respect of 2013, approved and paid in 2013, was paid at the rate of 6.25p per share to equity shareholders of the Parent Company registered at the close of business on 13 September 2013, the dividend record date.

A final dividend of 11.63p per share in respect of the year ended 31 December 2013 payable on 22 May 2014 to equity shareholders of the Parent Company registered at the close of business on 11 April 2014, the dividend record date, was approved by the Directors after the balance sheet date. The resulting total final dividend of £13.4m has not been provided for in these financial statements and there are no income tax consequences.

The following summarises dividends per share in respect of the year ended 31 December 2013 and 31 December 2012:

Year ended 31 December

	2013 p	2012 p
Interim – approved and paid	6.25	6.10
Final – proposed/paid	11.63	11.25
Total	**17.88**	**17.35**

Company
Year ended 31 December

	2013 £000	2012 £000
Balance at 1 January	**96,791**	**76,648**
Profit for the year	35,842	39,668
Dividends paid		
Final approved and paid for 2011	–	(12,519)
Interim approved and paid for 2012	–	(7,006)
Final approved and paid for 2012	(12,921)	–
Interim approved and paid for 2013	(7,178)	–
Balance at 31 December	**112,534**	**96,791**

Details of dividends, approved and paid, are set out in the ‘Group’ section above.

48 Employee benefit expense, including Directors

Year ended 31 December	CA £000	S&P £000	Movestic £000	Other Group Activities £000	2013 £000	2012 £000
Wages and salaries	1,004	700	7,324	1,183	10,211	9,081
Social security costs	123	86	2,629	148	2,986	2,332
Pension costs-defined contribution plans	131	92	1,351	135	1,709	1,497
Total	**1,258**	**878**	**11,304**	**1,466**	**14,906**	**12,910**
Average number of employees						
Company					23	23
Subsidiaries					123	125
Total					**146**	**148**

Directors
Note 53 provides detail of compensation to Directors of the Company.

UK-based employees
UK-based employees are all employed by Chesnara plc.

At the end of May 2005 the Group allowed eligible employees to enter a pension scheme known as the Chesnara plc Stakeholder Scheme, on a basis where employer contributions are made to the scheme at the same rate as would be payable had their membership of their predecessor scheme continued, provided that employee contributions also continued to be made at the same rate. The employee may opt to request the Company to pay employer contributions into a personal pension plan, in which instance, employer contributions will be made on the same terms as for the Chesnara plc Stakeholder Scheme.

The employee who joined the Group as a result of the acquisition of CWA Life Holdings plc continues to be a member of the pre-existing defined contribution Group Personal Pension scheme, to which employer and employee contributions are made.

The Group has, for the period covered by these financial statements, only made contributions to defined contribution plans to provide pension benefits for employees upon retirement and, otherwise, has no residual obligation or commitments in respect of any defined benefit scheme.

The Group has established frameworks for approved and unapproved discretionary share option plans which may, at the discretion of the Remuneration Committee, be utilised for granting options to Executive Directors and to other Group employees. No options have been granted in relation to these plans. A Sharesave Plan was launched to all UK employees of the Group in October 2011.

Swedish-based employees
The Swedish Business participates in a combined defined benefit and defined contribution scheme operated by Försäkringsbranschen Pensionskassa (the 'Scheme'). The Scheme is a multi-employer scheme with participants including other Swedish insurance companies not related to the Group. The Scheme provides, for those born in 1978 or earlier, benefits to employees which are linked to their final salary and to the amount of time working for companies which are members of the Scheme. For those employees born in 1979 or later, the scheme operates on a defined contribution basis.

Assets and liabilities are held on a pooled basis and are not allocated by the Trustee to any individual company. Consequently, reliable information is not available to account for the Scheme as a defined benefit scheme and therefore, in accordance with IAS 19 Employee Benefits, the Scheme is accounted for as a defined contribution scheme.

Contributions to the Scheme are based on the funding recommendations of the independent qualified actuary: the contributions paid to the Scheme subsequent to the acquisition of the Swedish Business on 23 July 2009 and up to 31 December 2012, totalled SEK11,178,095 (£1,026,002). During 2013 further contributions of SEK 4,888,430 (£479,723) were made.

The employers within the Scheme are responsible collectively for the funding of the Scheme as a whole and therefore in the event that other employers exit from the Scheme, remaining employers would be responsible for the ongoing funding. The collective nature of the Scheme results in all participating entities sharing the actuarial risk associated with the Scheme.

Försäkringsbranschens Pensionskassa ("FPK") issues an audited annual report (under Swedish law-limited IFRS) each year. The last available published report was as at 31 December 2012.

The annual report states that the Scheme's surplus is SEK 469m (£44.6m) as at 31 December 2012 (SEK 179m (£16.8m) as at 31 December 2011). As at 31 December 2012, the fund had assets under management of SEK 10.9bn (£1,036m), 143 employer insurance companies participating in the Scheme and 26,000 insured individuals.

From the available information, it cannot be determined with certainty as to whether there would be a change in the required employer funding rate, although there is currently no deficit in the Scheme.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

49 Earnings per share

Earnings per share are based on the following:

Year ended 31 December	2013	2012
Profit for the year attributable to shareholders (£000)	49,363	27,941
Weighted average number of ordinary shares	114,851,282	114,848,651
Basic earnings per share	42.98p	24.33p
Diluted earnings per share	42.98p	24.33p

The weighted average number of ordinary shares in respect of the years ended 31 December 2013 and 31 December 2012 is based upon 115,047,662 shares in issue less 196,380 (2012: 199,011) own shares held in treasury.

There were no share options outstanding during the year ended 31 December 2012 or during the year ended 31 December 2013. Accordingly, there is no dilution of the average number of ordinary shares in issue in respect of these periods.

50 Operating leases

Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

Operating lease rentals Year ended 31 December	2013 Non-investment properties £000	Motor vehicles £000	Total £000	2012 Non-investment properties £000	Motor vehicles £000	Total £000
Less than one year	1,237	88	1,325	1,437	31	1,468
Between one and two years	1,139	46	1,185	1,169	19	1,188
Between two and five years	1,949	20	1,969	2,411	3	2,414
More than five years	266	–	266	746	–	746
Expenses recognised in the year in respect of operating leases	**1,432**	**110**	**1,542**	**1,347**	**46**	**1,393**

The Group leases a property under an operating lease which it part occupies in the course of its day-to-day business. The lease expires on 22 July 2019, with an option to renew the lease after that date. Lease payments are reviewed every five years to reflect market rentals. The lease does not include any contingent rentals. The Group also leases a number of office premises which are no longer used for Group purposes. The leases typically run for approximately a further 3 years after the balance sheet date. Lease payments are reviewed every five years to reflect market rentals. None of the leases includes contingent rentals. These leased properties are sublet by the Group. Sublease payments as detailed below are expected to be received during the following years. The Group has recognised a provision of £3,487,000 at 31 December 2013 (31 December 2012: £4,147,000) in respect of these leases (see Note 37).

Leases as lessor

The Group subleases out both investment properties from its investment portfolio and the office premises which are no longer used for Group purposes. The future minimum lease payments under non-cancellable leases are as follows:

Sub lease rentals Year ended 31 December	2013 Investment properties £000	Non-investment properties £000	Total £000	2012 Investment properties £000	Non-investment properties £000	Total £000
Less than one year	1,218	52	1,270	6,011	244	6,255
Between one and two years	1,048	18	1,066	5,426	25	5,451
Between two and five years	2,841	4	2,845	13,577	45	13,622
More than five years	4,389	–	4,389	20,313	30	20,343
Rental income recognised in the year	**4,604**	**92**	**4,696**	**7,612**	**220**	**7,832**
Repairs and maintenance costs recognised in the year	**1,142**	**60**	**1,202**	**1,212**	**74**	**1,286**

51 Contingencies

Past sales

The Group has made provision for the estimated cost of settling complaints in respect of past sales of endowment mortgages. Although the provisions are regularly reviewed, the final outcome could be different from the provisions established as these costs cannot be calculated with certainty and are influenced by external factors beyond the control of management, including future regulatory actions.

52 Capital commitments

There were no capital commitments as at 31 December 2013 or as at 31 December 2012.

53 Related party transactions

(a) Identity of related parties

The shares of the Company were widely held and no single shareholder exercised significant influence or control over the Company.

The Company has related party relationships with:

(i) key management personnel who comprise only the Directors of the Company;

(ii) its subsidiary companies;

(iii) its associated company; and

(iv) other companies over which the Directors have significant influence.

(b) Related party transactions

(i) Transactions with key management personnel.

Key management personnel comprise of the Directors of the Company. There are no executive officers other than certain of the Directors. Key management compensation is as follows:

Year ended 31 December	2013 £000	2012 £000
Short-term employee benefits	1,612	1,440
Post-employment benefits	131	136
Long-term employment benefits	–	39
Total	**1,743**	**1,615**

In addition to their salaries the Company also provides non-cash benefits to Directors, and contributes to a post employment defined contribution pension plan on their behalf, or where regulatory contribution limits are reached, pay an equivalent amount as an addition to base salary.

The following amounts were payable to Directors in respect of bonuses and incentives:

Year ended 31 December	2013 £000	2012 £000
Annual bonus scheme (included in the short-term employee benefits above)	616	442
Long-term incentive plan	330	453
Discretionary bonus	–	238
Compensation for loss of office	–	117
Total	**946**	**1,250**

These amounts have been included in Accrued Expenses as disclosed in Note 43.

The amounts payable under the annual bonus scheme were payable within one year.

As at 31 December 2013, £292,105 is payable within one year in respect of the long-term incentive plan (as at 31 December 2012: £415,715).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

53 Related party transactions (continued)

(b) Related party transactions (continued)

(ii) Transactions with subsidiaries

The Company undertakes centralised administration functions, the costs of which it charges back to its operating subsidiaries. The following amounts which effectively comprised a recovery of expenses at no mark up were credited to the Consolidated Statement of Comprehensive Income of the Company for the respective periods:

Year ended 31 December	2013 £000	2012 £000
Recovery of expenses	**2,800**	**2,834**

(iii) Transactions with associate

Movestic Livförsäkring AB and its associate Modernac SA

Year ended 31 December	2013 £000	2012 £000
Reinsurance premiums paid	(10,708)	(9,442)
Reinsurance recoveries received	5,727	4,109
Reinsurance commission received	2,675	899
	(2,306)	(4,434)
Amounts outstanding as at balance sheet date	**(5,148)**	**(6,731)**

Movestic Livförsäkring AB had the following amounts outstanding at the balance sheet date:

31 December 2013	Amounts owed by associate £000	Amounts owed to associate £000
Modernac S.A.	**–**	**5,148**

31 December 2012	Amounts owed by associate £000	Amounts owed to associate £000
Modernac S.A.	**130**	**6,861**

These amounts have been included in other payables as disclosed in Note 43 and other receivables as disclosed in Note 28.

54 Group entities

Control of the Group

The issued share capital of Chesnara plc the Group parent company is widely held, with no single party able to control 20% or more of such capital or of the rights which such ownership confers.

Group Subsidiary Companies

Name	Country of Incorporation or Registration	Ownership interest 31 December 2013	Ownership interest 31 December 2012	Functional Currency
Countrywide Assured plc	England & Wales	100% of all share capital (1)	100% of all share capital (1)	Sterling
Countrywide Assured Life Holdings Limited	England & Wales	100% of all share capital	100% of all share capital	Sterling
Countrywide Assured Services Limited	England & Wales	100% of all share capital	100% of all share capital (1)	Sterling
Countrywide Assured Trustee Company Limited	England & Wales	100% of all share capital	100% of all share capital (1)	Sterling
CWA Life Holdings plc	England & Wales	100% of all share capital	100% of all share capital	Sterling
Movestic Livförsäkring AB	Sweden	100% of all share capital	100% of all share capital	Swedish Krona
Modernac S.A.	Luxembourg	49% of all share capital (2)	49% of all share capital (2)	Swedish Krona
Movestic Kapitalförvältning AB	Sweden	100% of all share capital (2)	100% of all share capital (2)	Swedish Krona
Save & Prosper Insurance Limited	England & Wales	Dissolved (4)	100% of all share capital	Sterling
Save & Prosper Pensions Limited	England & Wales	Dissolved (4)	100% of all share capital (3)/(4)	Sterling
Protection Life Company Limited (previously Direct Line Life Insurance Company Limited)	England & Wales	100% of all share capital (5)	–	Sterling

(1) Held indirectly through Countrywide Assured Life Holdings Limited.

(2) Held indirectly through Movestic Livförsäkring AB.

(3) Held indirectly through Save & Prosper Insurance Limited.

(4) Dissolved 22 January 2013.

(5) Acquired on 28 November 2013.

SECTION E

EEV SUPPLEMENTARY INFORMATION

IN THIS SECTION

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181 Summarised EEV Consolidated Balance Sheet
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DIRECTORS' RESPONSIBILITIES STATEMENT IN RESPECT OF THE EEV SUPPLEMENTARY INFORMATION

The Directors have chosen to prepare Supplementary Information in accordance with the EEV Principles issued in May 2004 by the CFO Forum of European Insurance Companies and expanded by the Additional Guidance on European Embedded Value Disclosures issued in October 2005.

When compliance with the EEV Principles is stated, those principles require the Directors to prepare supplementary information in accordance with the Embedded Value Methodology ('EVM') contained in the EEV Principles and to disclose and explain any non-compliance with the EEV guidance included in the EEV Principles.

In preparing the EEV supplementary information, the Directors have:

- Prepared the supplementary information in accordance with the EEV Principles;
- Identified and described the business covered by the EVM;
- Applied the EVM consistently to the covered business;
- Determined assumptions on a realistic basis, having regard to past, current and expected future experience and to any relevant external data, and then applied them consistently;
- Made estimates that are reasonable and consistent; and
- Described the basis on which business that is not covered business has been included in the supplementary information, including any material departures from the accounting framework applicable to the Group's financial statements.

By order of the Board

Chairman	Chief Executive Officer
Peter Mason	Graham Kettleborough
27 March 2014	27 March 2014

INDEPENDENT AUDITOR'S REPORT TO THE DIRECTORS OF CHESNARA PLC ON THE EEV SUPPLEMENTARY INFORMATION

We have audited the EEV Supplementary Information of Chesnara plc for the year ended 31 December 2013 which comprises the summarised EEV consolidated income statement, the summarised EEV consolidated balance sheet and the related notes 1 to 11. The financial reporting framework that has been applied in their preparation is the EEV Principles issued in May 2004 by the CFO Forum of European Insurance Companies and expanded by the Additional Guidance on European Embedded Value Disclosures issued in October 2005 ("the EEV Principles").

We have reported separately on the statutory group financial statements of Chesnara plc for the year ended 31 December 2013. The EEV Supplementary Information should be read in conjunction with the financial statements prepared on an IFRS basis.

This report is made solely to the company's directors in accordance with our engagement letter and solely for the purpose of expressing an opinion on whether the EEV Supplementary Information has been properly prepared in accordance with the EEV principles. Our audit work has been undertaken so that we might state to the company's directors those matters we are required to state to them in an independent auditors' report and for no other purpose. To the fullest extent permitted by law, we will not accept or assume responsibility to anyone other than the company, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors

As explained more fully in the Directors' Responsibility Statement in respect of the EEV Supplementary Information, the Directors are responsible for the preparation of the EEV Supplementary Information.

Our responsibility

Our responsibility is to audit and express an opinion on the EEV Supplementary Information in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

Scope of review

An audit involves obtaining evidence about the amounts and disclosures in the Supplementary Information sufficient to give reasonable assurance that the Supplementary Information is 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 Supplementary Information. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Conclusion

In our opinion, the EEV Supplementary Information for the year ended 31 December 2013 has been properly prepared in accordance with the EEV principles using the methodology and assumptions set out on pages 182 to 187.

Deloitte LLP
Chartered Accountants and Statutory Auditor
Manchester
United Kingdom
27 March 2014

SUMMARISED EEV CONSOLIDATED INCOME STATEMENT

31 December	**Note**	**2013 £000**	**2012 £000**
Operating profit of covered business	**6(b)**	8,901	**19,032**
Other operational result	**6(b)**	(2,276)	(4,446)
Operating profit		**6,625**	**14,586**
Variation from longer-term investment return	**6(b)**	54,646	28,035
Effect of economic assumption changes	**6(b)**	16,447	(6,504)
Profit before tax and before exceptional item		**77,178**	**36,117**
Exceptional items			
Profit recognised on business combination	**9**	12,283	–
Effect of modelling adjustments	**6(a)**	4,073	3,574
Profit before tax		**94,074**	**39,691**
Tax	**6(b)**	(7,307)	(4,862)
Profit for the period attributable to the equity holders of the parent company		**86,767**	**34,829**
Earnings per share			
Based on profit for the year		75.55p	30.33p
Diluted profit per share			
Based on profit for the year		75.55p	30.33p

The notes and information on pages 182 to 195 form part of this supplementary information.

SUMMARISED EEV CONSOLIDATED BALANCE SHEET

31 December Assets	Note	2013 £000	2012 £000
Value of in-force business	5, 8	262,161	210,080
Deferred acquisition costs arising on unmodelled business		487	497
Acquired value of customer relationships		419	562
Property and equipment		673	369
Investment in associate		4,088	2,902
Deferred tax asset		509	1,280
Reinsurers' share of insurance contract provisions		328,810	235,782
Amounts deposited with reinsurers		33,102	28,941
Investment properties		20,387	100,167
Financial assets			
Equity securities at fair value through income		479,617	427,303
Holdings in collective investment schemes at fair value through income		3,440,992	3,009,799
Debt securities at fair value through income		370,666	363,377
Insurance and other receivables		46,382	24,313
Prepayments		4,889	3,160
Policyholders' funds held by the Group		130,237	61,171
Derivative financial instruments		2,956	3,095
Total financial assets		4,475,739	3,892,218
Reinsurers' share of accrued policy claims		11,399	4,489
Income taxes		2,608	8,649
Cash and cash equivalents		184,263	228,676
Total assets		**5,324,645**	**4,714,612**
Liabilities			
Insurance contract provisions		2,323,643	2,171,259
Other provisions		5,348	5,161
Financial liabilities			
Investment contracts at fair value through income		2,293,836	2,033,131
Borrowings		100,290	55,373
Derivative financial instruments		387	286
Liabilities relating to policyholders' funds held by the Group		130,237	61,171
Total financial liabilities		2,524,750	2,149,961
Reinsurance payables		11,154	16,183
Payables related to direct insurance and investment contracts		47,137	38,894
Income taxes		8,012	4,350
Other payables		27,104	17,057
Bank overdraft		1,127	602
Total liabilities		**4,948,275**	**4,403,467**
Net assets		**376,370**	**311,145**
Equity			
Share capital		42,024	42,024
Share premium		42,526	42,523
Treasury shares		(212)	(217)
Foreign exchange reserve		13,927	15,378
Other reserves		50	50
Retained earnings		278,055	211,387
Total shareholders' equity	**5, 8**	**376,370**	**311,145**

The notes and information on pages 182 to 195 form part of this supplementary information. Approved by the Board of Directors on 27 March 2014 and signed on its behalf by:

David Rimmington
Finance Director

Graham Kettleborough
Chief Executive Officer

NOTES TO THE EEV SUPPLEMENTARY INFORMATION

1 Basis of preparation

This section sets out the detailed methodology followed for producing these Group financial statements which are supplementary to the Group's primary financial statements which have been prepared in accordance with International Financial Reporting Standards ('IFRS'), as adopted by the EU. These financial statements have been prepared in accordance with the European Embedded Value ('EEV') principles issued in May 2004 by the European CFO Forum and supplemented by Additional Guidance on EEV Disclosures issued by the same body in October 2005. The principles provide a framework intended to improve comparability and transparency in embedded value reporting across Europe.

In order to improve understanding of the Group's financial position and performance, certain of the information presented in these financial statements is presented on a segmental basis: the business segments are the same as those described in Note 9 to the consolidated financial statements prepared on the IFRS basis. The PL business was acquired on 28 November 2013: accordingly, the results relating thereto, as reflected in segmental analysis are for a period of 34 days. Prior year information in respect of the financial position as at 31 December 2012 and for the year then ended is designated as £nil in respect of the PL business, while other prior year data are designated as not applicable ('n/a').

2 Covered business

The Group uses EEV methodology to value the bulk of its long-term business (the 'covered business'), which is written primarily in the UK and Sweden, as follows:

(i) for the UK Business, the covered business of CA and S&P comprises the business's long-term business being those individual life insurance, pensions and annuity contracts falling under the definition of long-term insurance business for UK regulatory purposes. The covered business for the PL segment comprises the business's long-term protection business and Payment Protection Insurance business.

(ii) for the Swedish Business (comprising the Movestic segment), the covered business comprises the business's long-term pensions and savings unit-linked business. Group life and sickness business, including waiver of premium and non-linked individual life assurance policies are not included in the covered business: the result relating to this business is established in accordance with IFRS principles and is included within 'other operational result' within the consolidated summarised income statement.

(iii) The operating expenses of the holding company, Chesnara plc, are allocated across the segments.

Under EEV principles no distinction is made between insurance and investment contracts, as there is under IFRS, which accords these classes of contracts different accounting treatments.

3 Methodology

(a) Embedded value

Overview

Shareholders' equity comprises the embedded value of the covered business, together with the net equity of other Group companies, including that of the holding company which is stated after writing down fully the carrying value of the covered business.

The embedded value of the covered business is the aggregate of the shareholder net worth ('SNW') and the present value of future shareholder cash flows from in-force covered business (value of in-force business) less any deduction for (i) the cost of guarantees within S&P, and (ii) the cost of required capital. It is stated after allowance has been made for aggregate risks in the business. SNW comprises those amounts in the long-term business, which are either regarded as required capital or which represent surplus assets within that business.

New business

CA, S&P and PL

Much of the covered business is in run-off and is, accordingly, substantially closed to new business. Up to 31 December 2012 the UK businesses did still sell a small amount of new business but, overall, the contribution from new business to the results established using EEV methodology is not material. Accordingly, not all of those items related to new business values, which are recommended by the EEV guidelines, are reported in this supplementary financial information.

Movestic

New business, in relation to the pensions and savings covered business is taken as all business where contracts are signed and new premiums paid during the reporting period, for both new policies and premium increases on existing business, but excluding standard renewals. New business premium volumes as disclosed in "Enhance value through new business" on pages 22 to 23 are not consistent with this definition, as they include non-covered business.

New business premium volumes for the year are as follows:

Pensions and savings covered business **31 December**	**2013** **£m**	**2012** **£m**
New business premium income	46.0	18.8
Regular premium increments	16.0	13.9
Total new business premium income*	**62.0**	**32.7**

*Basis: annualised premium plus 1/10 single premium translated into sterling at the 2013 average rate of SEK 10.1901 = £1 (2012: SEK 10.7326) = £1).

The new business contribution has been assessed as at the end of the year, using opening assumptions.

(a) Embedded value (continued)

Value of in-force business

The cash flows attributable to shareholders arising from in-force business are projected using best estimate assumptions for each component of cash flow.

The present value of the projected cash flows is established by using a discount rate which reflects the time value of money and the risks associated with the cash flows which are not otherwise allowed for. There is a deduction for the cost of holding the required capital, as set out below.

In respect of Movestic there are certain non-linear exposures of shareholder profit to asset returns arising from variable administrative fees and variable investment fund rebates which are modelled deterministically rather than stochastically.

Participating business

For participating business within the S&P business the Group maintains the assets and liabilities in separate with-profits funds. In accordance with the Principles and Practices of Financial Management, in the first instance all benefits, which in some cases include guaranteed minimum investment returns, are paid from policyholder assets within the fund. The participating business effectively operates as a smoothed unit-linked contract subject to minimum benefit guarantees. The with-profits funds contain assets which are attributable to shareholders as well as those attributable to policyholders. Assets attributable to shareholders can only be released from the fund subject to meeting prudent liabilities in respect of minimum benefits and the frictional cost of this restriction has been allowed for in determining the value of the in-force business.

Fundamentally, the value of the with-profits in-force business is driven by the fund management charges levied on the policyholder assets, subject to the effect of minimum benefit guarantees.

Taxation

The present value of the projected cash flows arising from in-force business takes into account all tax which is expected to be paid under current legislation, including tax which would arise if surplus assets within the covered business were eventually to be distributed. For the UK business, allowance has been made for planned reductions in corporation tax, as announced by the Chancellor in his budget speech on 20 March 2013. The value as at 31 December 2012 was adjusted in the 2012 Report & Accounts to allow for this announcement.

The value of the in-force business has been calculated on an after-tax basis and is grossed up to the pre-tax level for presentation in the income statement. The amount used for the grossing up is the amount of shareholder tax, excluding those payments made on behalf of policyholders, being policyholder tax in the UK businesses and yield tax in Movestic.

Cost of capital

The valuation approach used requires consideration of 'frictional' costs of holding shareholder capital: in particular, the cost of tax on investment returns and the impact of investment management fees can reduce the face value of shareholder funds. For CA, the expenses relating to corporate governance functions eliminate any taxable investment return in shareholder funds, while investment management fees are not material. The cost of holding the required capital to support the covered business (see 3(b) below) is reflected as a deduction from the value of in-force business.

Financial options and guarantees

CA

The principal financial options and guarantees in CA are (i) guaranteed annuity rates offered on some unit-linked pension contracts and (ii) a guarantee offered under Timed Investment Funds that the unit price available at the selected maturity date (or at death, if earlier) will be the highest price attained over the policy's life. The cost of these options and guarantees has been assessed, in principle, on a market-consistent basis, but, in practice, this has been carried out on approximate bases, which are appropriate to the level of materiality of the results.

S&P

The principal financial options and guarantees in S&P are (i) minimum benefits payable on maturity or retirement for participating business; (ii) the option to extend the term under the Personal Retirement Account contract on terms potentially beneficial to the policyholder; (iii) the option to increase premiums under the Personal Retirement Account contract on terms potentially beneficial to the policyholder; and (iv) certain insurability options offered.

The cost of guaranteeing a minimum investment return on participating contracts, being the only material guarantee, has been assessed on a market consistent basis. This has involved the use of a stochastic asset model, which is designed to establish a cost of guarantees which is consistent with prices in the market at the valuation date, for example the prices of derivative instruments. For the remaining options and guarantees the cost has been assessed on an approximate basis, appropriate to the level of materiality of the results.

PL

There are no material financial options and guarantees within PL.

NOTES TO THE EEV SUPPLEMENTARY INFORMATION (CONTINUED)

3 Methodology (continued)

(a) Embedded value (continued)

Movestic

In respect of Movestic, some contracts provide policyholders with an investment guarantee, whereby a minimum rate of return is guaranteed for the first 5 years of the policy, at a rate of 3% per annum. The value of the guarantee is ignored as it is not material to the results.

Allowance for risk

Allowance for risk within the covered business is made by:

(i) setting required capital levels by reference to the assessment of capital needs made by the Directors of the regulated entities within the respective businesses;

(ii) setting the risk discount rate, which is applied to the projected cash flows arising on the in-force business, at a level which includes an appropriate risk margin (see 3(c) below); and

(iii) explicit allowance for the cost of financial options and guarantees and, where appropriate, for reinsurer default.

Internal group company

EEV Guidance requires that actual and expected profit or loss incurred by an internal group company on services provided to the covered business should be included in allowances for expenses. The covered business in Movestic is partially managed by an internal group fund management company. Not all relevant future income and expenses of that company have been included in the calculation of embedded value. However, the effect is not considered to be material.

Consolidation adjustments

Consolidation adjustments have been made to:

(i) eliminate the investment in subsidiaries;

(ii) allocate group debt finance against the segment to which it refers; and

(iii) allocate corporate expenses as explained in note 4(d) below.

(b) Level of required capital

The level of required capital of the covered business reflects the amount of capital that the Directors consider necessary and appropriate to manage the respective businesses. In forming their policy the Directors have regard to the minimum statutory requirements and an internal assessment of the market, insurance and operational risks inherent in the underlying products and business operations. The capital requirement resulting from this assessment represents:

(i) for CA plc (comprising the CA and S&P segments), 162.5% of the long-term insurance capital requirement ('LTICR') together with 100% of the resilience capital requirement ('RCR'), as determined by the regulations of the Prudential Regulatory Authority in the UK;

(ii) for PL, 150% of the long-term insurance capital requirement ('LTICR'), deferred by the Prudential Regulatory Authority; and

(iii) for Movestic, 150% of the regulatory solvency requirement as determined by Finansinspektionen in Sweden.

The required level of regulatory capital is provided as follows:

(i) for the UK Business, by the retained surplus within the long-term business fund and by share capital and retained earnings within the shareholder funds of the regulated entity; and

(ii) for Movestic, by share capital and additional equity contributions from the parent company, net of the accumulated deficit in the regulated entity, these components together comprising shareholder's equity.

Movestic is reliant, in the short to medium term, on further equity contributions from the parent company, Chesnara plc.

(c) Discount rates

The discount rates are a combination of the reference rate and a risk margin. The reference rate reflects the time value of money and the risk margin reflects any residual risks inherent in the covered business and makes allowance for the risk that future experience will differ from that assumed. In order to reduce the subjectivity when setting the discount rates, the Group has decided to adopt a 'bottom up' market-consistent approach to allow explicitly for market risk.

Using the market-consistent approach, each cash flow is valued at a discount rate consistent with that used in the capital markets: in accordance with this, equity-based cash flows are discounted at an equity discount rate and bond-based cash flows at a bond discount rate. In practice a short-cut method known as the 'certainty equivalent' approach has been adopted. This method assumes that all cash flows earn the reference rate of return and are discounted at the reference rate.

In general, and consistent with the market's approach to valuing financial instruments for hedging purposes, the reference rate is based on swap yields. These have been taken as mid swap yields available in the market at the end of the reporting period.

Allowance also needs to be made for non-market risks. For some of these risks, such as mortality and expense risk, it is assumed that the shareholder can diversify away any uncertainty where the impact of variations in experience on future cash flows is symmetrical. For those risks that are assumed to be diversifiable, no adjustment has been made. For any remaining risks that are considered to be non-diversifiable risks, there is no risk premium observable in the market and, therefore, a constant margin has been added to the risk margin. The margin added reflects the assumed risks within the businesses and is 50 basis points for CA, S&P and PL (as at 31 December 2012: 50 basis points), and 100 basis points for Movestic (as at 31 December 2012: 70 basis points). This margin is applied to the basic value of in-force business prior to the deductions for financial options and guarantees and the cost of required capital.

(d) Analysis of profit

The contribution to operating profit, which is identified at a level which reflects an assumed longer-term level of investment return, arises from three sources:

(i) new business;

(ii) return from in-force business; and

(iii) return from shareholder net worth.

Additional contributions to profit arise from:

(i) variances between the actual investment return in the year and the assumed long-term investment return; and

(ii) the effect of economic assumption changes.

The contribution from new business represents the value recognised at the end of each year in respect of new business written in that year, after allowing for the cost of acquiring the business, the cost of establishing the required technical provisions and after making allowance for the cost of capital, calculated on opening assumptions.

The return from in-force business is calculated using closing assumptions and comprises:

(i) the expected return, being the unwind of the discount rates over the year applied to establish the value of in-force business at the beginning of the year;

(ii) variances between the actual experience over the year and the assumptions made to establish the value of business in force at the beginning of the year; and

(iii) the net effect of changes in future assumptions, made prospectively at the end of the year, from those used in establishing the value of business in force at the beginning of the year, other than changes in economic assumptions.

The contribution from shareholder net worth comprises the actual investment return on residual assets in excess of the required capital.

(e) Assumption setting

There is a requirement under EEV methodology to use best estimate demographic assumptions and to review these at least annually with the economic assumptions being reviewed at each reporting date. The current practice is detailed below.

Each year the demographic assumptions are reviewed as part of year-end processes and hence were reviewed in December 2013.

The detailed projection assumptions, including mortality, morbidity, persistency and expenses reflect recent operating experience. Allowance is made for future improvement in annuitant mortality based on experience and externally published data. Favourable changes in operating experience, particularly in relation to expenses and persistency, are not anticipated until the improvement in experience has been observed. Holding company expenses (for the Chesnara Group such expenses relate largely to listed company functions) are allocated across the segments in proportion to the value before tax of the in-force business. Hence the expense assumptions used for the cash flow projections include the full cost of servicing this business.

For the Movestic business, persistency assumptions have been updated reflecting latest experience and Management's view of future trends.

The economic assumptions are reviewed and updated at each reporting date based on underlying investment conditions at the reporting date. The assumed discount rates and inflation rates are consistent with the investment return assumptions.

In addition, the demographic assumptions used at 31 December 2013 are considered to be best estimate and, consequently, no further adjustments are required. In respect of the CA Business, the assumptions required in the calculation of the value of the annuity rate guarantee on pension business have been set equal to best-estimate assumptions.

(f) Pension schemes

In Movestic, where the Group participates in a combined defined benefit and defined contribution scheme, future contributions to the scheme are reflected in the value of in-force business.

(g) Financial reinsurance

In respect of Movestic the Group uses financial reinsurance to manage the impact of its new business strain. Whilst this liability is valued at fair value within the IFRS statements, allowing for an option which provides the Group with the right to settle the liability early on beneficial terms, when valuing the shareholder net worth within the EEV it is considered more appropriate to assess this liability at a higher cost, reflecting the likelihood of the option not being utilised.

NOTES TO THE EEV SUPPLEMENTARY INFORMATION (CONTINUED)

4 Assumptions

(a) Investment returns

Investment returns are assumed to be equal to the reference rate, as covered in Note 3(c). For linked business, the aggregate return has been determined by the reference rate less an appropriate allowance for tax. For the valuation at 31 December 2012 the models for the CA business were enhanced to allow for the use of a full yield curve. Refer to Note 6(a) below for the impact of this change which was classified as a modelling adjustment in the year ended 31 December 2012.

The rates presented below are indicative spot rates:

31 December	CA		S&P		PL*		Movestic	
	2013	2012	2013	2012	2013	2012	2013	2012
Investment Return					2.80%	n/a		
5 year	2.18%	1.03%	2.18%	1.03%	–	–	2.18%	1.52%
10 year	3.11%	1.93%	3.11%	1.93%	–	–	2.87%	2.04%
15 year	3.48%	2.58%	3.48%	2.58%	–	–	3.12%	2.28%
20 year	3.58%	2.94%	3.58%	2.94%	–	–	3.20%	2.33%
25 year	3.59%	3.15%	3.59%	3.15%	–	–	3.20%	2.33%
30 year	3.56%	3.23%	3.56%	3.23%	–	–	3.20%	2.33%
Inflation – RPI	3.00%	2.30%	3.00%	2.30%	3.00%	n/a	1.82%	1.71%

*For PL a single rate is applied for all durations.

(b) Actuarial assumptions

The demographic assumptions used to determine the value of the in-force business have been set at levels commensurate with the underlying operating experience identified in the periodic actuarial investigations.

Certain products contain provisions that provide for the charges in respect of mortality risk to be reviewable. In these cases assumptions for future experience and charges are assumed to be linked and assumptions are only updated when decisions have been made regarding product charges, so as not to capitalise any benefits that may not accrue to shareholders.

(c) Taxation

Projected tax has been determined assuming current tax legislation and rates continue unaltered, except where future tax rates or practices have been announced. The tax rates for the UK business allow for changes in Corporation Tax as announced by the Chancellor in his budget speech of 20 March 2013, so reflect a reduction from the current rate of 23% to 20% from April 2015.

(d) Expenses

The expense levels are based on internal expense analysis investigations and are appropriately allocated to the new business and policy maintenance functions.

For CA, S&P and PL, these have been determined by reference to:

(i) the outsourcing agreements in place with our third-party business process administrators;

(ii) anticipated revisions to the terms of such agreements as they fall due for renewal; and

(iii) corporate governance costs relating to the covered business.

For Movestic, these have been determined by reference to:

(i) an expense analysis in which all expenses were allocated to covered and uncovered business, with expenses for the covered business being allocated to acquisition and maintenance activities; and

(ii) expense drivers, being, in relation to acquisition costs, the number of policies sold during the year and, in relation to maintenance expenses, the average number of policies in force during the year.

Holding company expenses (for the Chesnara Group such expenses relate largely to listed company functions) are allocated across the segments on a basis that reflects each segment's economic consumption of such costs.

EEV Guidance requires that no allowance is made for future productivity improvements in expense assumptions. For the UK business, for expenses relating to policy administration this requirement is met. As the UK company is essentially closed to new business, those governance expenses which are not immediately variable can reasonably be expected to reduce through management control in the future, though the timing and scale of such reductions is not fixed. A prudent estimate of the reductions has been allowed for within the expense assumptions.

(e) Discount rate

An explicit constant margin is added to the reference rate shown in (a) above to cover any remaining risks that are considered to be non-market, non-diversifiable risks, as there is no risk premium observable in the market. This margin, which is 50 basis points for CA, S&P and PL (as at 31 December 2012: 50 basis points) and 100 basis points for Movestic (as at 31 December 2012: 70 basis points), gives due recognition to the relative sensitivity of the value of in-force business to the discount rate for the different businesses, and to the fact that:

a) For CA:

- (i) the covered business is closed to new business;
- (ii) there is no significant exposure in the with-profit business, which is wholly reinsured;
- (iii) expense risk is limited as a result of the outsourcing of substantially all policy administration and related functions to third-party business process administrators; and
- (iv) for much of the life business the Group has the ability to vary risk charges made to policyholders.

b) For S&P and PL:

- (i) the covered business is closed to new business; and
- (ii) expense risk is limited as a result of the outsourcing of substantially all policy administration and related functions to third-party business process administrators.

c) For Movestic:

- (i) the covered business remains open;
- (ii) the in-force business is relatively small;
- (iii) reinsurance is used to significantly reduce insurance risks; and
- (iv) a number of the risks provide diversification benefits within the Chesnara Group, in relation to reinsurance counterparties, market exposures and policyholder populations.

NOTES TO THE EEV SUPPLEMENTARY INFORMATION (CONTINUED)

5 Analysis of shareholders' equity

31 December 2013	CA £000	S&P £000	PL £000	Movestic £000	Other group activities £000	Total £000
Regulated entities						
Capital required	23,776	43,447	37,845	16,863	–	121,931
Restricted capital	–	–	–	–	–	–
Free surplus	32,386	44,750	1,397	17,969	–	96,502
Regulatory capital resource of regulated entities	**56,162**	**88,197**	**39,242**	**34,832**	**–**	**218,433**
Adjustments to shareholder net worth:						
Deferred acquisition costs	–	–	–	(54,498)	–	(54,498)
Financial reinsurance liability	–	–	–	(4,358)	–	(4,358)
Software asset adjustment	–	–	–	(5,004)	–	(5,004)
Adjustment to provisions on insurance contracts	–	2,602	–	–	–	2,602
Deferred tax	2,372	–	–	–	–	2,372
Policyholder funds	–	(14,807)	–	–	–	(14,807)
Other asset/liability adjustments	322	2	–	5,455	–	5,779
Adjusted shareholder net worth	**58,856**	**75,994**	**39,242**	**(23,573)**	**–**	**150,519**
In-force value of covered business	67,171	30,482	25,507	139,001	–	262,161
Embedded value of regulated entities	**126,027**	**106,476**	**64,749**	**115,428**	**–**	**412,680**
Less: amount financed by borrowings	–	(29,699)	(43,341)	–	–	(73,040)
Embedded value of regulated entities attributable to shareholders	**126,027**	**76,777**	**21,408**	**115,428**	**–**	**339,640**
Net equity of other Group companies	–	–	–	1,894	34,836	36,730
Total shareholders' equity	**126,027**	**76,777**	**21,408**	**117,322**	**34,836**	**376,370**

31 December 2012	CA £000	S&P £000	Movestic £000	Other group activities £000	Total £000
Regulated entities					
Capital required	26,967	47,731	17,355	–	92,053
Restricted capital	–	–	–	–	–
Free surplus	37,142	27,513	15,127	–	79,782
Regulatory capital resource of regulated entities	**64,109**	**75,244**	**32,482**	**–**	**171,835**
Adjustments to shareholder net worth:					
Deferred acquisition costs	–	–	(54,314)	–	(54,314)
Financial reinsurance liability	–	–	(5,213)	–	(5,213)
Software asset adjustment	–	–	(5,712)	–	(5,712)
Adjustment to provisions on insurance contracts	–	3,052	–	–	3,052
Policyholder funds	–	(15,351)	–	–	(15,351)
Other asset/liability adjustments	388	–	6,340	–	6,728
Adjusted shareholder net worth	**64,497**	**62,945**	**(26,417)**	**–**	**101,025**
In-force value of covered business	67,040	18,537	124,503	–	210,080
Embedded value of regulated entities	**131,537**	**81,482**	**98,086**	**–**	**311,105**
Less: amount financed by borrowings	–	(29,662)	–	–	(29,662)
Embedded value of regulated entities attributable to shareholders	**131,537**	**51,820**	**98,086**	**–**	**281,443**
Net equity of other Group companies	–	–	1,587	28,115	29,702
Total shareholders' equity	**131,537**	**51,820**	**99,673**	**28,115**	**311,145**

NOTES TO THE EEV SUPPLEMENTARY INFORMATION (CONTINUED)

5 Analysis of shareholders' equity (continued)

EEV free surplus, as shown above, represents the balance of the shareholder net worth above the capital required. The movement in free surplus is analysed as follows:

Year ended 31 December 2013	CA £000	S&P £000	PL £000	Movestic £000	Total £000
Free surplus at beginning of the year	**37,142**	**27,513**	**–**	**15,127**	**79,782**
Dividend paid to parent	(22,250)	(17,750)	–	–	(40,000)
Surplus arising in the year	14,303	31,246	191	2,350	48,090
Adjustments to required capital	3,191	4,284	1,206	492	9,173
Decrease in policyholder funds cover for capital requirement	–	(543)	–	–	(543)
Free surplus at end of the year	**32,386**	**44,750**	**1,397**	**17,969**	**96,502**

Year ended 31 December 2012	CA £000	S&P £000	Movestic £000	Total £000
Free surplus at beginning of the year	**37,147**	**29,854**	**11,474**	**78,475**
Dividend paid to parent	(22,000)	(22,000)	–	(44,000)
Synergies and adjustments arising from the Part VII transfer, including adjustments to required capital	7,000	–	–	7,000
Surplus arising in the year	13,261	14,557	2,877	30,695
Adjustments to required capital	1,734	5,394	776	7,904
Decrease in policyholder funds cover for capital requirement	–	(292)	–	(292)
Free surplus at end of the year	**37,142**	**27,513**	**15,127**	**79,782**

The movement in the in-force value of covered business comprises:

Year ended 31 December 2013	CA £000	S&P £000	PL £000	Movestic £000	Total £000
Value at beginning of year	**67,040**	**18,537**	**–**	**124,503**	**210,080**
Amount arising on acquisition	–	–	25,646	–	25,646
Amount charged to foreign exchange reserve	–	–	–	(1,491)	(1,491)
Amount credited/(charged) to operating profit	131	11,945	(139)	15,989	27,926
Value at end of year	**67,171**	**30,482**	**25,507**	**139,001**	**262,161**

Year ended 31 December 2012	CA £000	S&P £000	Movestic £000	Total £000
Value at beginning of year	**60,655**	**17,519**	**121,386**	**199,560**
Amount credited to foreign exchange reserve	–	–	1,640	1,640
Amount credited to operating profit	6,385	1,018	1,477	8,880
Value at end of year	**67,040**	**18,537**	**124,503**	**210,080**

S&P and PL
EEV shareholders equity for the S&P and PL segments is presented net of the borrowings that were used to fund their respective acquisitions.

Movestic
The adjusted shareholder net worth of Movestic is that of the regulated entity, which includes also the net worth attributable to the non-covered business within the regulated entity. Accordingly, for Movestic, the embedded value of regulated entities comprises the embedded value of covered business and the value of the non-covered business of the regulated entity, the latter component being valued on an IFRS basis.

6 Summarised statement of changes in equity and analysis of profit/(loss)

(a) Changes in equity may be summarised as:

Statement of changes in equity
Year ended 31 December

		2013 £000		2012 £000
Shareholders' equity at beginning of the year		**311,145**		**294,489**
Profit for the year attributable to shareholders before modelling adjustments	82,694		31,255	
Effect of modelling adjustments	4,073		3,574	
Profit for the year		**86,767**		**34,829**
Issue of new shares				
Share premium		3		–
Sale of treasury shares		5		–
Foreign exchange reserve movement		(1,451)		1,352
Dividends paid		(20,099)		(19,525)
Shareholders' equity at end of the year		**376,370**		**311,145**

Effect of modelling adjustments

Year ended 31 December 2013

Modelling adjustments during the year have reduced when compared with those included in the prior year.

Positive modelling adjustments this period of £4.1m relate entirely to the Movestic business. These have arisen due to refinements being made to the way in which modelling of commission is performed, which is now performed at a more granular level.

Year ended 31 December 2012

Modelling adjustments during the year ended 31 December 2012 give rise to a net increase in EEV of £3.6m, comprising:

Movestic

During 2012, there has been a continued focus on ensuring that the Movestic EEV model is robust. The process, which has included independent review, has identified the following:

(i) Levels of commission claw-back within the future cash flow projections were overstated by £7.9m; and

(ii) Several enhancements to policy fee cash flow estimates and data input routines have been identified with a total net adverse impact of £1.1m.

UK

The CA and CWA EEV models previously assumed a single average rate of investment return for all durations as opposed to the use of a full yield curve. This approximation was reported in the EEV assumptions section 4(a) of the Supplementary Information within the Interim Financial Statements for the Six Months Ended 30 June 2012. As at 31 December 2012 the models were enhanced to recognise differing rates of return across the different durations of the yield curve resulting in a net of tax increase of £12.6m.

The PL EEV model assumes a single average rate of investment return for all durations as opposed to the use of a full yield curve.

The effect of modelling adjustments is classified as an exceptional item in the consolidated income statement and is presented after operating profit.

NOTES TO THE EEV SUPPLEMENTARY INFORMATION (CONTINUED)

6 Summarised statement of changes in equity and analysis of profit/(loss) (continued)

(b) The profit/(loss) for the year before modelling adjustments is analysed as:

Year ended 31 December 2013	CA £000	S&P £000	PL £000	UK Total £000	Movestic £000	Other Group Activities £000	Total £000
Covered business							
New business contribution	704	13	–	717	7,196	–	7,913
Return from in-force business							
Expected return	1,389	151	61	1,601	3,929	–	5,530
Experience variances	7,590	4,695	–	12,285	(6,490)	–	5,795
Operating assumption changes	(4,295)	4,458	–	163	(10,233)	–	(10,070)
Return on shareholder net worth	185	(452)	–	(267)	–	–	(267)
Operating profit of covered business	**5,573**	**8,865**	**61**	**14,499**	**(5,598)**	**–**	**8,901**
Variation from longer-term investment return	22,394	11,414	–	33,808	20,838	–	54,646
Effect of economic assumption changes	(3,596)	22,463	–	18,867	(2,420)	–	16,447
Profit of covered business before tax	**24,371**	**42,742**	**61**	**67,174**	**12,820**	**–**	**79,994**
Tax thereon				(7,639)	–	–	(7,639)
Profit of covered business after tax				**59,535**	**12,820**	**–**	**72,355**
Results of non-covered business and of other group companies							
Profit/(loss) before tax				–	2,677	(4,953)	(2,276)
Exceptional profit arising on purchase of Protection Life				–	–	12,283	12,283
Tax				–	(468)	800	332
Profit after tax				**59,535**	**15,029**	**8,130**	**82,694**

Year ended 31 December 2012	CA £000	S&P £000	UK Total £000	Movestic £000	Other Group Activities £000	Total £000
Covered business						
New business contribution	339	(33)	306	2,596	–	2,902
Return from in-force business						
Expected return	2,308	274	2,582	3,290	–	5,872
Experience variances	5,194	3,029	8,223	(7,855)	–	368
Operating assumption changes	(335)	(2,858)	(3,193)	5,176	–	1,983
Return on shareholder net worth	859	7,048	7,907	–	–	7,907
Operating profit of covered business	**8,365**	**7,460**	**15,825**	**3,207**	–	**19,032**
Variation from longer-term investment return	8,864	10,967	19,831	8,204	–	28,035
Effect of economic assumption changes	(4,106)	(2,713)	(6,819)	315	–	(6,504)
Profit of covered business before tax	**13,123**	**15,714**	**28,837**	**11,726**	–	**40,563**
Tax thereon			(5,990)	–	–	(5,990)
Profit of covered business after tax			**22,847**	**11,726**	–	**34,573**
Results of non-covered business and of other group companies						
Profit/(loss) before tax			–	1,299	(5,745)	(4,446)
Tax			–	(295)	1,423	1,128
Profit/(loss) after tax			**22,847**	**12,730**	**(4,322)**	**31,255**

The results of the non-covered business and of other group companies before tax and before exceptional item are presented as 'other operational result' in the consolidated income statement.

7 Sensitivities to alternative assumptions

The following tables show the sensitivity of the embedded value as reported at 31 December 2013, and of the new business contribution of Movestic, to variations in the assumptions adopted in the calculation of the embedded value. Sensitivity analysis is not provided in respect of the new business contribution of CA for the year ended 31 December 2013 as the reported level of new business contribution is not considered to be material (see Note 3(a)).

	Embedded value						New business contribution
	UK business					Swedish business	Swedish business
	CA Pre-tax £m	S&P Pre-tax £m	PL Pre-tax £m	Tax £m	UK Post-tax £m	Post-tax £m	£m
Published value as at 31 December 2013	**147.9**	**106.5**	**64.8**	**(21.9)**	**297.3**	**115.4**	**5.2**
Changes in embedded value/new business contribution arising from:							
Economic sensitivities							
100 basis point increase in yield curve	(4.3)	12.7	(3.3)	(2.1)	3.0	0.7	(0.2)
100 basis point reduction in yield curve	4.9	(12.6)	3.6	0.6	(3.5)	(0.6)	0.2
10% decrease in equity and property values	(12.1)	(12.5)	–	4.3	(20.3)	(11.7)	(0.1)
Operating sensitivities							
10% decrease in maintenance expenses	2.6	4.5	1.3	(0.8)	7.6	6.3	0.7
10% decrease in lapse rates	2.3	(0.3)	0.4	(0.2)	2.2	8.7	1.3
5% decrease in mortality/morbidity rates:							
Assurances	0.8	0.7	1.5	(0.5)	2.5	0.1	–
Annuities	(1.7)	(0.3)	n/a	–	(2.0)	n/a	n/a
Reduction in the required capital to statutory minimum	0.4	0.7	1.3	(0.3)	2.1	0.0	–

The key assumption changes represented by each of these sensitivities are as follows:

Economic sensitivities

(i) 100 basis point increase in the yield curve: The reference rate is increased by 1% and the rate of future inflation has also been increased by 1% so that real yields remain constant;

(ii) 100 basis point reduction in the yield curve: The reference rate is reduced by 1% (with a minimum of zero to avoid negative yields where relevant) and the rate of future inflation has also been reduced by 1% so that real yields remain constant; and

(iii) 10% decrease in the equity and property values. This gives rise to a situation where, for example, a Managed Fund unit liability with a 60% equity holding would reduce by 6% in value.

Operating sensitivities

(i) 10% decrease in maintenance expenses, giving rise to, for example, a base assumption of £20 per policy pa reducing to £18 per policy pa;

(ii) 10% decrease in persistency rates giving rise to, for example, a base assumption of 10% of policy base lapsing pa reducing to 9% pa;

(iii) 5% decrease in mortality/morbidity rates giving rise to, for example, a base assumption of 95% of the parameters in a selected mortality/morbidity table reducing to 90.25% of the parameters in the same table, assuming no changes are made to policyholder charges or any other management actions; and

(iv) the sensitivity to the reduction in the required capital to the statutory minimum shows the effect of reducing the required capital from that defined in Note 3(b) to the minimum requirement prescribed by regulation.

In each sensitivity calculation all other assumptions remain unchanged except where they are directly affected by the revised economic conditions: for example, as stated, changes in interest rates will directly affect the reference rate.

NOTES TO THE EEV SUPPLEMENTARY INFORMATION (CONTINUED)

8 Reconciliation of shareholders' equity on the IFRS basis to shareholders' equity on the EEV

31 December 2013	CA £000	S&P £000	PL £000	Movestic £000	Other Group Activities £000	Total £000
Shareholders' equity on the IFRS basis	**74,994**	**93,863**	**55,276**	**61,431**	**(38,462)**	**247,102**
Reclassifications						
Debt finance	–	(29,699)	(43,341)	–	73,040	–
Other	(258)	–	–	–	258	–
Adjustments						
Deferred acquisition costs	(4,026)	–	–	(23,264)	–	(27,290)
Deferred income	7,261	–	–	–	–	7,261
Adjustment to provisions on investment contracts, net of amounts deposited with reinsurers	(11,020)	–	–	–	–	(11,020)
Adjustments to provisions on insurance contracts, net of reinsurers' share	33	(12,697)	–	–	–	(12,664)
Acquired in-force value	(9,751)	(5,172)	(16,034)	(49,873)	–	(80,830)
Acquired value of customer relationships	–	–	–	(1,164)	–	(1,164)
Software assets	–	–	–	(5,004)	–	(5,004)
Adjustment to borrowings	–	–	–	(5,913)	–	(5,913)
Deferred tax	1,623	–	–	2,108	–	3,731
Shareholder net worth	**58,856**	**46,295**	**(4,099)**	**(21,679)**	**34,836**	**114,209**
Value of in-force business	67,171	30,482	25,507	139,001	–	262,161
Shareholders' equity on the EEV	**126,027**	**76,777**	**21,408**	**117,322**	**34,836**	**376,370**
Shareholder net worth comprises:						
Shareholder net worth in regulated entities	58,856	75,994	39,242	(23,573)	–	150,519
Shareholders' net equity in other Group companies	–	–	–	1,894	34,836	36,730
Debt finance	–	(29,699)	(43,341)	–	–	(73,040)
Total	**58,856**	**46,295**	**(4,099)**	**(21,679)**	**34,836**	**114,209**

31 December 2012

	CA £000	S&P £000	Movestic £000	Other Group Activities £000	Total £000
Shareholders' equity on the IFRS basis	**86,498**	**75,570**	**58,078**	**(1,800)**	**218,346**
Reclassifications					
Debt finance	–	(29,662)	–	29,662	–
Other	(253)	–	–	253	–
Adjustments					
Deferred acquisition costs	(4,631)	–	(17,000)	–	(21,631)
Deferred income	8,214	–	–	–	8,214
Adjustment to provisions on investment contracts, net of amounts deposited with reinsurers	(11,451)	–	–	–	(11,451)
Adjustments to provisions on insurance contracts, net of reinsurers' share	(40)	(7,051)	–	–	(7,091)
Acquired in-force value	(11,403)	(5,574)	(54,286)	–	(71,263)
Acquired value of customer relationships	–	–	(1,322)	–	(1,322)
Software assets	–	–	(5,712)	–	(5,712)
Adjustment to borrowings	–	–	(7,049)	–	(7,049)
Deferred tax	(2,437)	–	2,461	–	24
Shareholder net worth	**64,497**	**33,283**	**(24,830)**	**28,115**	**101,065**
Value of in-force business	67,040	18,537	124,503	–	210,080
Shareholders' equity on the EEV	**131,537**	**51,820**	**99,673**	**28,115**	**311,145**
Shareholder net worth comprises:					
Shareholder net worth in regulated entities	64,497	62,945	(26,417)	–	101,025
Shareholders' net equity in other Group companies	–	–	1,587	28,115	29,702
Debt finance	–	(29,662)	–	–	(29,662)
Total	**64,497**	**33,283**	**(24,830)**	**28,115**	**101,065**

9 Profit recognised on business combination

An EEV profit has arisen as a result of the purchase of 100% of the share capital of Protection Life Company Limited on 28 November 2013. The profit has been measured as the difference between the purchase consideration of £39,300,000 and the European Embedded Value of Protection Life at the purchase date, being £51,583,000, which was established in accordance with the methodology set out in Notes 2 to 4 of the EEV supplementary financial information.

10 Earnings per share

Year ended 31 December	2013 p	2012 p
Basic earnings per share		
Based on profit for the year	75.55	30.33
Based on profit for the year before exceptional item	72.00	27.21
Diluted earnings per share		
Based on profit for the year	75.55	30.33
Based on profit for the year before exceptional item	72.00	27.21

11 Foreign exchange translation reserve

A foreign exchange translation reserve arises on the translation of the financial statements of Movestic, the functional currency of which is the Swedish Krona, into pounds sterling, which is the presentational currency of the Group financial statements. Items in the consolidated income statement are translated at the average exchange rate of SEK10.1901 = £1 ruling in the year ended 31 December 2013 (year ended 31 December 2012: SEK10.7326 = £1), while all items in the balance sheet are stated at the closing rates ruling at the reported balance sheet date, being SEK10.5919 = £1 at 31 December 2013 (SEK10.5247 = £1 at 31 December 2012). The differences arising on translation using this methodology are recognised directly in shareholders' equity within the foreign exchange translation reserve.

The reported embedded value is sensitive to movements in the SEK: £ exchange rate. Had the exchange rate as at 31 December 2013 been 10% higher at SEK11.6511 = £1, then the reported embedded value of £376.4m as at 31 December 2013 would have been reported as £364.9m.

SECTION F

ADDITIONAL INFORMATION

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FINANCIAL CALENDAR

28 March 2014
Results for the year ended 31 December 2013 announced

9 April 2014
Ex dividend date

11 April 2014
Dividend record date

14 April 2014
Published Financial Statements issued to shareholders

16 May 2014
Annual General Meeting

19 May 2014
Interim Management Statement for the quarter ending 31 March 2014

22 May 2014
Dividend payment date

29 August 2014
Interim results for the 6 months ending 30 June 2014 announced

19 November 2014
Interim Management Statement for the quarter ending 30 September 2014 announced

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Auditor
Deloitte LLP
Chartered Accountants and Statutory Auditor
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NOTICE OF ANNUAL GENERAL MEETING

This document is important and requires your immediate attention

If you are in any doubt as to the action you should take, you should immediately consult your stockbroker, bank manager, solicitor, accountant or other independent professional adviser authorised under the Financial Services and Markets Act 2000 if you are resident in the United Kingdom or, if you reside elsewhere, another appropriately authorised financial adviser.

If you have sold or otherwise transferred all of your shares in Chesnara plc please pass this document together with the accompanying proxy form as soon as possible to the purchaser or transferee, or to the person who arranged the sale or transfer so they can pass these documents to the person who now holds the shares.

Company No. 4947166

Chesnara plc
Notice is given that the 2014 Annual General Meeting of Chesnara plc will be held at the offices of Panmure Gordon (UK) Limited, One New Change, London EC4M 9AF on 16 May 2014 at 11am. for the business set out below. Resolutions 1 to 14 inclusive will be proposed as ordinary resolutions and resolutions 16 to 18 inclusive will be proposed as special resolutions.

1. To receive and adopt the audited accounts for the financial year ended 31 December 2013, together with the reports of the directors and auditor thereon.

2. To declare a final dividend of 11.63 pence per share for the financial year ended 31 December 2013.

3. To approve the directors' remuneration report (other than the part of it which contains the directors' remuneration policy) for the year ended 31 December 2013.

4. To approve the directors' remuneration policy report (as contained in the directors' remuneration report for the year ended 31 December 2013).

5. To re-elect Peter Mason as a director (who retires by rotation in accordance with the Company's articles of association).

6. To re-elect Veronica France as a director.

7. To re-elect David Brand as a director.

8. To re-elect Mike Evans as a director.

9. To re-elect Peter Wright as a director.

10. To reappoint Deloitte LLP as auditor of the Company to hold office until the conclusion of the next general meeting of the Company at which accounts are laid before shareholders.

11. To authorise the directors to fix the auditor's remuneration.

12. That, from the passing of this resolution until the earlier of 15 November 2015 and the conclusion of the Company's next Annual General Meeting, the Company and all companies which are its subsidiaries at any time during such period are authorised:

(a) to make donations to political parties or independent election candidates;

(b) to make donations to political organisations other than political parties; and

(c) to incur political expenditure

up to an aggregate total amount of £100,000, with the individual amount authorised for each of heads (a) to (c) above being limited to £100,000. Any such amounts may comprise sums paid or incurred in one or more currencies. Any sum paid or incurred in a currency other than sterling shall be converted into sterling at such rate as the board may decide is appropriate. Terms used in this resolution have, where applicable, the meanings that they have in Part 14 of the Companies Act 2006.

13. That:

(a) the rules of the Chesnara 2014 Short-Term Incentive scheme (the "2014 STI Scheme"), a copy of which is produced to the meeting and initialled by the Chairman of the meeting for the purposes of identification, be and are hereby approved and adopted and the Directors of the Company be and are hereby authorised to do all such things in accordance with applicable law as may be necessary or desirable to carry the 2014 STI Scheme into effect; and

(b) the Directors of the Company be and are hereby also authorised to adopt further schemes based on the 2014 STI Scheme but modified to take account of local tax, exchange control or securities law in overseas territories, provided that any shares made available under such further schemes are treated as counting against any limits on individual or overall participation in the 2014 STI Scheme.

14. That:

(a) the rules of the Chesnara 2014 Long-Term Incentive scheme (the "2014 LTI Scheme"), a copy of which is produced to the meeting and initialled by the Chairman of the meeting for the purposes of identification, be and are hereby approved and adopted and the Directors of the Company be and are hereby authorised to do all such things in accordance with applicable law as may be necessary or desirable to carry the 2014 LTI Scheme into effect; and

(b) the Directors of the Company be and are hereby also authorised to adopt further schemes based on the 2014 LTI Scheme but modified to take account of local tax, exchange control or securities law in overseas territories, provided that any shares made available under such further schemes are treated as counting against any limits on individual or overall participation in the 2014 LTI Scheme.

15. That the directors be and they are hereby generally and unconditionally authorised in accordance with section 551 of the Companies Act 2006 to exercise all powers of the Company to allot shares in the Company and to grant rights to subscribe for or to convert any security into such shares ("Allotment Rights"), but so that:

(a) the maximum amount of shares that may be allotted or made the subject of Allotment Rights under this authority are shares with an aggregate nominal value of £3,828,066, of which:

(i) half may be allotted or made the subject of Allotment Rights in any circumstances; and

(ii) the other half may be allotted or made the subject of Allotment Rights pursuant to any rights issue (as referred to in the Financial Conduct Authority's listing rules) or pursuant to any arrangements made for the placing or underwriting or other allocation of any shares or other securities included in, but not taken up under, such rights issue;

(b) this authority shall expire 18 months after the passing of this resolution or, if earlier, on the date of the Company's next Annual General Meeting;

(c) the Company may make any offer or agreement before such expiry which would or might require shares to be allotted or Allotment Rights to be granted after such expiry; and

(d) all authorities vested in the directors on the date of the notice of this meeting to allot shares or to grant Allotment Rights that remain unexercised at the commencement of this meeting are revoked.

16. That, subject to the passing of the resolution numbered 14 in the notice convening this meeting, the directors be and they are hereby empowered, pursuant to sections 570 and 573 of the Companies Act 2006, to allot equity securities (as defined in section 560 of that Act) pursuant to the authority conferred on them by the foregoing resolution numbered 15 in the notice of this meeting or by way of a sale of treasury shares as if section 561 of that Act did not apply to such allotment or sale, provided that this power shall be limited to:

(a) the allotment of equity securities or sale of treasury shares in connection with any rights issue or open offer (each as referred to in the Financial Conduct Authority's listing rules) or any other pre-emptive offer that is open for acceptance for a period determined by the directors to the holders of ordinary shares on the register on any fixed record date in proportion to their holdings of ordinary shares (and, if applicable, to the holders of any other class of equity security in accordance with the rights attached to such class), subject, in each case, to such exclusions or other arrangements as the directors may deem necessary or appropriate in relation to fractions of such securities, the use of more than one currency for making payments in respect of such offer, any such shares or other securities being represented by depositary receipts, treasury shares, any legal or practical problems in relation to any territory or the requirements of any regulatory body or any stock exchange; and

(b) the allotment of equity securities or sale of treasury shares for cash (otherwise than as mentioned in sub-paragraph (a) above), provided that the maximum aggregate nominal value of equity securities allotted and treasury shares sold does not exceed £287,618,

and shall expire 18 months after the passing of this resolution or, if earlier, on the date of the Company's next Annual General Meeting save that, before the expiry of this power, the Company may make any offer or agreement which would or might require equity securities to be allotted and/or treasury shares to be sold after such expiry.

17. That the Company be and is hereby generally and unconditionally authorised for the purposes of section 701 of the Companies Act 2006 to make one or more market purchases (as defined in section 693 of that Act) of ordinary shares of 5p each in the capital of the Company, provided that:

(a) the maximum aggregate number of ordinary shares hereby authorised to be purchased is 11,485,347;

(b) the minimum price (exclusive of expenses) which may be paid for such ordinary shares is 5p per share;

(c) the maximum price (exclusive of expenses) which may be paid for such ordinary shares is the maximum price permitted under the Financial Conduct Authority's listing rules or, in the case of a tender offer (as referred to in those rules), 5% above the average of the middle market quotations for those shares (as derived from the Daily Official List of London Stock Exchange plc) for the five business days immediately preceding the date on which the terms of the tender offer are announced;

(d) the authority hereby conferred shall expire 18 months after the passing of this resolution or, if earlier, on the date of the Company's next Annual General Meeting; and

(e) the Company may make a contract or contracts to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority which will or may be completed wholly or partly after the expiry of such authority, and may make a purchase of ordinary shares in pursuance of any such contract or contracts.

18. That a general meeting of the Company (other than an Annual General Meeting) may be called on not less than 14 clear days' notice.

By order of the Board

Mary Fishwick
Company Secretary

Registered office:
Harbour House
Portway
Preston
Lancashire
PR2 2PR

27 March 2014

NOTES

1. Any member who is entitled to attend and vote at this Annual General Meeting is entitled to appoint another person, or two or more persons in respect of different shares held by him, as his proxy to exercise all or any of his rights to attend and to speak and to vote at the Annual General Meeting.

2. A member wishing to attend and vote at the Annual General Meeting in person should arrive prior to the time fixed for its commencement. A member that is a corporation can only attend and vote at the Annual General Meeting in person through one or more representatives appointed in accordance with section 323 of the Companies Act 2006. Any such representative should bring to the Annual General Meeting written evidence of his appointment, such as a certified copy of a board resolution of, or a letter from, the corporation concerned confirming the appointment. Any member wishing to vote at the Annual General Meeting without attending in person or (in the case of a corporation) through its duly appointed representative must appoint a proxy to do so. A proxy need not be a member of the Company. A form of proxy for this Annual General Meeting is enclosed and, in order to be valid, must be completed in accordance with the instructions that accompany it and then be delivered by hand only (together with any power of attorney or other authority under which it is signed, or a certified copy of such item), to the Company's Registrars, Capita Asset Services at, 34 Beckenham Road, Beckenham, Kent, BR3 4TU or by post to Business Reply Plus Licence No RLUB-TBUX-EGUC, PXS 1, 34 Beckenham Road, Beckenham, Kent, BR3 4ZF by 11am. on Wednesday 14 May 2014. Alternatively, members may appoint a proxy online by following the instructions for the electronic appointment of a proxy at www.capitashareportal.com, by entering the company name "Chesnara plc" and following the on screen instructions. To be a valid proxy appointment, the member's electronic message confirming the details of the appointment completed in accordance with those instructions must be transmitted so as to be received by the same time. Members who hold their shares in uncertificated form may also use the "CREST" voting service to appoint a proxy electronically, as explained below. The appointment of a proxy will not preclude a member from attending and voting at the Annual General Meeting.

3. CREST members who wish to appoint one or more proxies through the CREST system may do so by using the procedures described in "the CREST voting service" section of the CREST Manual. CREST personal members or other CREST sponsored members, and those CREST members who have appointed one or more voting service providers, should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf. In order for a proxy appointment or a proxy instruction made using the CREST voting service to be valid, the appropriate CREST message (a "CREST proxy appointment instruction") must be properly authenticated in accordance with the specifications of CREST's operator, Euroclear UK & Ireland Limited ("Euroclear"), and must contain all the relevant information required by the CREST Manual. To be valid, the message (regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy) must be transmitted so as to be received by Capita Asset Services (ID RA10), by 6pm. on Wednesday 14 May 2014, which is acting as the Company's "issuer's agent". After this time, any change of instruction to a proxy appointed through the CREST system should be communicated to the appointee through other means. The time of the message's receipt will be taken to be when (as determined by the timestamp applied by the CREST Applications Host) the issuer's agent is first able to retrieve it by enquiry through the CREST system in the prescribed manner. Euroclear does not make available special procedures in the CREST system for transmitting any particular message. Normal system timings and limitations apply in relation to the input of CREST proxy appointment instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member or a CREST sponsored member or has appointed any voting service provider(s), to procure that his CREST sponsor or voting service provider(s) take(s)) such action as is necessary to ensure that a message is transmitted by means of the CREST system by any particular time. CREST members and, where applicable, their CREST sponsors or voting service providers should take into account the provisions of the CREST Manual concerning timings as well as its section on "Practical limitations of the system". In certain circumstances, the Company may, in accordance with the Uncertificated Securities Regulations 2001 or the CREST Manual, treat a CREST proxy appointment instruction as invalid.

4. Copies of Directors' service contracts and letters of appointment are available for inspection at the registered office of the Company during normal business hours each business day. They will also be available for inspection at the Annual General Meeting for at least 15 minutes prior to and during the Annual General Meeting.

5. Copies of the rules of the Chesnara 2014 Short-Term Incentive scheme and the Chesnara 2014 Long-Term Incentive scheme will be available for inspection at the registered offices of the Company and at the place of the Annual General Meeting during normal business hours each business day from the date of this notice until the conclusion of the Annual General Meeting.

6. The time by which a person must be entered on the register of members in order to have the right to attend and vote at the Annual General Meeting (and for the purpose of the determination by the Company of the votes they may cast) is 6.00pm. on Wednesday 14 May 2014. Changes to entries on the register of members after that time will be disregarded in determining the right of any person to attend or vote at the Annual General Meeting.

7. The right to appoint proxies does not apply to persons nominated to receive information rights under section 146 of the Companies Act 2006, as such rights can only be exercised by the member concerned. Any person nominated to enjoy information rights under section 146 of the Companies Act 2006 who has been sent a copy of this notice of Annual General Meeting is hereby informed, in accordance with section 149(2) of the Companies Act 2006, that they may have a right under an agreement with the registered member by whom they were nominated to be appointed, or to have someone else appointed, as a proxy for this Annual General Meeting. If they have no such right, or do not wish to exercise it, they may have a right under such an agreement to give instructions to the member as to the exercise of voting rights. Nominated persons should contact the registered member by whom they were nominated in respect of these arrangements.

8. As at 27 March 2014 (being the last practicable date prior to the publication of this document), the Company's issued share capital consisted of 115,047,662 ordinary shares, carrying one vote each. The total voting rights in the Company as at 27 March 2014 (being the last practicable date prior to the publication of this document) were 114,853,479.

9. Information regarding this Annual General Meeting, including information required by section 311A of the Companies Act 2006, is available at **www.chesnara.co.uk**. Any electronic address provided either in this notice or any related documents (including the proxy appointment form) may not be used to communicate with the Company for any purposes other than those expressly stated.

10. In accordance with section 319A of the Companies Act 2006, any member attending the Annual General Meeting has the right to ask questions. The Company must cause to be answered any such question relating to the business being dealt with at the Annual General Meeting, but no such answer need be given if (a) to do so would interfere unduly with the preparations for the Annual General Meeting or involve the disclosure of confidential information, (b) the answer has already been given on a website in the form of an answer to a question or (c) it is undesirable in the interests of the Company or the good order of the Annual General Meeting that the question be answered.

11. Under section 527 of the Companies Act 2006, members meeting the threshold requirements set out in that section have the right to require the Company to publish on a website a statement in accordance with section 528 of the Companies Act 2006 setting out any matter relating to (i) the audit of the Company's accounts (including the auditor's report and the conduct of the audit) that are to be laid before the Annual General Meeting or (ii) any circumstances connected with an auditor of the Company ceasing to hold office since the previous meeting at which annual accounts and reports were laid in accordance with section 437 of the Companies Act 2006. The Company may not require the members requesting any such website publication to pay its expenses in complying with sections 527 or 528 of the Companies Act 2006. Where the Company is required to place a statement on a website under section 527 of the Companies Act 2006, it must forward the statement to the Company's auditor not later than the time when it makes the statement available on the website. The business which may be dealt with at the Annual General Meeting includes any statement that the Company has been required under section 527 of the Companies Act 2006 to publish on a website

EXPLANATORY NOTES TO THE NOTICE OF ANNUAL GENERAL MEETING

The notes on the following pages give an explanation of the proposed resolutions:

Resolution 1:

Report and accounts
The Companies Act 2006 requires the directors of a public company to lay its annual report and accounts before the company in general meeting, giving shareholders the opportunity to ask questions on the contents. The annual report and accounts comprise the audited financial statements, the auditor's report, the directors' report, the directors' remuneration report and, for the first time this year, the directors' strategic report. In accordance with the UK Corporate Governance Code, the Company proposes, as an ordinary resolution, a resolution on its annual report and accounts for the year ended 31 December 2013.

Resolution 2:

Final dividend
The payment of the final dividend requires the approval of shareholders in general meeting. If the Annual General Meeting approves resolution 2, the final dividend of 11.63 pence per share will be paid on 22 May 2014 to ordinary shareholders who are on the register of members at the close of business on 11 April 2014 in respect of each ordinary share.

Resolution 3:

Approval of the directors' remuneration report
In accordance with the Companies Act 2006, the Company proposes an ordinary resolution to approve the directors' remuneration report for the financial year ended 31 December 2013. The directors' remuneration report can be found on pages 60 to 81 of the 2013 Report & Accounts and, for the purposes of this resolution, does not include the parts of the directors' remuneration report containing the Directors' Remuneration Policy Report set out on pages 63 to 72. The vote on this resolution is advisory only and the directors' entitlement to remuneration is not conditional on it being passed.

Resolution 4:

Approval of the Directors' Remuneration Policy Report
For the first time this year, and in accordance with the Companies Act 2006, the Company proposes an ordinary resolution to approve the directors' remuneration policy report contained in the directors' remuneration report. The Remuneration Policy Report is set out on pages 63 to 72 of the 2013 Report & Accounts. The vote on this resolution is binding and, if passed, will mean that the directors can only make remuneration payments in accordance with the approved policy. The Company is required to ensure that a vote on its remuneration policy takes place annually unless the approved policy remains unchanged, in which case the Company will propose a similar resolution at least every three years.

Resolutions 5 – 9 inclusive:

Re-election of directors
Under the Company's articles of association, one third of the directors must retire by rotation at each Annual General Meeting and no director may serve beyond three years without being re-elected by shareholders. Accordingly, Peter Mason will retire at the 2014 Annual General Meeting. In accordance with its view of best practice, the Board of Directors has decided that, in addition, all of the Non-Executive Directors will retire at every Annual General Meeting. As a result, Veronica France, David Brand, Mike Evans and Peter Wright will also retire at the 2014 Annual General Meeting.

Peter Mason, Veronica France, David Brand, Mike Evans and Peter Wright are all put forward by the Board of Directors for re-election at the 2014 Annual General Meeting. Brief biographical details of each of them can be found on page 53 of this document. The Chairman confirms that, following formal performance evaluation of these Directors by the board, they continue to be effective and demonstrate commitment to the role. The remaining directors therefore unanimously recommend that each of these directors be re-elected as a director of the Company.

Resolutions 10 and 11:

Re-appointment and remuneration of auditors
The Company is required to appoint an auditor, at each general meeting before which accounts are laid, to hold office until the end of the next such meeting. Deloitte LLP has indicated that it is willing to continue to act as the Company's auditor. You are asked to re-appoint Deloitte LLP and, following normal practice, to authorise the directors to determine its remuneration. The directors recommend its appointment.

Resolution 12:

Political donations
It has always been the Company's policy that it does not make political donations. This remains the Company's policy.

Part 14 of the Companies Act 2006 imposes restrictions on companies making political donations to any political party or other political organisation or to any independent election candidate unless they have been authorised to make donations at a general meeting of the Company. Whilst the Company has no intention of making such political donations, that Act includes broad and ambiguous definitions of the terms "political donation" and "political expenditure" which may apply to some normal business activities which would not generally be considered to be political in nature.

The directors therefore consider that, as a purely precautionary measure, it would be prudent to obtain the approval of the shareholders to make donations to political parties, political organisations and independent election candidates and to incur political expenditure up to the specified limit. The directors intend to seek renewal of this approval at future Annual General Meetings, but wish to emphasise that the proposed resolution is a precautionary measure for the above reason and that they have no intention of making any political donations or entering into party political activities.

Resolutions 13 and 14

Approval of Incentive Schemes

These resolutions seek to approve the introduction of the Chesnara 2014 Short-Term Incentive scheme (the "2014 STI Scheme") and the Chesnara 2014 Long-Term Incentive scheme (the "2014 LTI Scheme"), which are intended to replace the Company's current annual bonus scheme and its long term incentive plan (the Chesnara 2012 Long-Term Incentive Plan (the "2012 LTIP")).

A summary of the background to the 2014 STI Scheme and the 2014 LTI Scheme and the key terms of initial awards which are intended to be made under those schemes shortly following the AGM (which are also described in the directors' remuneration policy which is being put to shareholders as Resolution 4, subject to their approval by shareholders, is set out below:

- Under the current annual bonus scheme, payments are made in cash with no deferral, and awards under the 2012 LTIP pay out in cash after three years. There is a combined limit of 100% of salary across the two schemes, with the amount of awards under the 2012 LTIP being reduced to the extent that payments are made under the annual bonus scheme.
- The performance target for the annual bonus scheme is based on the adjusted IFRS pre-tax profit of the Company, while that of the 2012 LTIP is based on the Group European embedded value ("EEV") for a financial year and then reflects the share price performance of the Company over three years as against the Group EEV.
- The Remuneration Committee of the board (the "Committee") has reviewed the current arrangements and now proposes that they are replaced by the 2014 STI Scheme and the 2014 LTI Scheme as these will provide a more appropriate incentive arrangement for the Executive Directors.
- The 2014 STI Scheme is intended to replace the annual bonus scheme and will provide for the mandatory deferral of a proportion of payments into shares which will vest after a three year deferral period. For the initial awards under the 2014 STI Scheme, provided that the amount due is at least £20,000, this proportion will be 35%.
- The initial awards under the 2014 STI Scheme will be subject to a combination of stretching performance targets which will be assessed over the 2014 financial year, being 50% adjusted IFRS pre-tax profit, 30% Group EEV operating profit adjusted for dividend payments and 20% Group strategic objectives (for instance, those related to the delivery of major corporate projects). The Committee believes that the combination of performance targets will provide a more balanced measure of performance than the previous use of a single target (IFRS pre-tax profit target). The exact performance targets are commercially sensitive and therefore will only be disclosed, along with the extent of vesting, in the year that the cash element of awards is paid.
- The 2014 LTI Scheme is intended to replace the 2012 LTIP and will provide for awards to be made over shares in the Company, which will vest subject to performance over a three year period.
- The initial awards under the 2014 LTI Scheme will be subject to a combination of performance targets, being 50% relative TSR against the FTSE 350 High Yield Index and 50% Group EEV adjusted for dividend payments. The Committee has selected these targets to provide a balance between relative and absolute measures, and continues to believe that Group EEV remains the key measure for the long term growth of the business.
- The individual limits for the initial awards made under each of the new schemes will be 75% of salary.
- Awards under the 2014 STI Scheme and the 2014 LTI Scheme will be subject to malus provisions which will reduce the number of shares or cash amounts payable on vesting in circumstances including a material misstatement of the Company's results, regulatory breach or gross misconduct on the part of the participant.

The principal features of the 2014 STI Scheme and the 2014 LTI Scheme are summarised in Appendix 1 to these notes.

Resolution 15

Power to allot shares

The directors are currently authorised to allot shares and to grant rights to subscribe for or to convert any security into shares of the Company, but their authorisation ends on the date of this year's Annual General Meeting. This resolution seeks to renew the directors' authority to allot shares.

The Association of British Insurers ("ABI") has published guidance to the effect that ABI members will regard as routine a request for authorisation to allot new shares in an amount of up to one third of the existing issued share capital and additionally that they will regard as routine requests to authorise the allotment of a further one third, provided that such additional authority is applied to fully pre-emptive rights issues only and the authorisation is valid for one year only.

This authority was conferred on the directors at last year's Annual General Meeting and the directors recommend that the Company should have this additional headroom this year. This authority is limited to a maximum nominal amount of £3,828,066 (representing 76,561,320 ordinary shares), which represents approximately two thirds in aggregate of the total ordinary share capital in issue (excluding treasury shares) as at 27 March 2014 (being the latest practicable date prior to the publication of this document). Of this amount, 38,280,660 ordinary shares (representing approximately one third in aggregate of the total ordinary share capital in issue, excluding treasury shares) can only be allotted pursuant to a rights issue.

As at 27 March 2014 (being the latest practicable date prior to the publication of this document), the Company held 194,183 treasury shares, being approximately 0.17% of the total ordinary share capital in issue (calculated exclusive of treasury shares).

The renewed authority will expire 18 months after the passing of this resolution or, if earlier, on the date of the next Annual General Meeting.

The directors have no present intention of exercising this authority. The purpose of giving the directors this authority is to maintain the Company's flexibility to take advantage of any appropriate opportunities that may arise.

EXPLANATORY NOTES TO THE NOTICE OF ANNUAL GENERAL MEETING (CONTINUED)

Resolution 16

Disapplication of pre-emption rights
This resolution, which will be proposed as a special resolution, seeks to renew the authority conferred on the Directors at last year's Annual General Meeting to issue equity securities or sell treasury shares for cash without first offering them to existing shareholders in proportion to their existing shareholdings. Other than in connection with a rights or other similar issue or scrip dividend (where difficulties arise in offering shares to certain overseas shareholders and in relation to fractional entitlements), the authority contained in this resolution will be limited to an aggregate nominal value of £287,618 (representing 5,752,360 ordinary shares), which represents approximately 5% of the Company's issued equity share capital as at 27 March 2014 (being the latest practicable date prior to the publication of this document). The renewed authority will expire 18 months after the passing of this resolution or, if earlier, on the date of the of the next Annual General Meeting. This is a standard resolution for most UK listed companies each year.

In accordance with the Statement of Principles on disapplying pre-emption rights issued in July 2008 by the Pre-Emption Group (which is supported by the Association of British Insurers, the National Association of Pension Funds Limited and the Investment Managers Association), the board confirms its intention that no more than 7.5% of the issued share capital will be issued or sold for cash on a non pre-emptive basis during any rolling three year period. The Directors have no present intention of exercising this authority.

Resolution 17:

Authority to purchase own shares
This resolution, which will be proposed as a special resolution, is to renew the authority granted to the Directors at last year's Annual General Meeting, which expires on the date of this year's Annual General Meeting, and to give the Company authority to buy back its own ordinary shares in the market as permitted by the Companies Act 2006. The authority limits the number of shares that can be purchased to a maximum of 11,485,347 (representing 10% of the issued ordinary share capital of the Company (excluding treasury shares) as at 27 March 2014 (being the latest practicable date prior to the publication of this document) and sets the minimum and maximum prices. This authority will expire no later than 18 months after the date of the Annual General Meeting.

Your Directors believe that the Company should continue to have the authority to purchase its own shares. The authority will be exercised only if the Directors believe that to do so would result in an increase in earnings per share and would promote the success of the Company for the benefit of its shareholders generally. To the extent that any shares so purchased are held in treasury (see below), earnings per share will be enhanced until such time, if any, as such shares are resold or transferred out of treasury.

Any purchases of ordinary shares would be by means of market purchases through the London Stock Exchange.

Sections 724 – 732 inclusive of the Companies Act 2006 provide that shares held in treasury can be cancelled, sold for cash or, in appropriate circumstances, used to meet obligations under employee share schemes. Any shares held in treasury would not be eligible to vote nor would any dividend be paid on any such shares. If any ordinary shares purchased pursuant to this authority are not held by the Company as treasury shares, then such shares would be immediately cancelled, in which event the number of ordinary shares in issue would be reduced.

The Directors believe that it continues to be desirable for the Company to have this choice. Holding the repurchased shares as treasury shares gives the Company the ability to re-issue them quickly and cost effectively and provides the Company with additional flexibility in the management of its capital base. No dividends will be paid on, and no voting rights will be exercised in respect of, treasury shares. In 2013, 4,828 shares were transferred out of treasury to meet sharesave plan options.

Resolution 18:

Notice of general meetings
The Companies Act 2006 requires the notice period for general meetings of the Company to be at least 21 days, but, as a result of a resolution which was passed by the Company's shareholders at last year's Annual General Meeting, the Company is currently able to call general meetings (other than an Annual General Meeting) on not less than 14 clear days' notice. In order to preserve this ability, shareholders must approve the calling of meetings on not less than 14 clear days' notice. Resolution 18 seeks such approval. The approval will be effective until the Company's next Annual General Meeting, when it is intended that a similar resolution will be proposed. The Company will also need to meet the requirements for electronic voting under the Companies (Shareholders' Rights) Regulations 2009 before it can call a general meeting on less than 21 days' notice.

The shorter notice period would not be used as a matter of routine for general meetings, but only where the flexibility is merited by the business of the meeting and is thought to be to the advantage of shareholders as a whole.

The Directors recommend all shareholders to vote in favour of all of the above resolutions, as the Directors intend to do in respect of their own shares, and consider that they are in the best interests of the Company and its shareholders as a whole.

APPENDIX 1 – SCHEME SUMMARIES

Summaries of the principal features of the Chesnara 2014 Short-Term Incentive scheme (the "2014 STI Scheme") and the Chesnara 2014 Long-Term Incentive scheme (the "2014 LTI Scheme")

The 2014 STI Scheme

Introduction
The 2014 STI Scheme comprises a discretionary annual incentive scheme together with provisions for the mandatory deferral of a proportion of the cash amounts payable into shares, under which awards may be made to selected employees or directors of the Company or any of its subsidiaries (the "Group").

The Remuneration Committee of the board (the "Committee") will be responsible for the operation of the 2014 STI Scheme. Awards to receive a cash amount, subject to the achievement of a performance target (which may comprise a combination of separate targets) measured over a financial year ("Cash Awards") will be made to participants. Following the determination of the extent to which the performance target has been met, a proportion of the cash amount due under a Cash Award is deferred into shares (a "Deferred Share Award") which will vest at the end of a 3 year deferral period, subject to the participant's continued employment.

Deferred Share Awards made under the 2014 STI Scheme will normally be nil-cost options to acquire shares at no cost to the participant, although Deferred Share Awards may also be made as conditional share awards.

Deferred Share Awards may be satisfied by the issue of new shares or by the transfer of shares held in treasury or by the trustee of an employee benefit trust.

Awards under the 2014 STI Scheme are not pensionable.

Eligibility
A participant must be an employee or director of the Group at the time a Cash Award is made. Participation in the 2014 STI Scheme will be at the discretion of the Committee.

Individual limits
As stated in the directors' remuneration policy report which is being put to shareholders as Resolution 4, the maximum cash amount which may be payable under any Cash Award made during 2014 may not exceed 75% of the participant's salary. The Committee may specify another limit from time to time.

Performance targets
A Cash Award will be subject to a performance target which will be set by the Committee at the time the Cash Award is made and which must be satisfied before the Cash Award can vest.

The Committee may vary or waive the performance target applying to a Cash Award if an event occurs which causes the Committee to consider that the performance target is no longer appropriate, provided that such variation or waiver is reasonable in the circumstances and, except in the case of a waiver, produces a fairer measure of performance and is not materially less difficult to satisfy.

Leaving employment before a Cash Award vests
If a participant ceases to be employed within the Group for any reason before a Cash Award made to him vests then that Cash Award will lapse unless the Committee in its discretion determines that the participant may retain a time pro-rated proportion of the Cash Award (according to the proportion of the performance period which has then elapsed) and it shall continue to vest, if at all, in accordance with its original terms. Alternatively, the Committee may determine that a time pro-rated proportion of the Cash Award will vest immediately upon the cessation of employment, subject to the Committee's assessment of the extent to which the applicable performance target shall be deemed to be met at that time.

The Committee may vary the time pro-rating applied to allow a greater proportion of the Cash Award to vest. Where a participant's Cash Award vests following his cessation of employment, the whole of the amount due shall be paid in cash, with no deferral into a Deferred Share Award.

The Committee may vary the time pro-rating applied to allow a greater proportion of the Cash Award to vest. Where a participant's Cash Award vests following his cessation of employment, the whole of the amount due shall be paid in cash, with no deferral into a Deferred Share Award.

Deferral into shares
The Committee will determine the extent to which the performance target applicable to a Cash Award has been met following the end of the relevant financial year, and accordingly the cash amount payable under the Cash Award. Subject to any applicable minimum cash payment under the Cash Award, a proportion of the cash amount shall be deferred into a Deferred Share Award, with the number of shares subject to the Deferred Share Award being determined by reference the share price on the dealing day preceding the day on which the Deferred Share Award is made. For Cash Awards made in 2014, unless the cash amount payable is £20,000 or less, 35% of the cash amount shall be deferred into a Deferred Share Award, as set out in the directors' remuneration policy report.

APPENDIX 1 – SCHEME SUMMARIES (CONTINUED)

Making of Deferred Share Awards
Deferred Share Awards will be made as soon as practicable following the determination of the extent to which the performance target applicable to the relevant Cash Award has been met, subject to the Company being prevented from making awards over shares by restrictions on dealings in shares by Directors or employees of the Group imposed by statute, order, regulation, Government directive or by the Model Code or the Company's own code on dealings in its securities by Directors and employees. No payment will be required for the making of a Deferred Share Award and Deferred Share Awards are not transferable (except on death).

Dilution limits
A Deferred Share Award may not be made under the 2014 STI Scheme if it would cause the number of shares issued or issuable under any employee share scheme operated by the Company in the preceding 10 years to exceed 10% of the Company's issued ordinary share capital at that time.

In addition, a Deferred Share Award may not be made under the 2014 STI Scheme if it would cause the number of shares issued or issuable under any discretionary employee share scheme operated by the Company in the preceding 10 years to exceed 5% of the Company's issued ordinary share capital at that time.

The above limits exclude any share awards which lapse, as well as any share awards which are satisfied by the transfer of existing shares. However, for as long as is required by guidelines issued the Association of British Insurers, the transfer of treasury shares will be treated as an issue of new shares.

Vesting of Deferred Share Awards
Deferred Share Awards will normally vest 3 years after they are made. A Deferred Share Award which is a nil-cost option will lapse 10 years after the date on which it is made.

Malus
At any time before a Deferred Share Award or an award under the 2014 LTI Scheme (a "Relevant Award") has vested the Committee may reduce the number of shares subject to the Relevant Award in the event of the discovery of a material misstatement in the accounts of the Company or another member of the Group, a regulatory breach by the Group resulting in material financial or reputational harm, the discovery of an error in the assessment of the extent to which a performance target applicable to a participant's Cash Award has been satisfied, or action or conduct of the participant amounting to fraud or gross misconduct.

Leaving employment during the deferral period
If a participant ceases to be employed within the Group during the deferral period a Deferred Share Award made to him will normally lapse.

If the reason for cessation of the participant's employment is death, injury or disability, redundancy, retirement, the sale of his employing business or company, or if the Committee in its discretion determines in any other particular case, the participant may retain the Deferred Share Award and it shall continue to vest in accordance with its original terms. Alternatively, the Committee may determine that the Deferred Share Award will vest immediately upon the cessation of employment. An Award which is a nil-cost option will ordinarily lapse if it has not been exercised within 6 months of cessation of employment or, if later, when it becomes exercisable.

Takeover, reconstruction etc.
In the event of a takeover, reconstruction, amalgamation or winding up of the Company or if the Committee determines where the Company is affected by a demerger or similar other event, a Deferred Share Award will vest immediately. The Deferred Share Award may be exchanged for an award over shares in an acquiring company if an offer to exchange is made and accepted by the participant or if the Committee, with consent of the acquiring company, determines that Deferred Share Awards should automatically be exchanged.

If the Committee is aware that an event described above is likely to occur and will result in Deferred Share Awards vesting in circumstances where the Company's entitlement to a corporation tax deduction may be lost, the Committee may determine that the time that Deferred Share Awards vest shall be immediately before such event takes place.

Variations of share capital
In the event of a variation of the share capital of the Company, including by way of a capitalisation issue, rights issue, demerger or other distribution, a special dividend or distribution, rights offer or bonus issue or any sub-division, consolidation, or reduction in the Company's share capital, either or both of the number of shares and the description of the shares subject to a Deferred Share Award may be adjusted in such manner as the Committee determines.

Rights attaching to shares
A Deferred Share Award will not confer any shareholder rights, such as the right to vote or to receive any dividend, where the record date is prior to the allotment or transfer of shares to the participant following the vesting of the Deferred Share Award.

A participant will be entitled to receive a payment in cash or shares upon his acquisition of the shares subject to his Deferred Share Award in respect of dividends on those shares. The payment will be of an amount equal to any dividends paid on the number of shares acquired pursuant to the Deferred Share Award during the period from the date that the Deferred Share Award was made to the date that the participant acquires the shares.

A further payment may also be made in respect of interest on any such dividends from the date the dividend was paid to the date that the participant acquires the shares, at a rate determined by the Committee.

Share ownership requirement
A participant will be required to retain the shares he acquires following the vesting of a Deferred Share Award, subject to being permitted to sell sufficient of those shares to meet income tax and national insurance contributions liabilities arising on such acquisition, until he has met any share ownership requirements which apply to him.

Amendments
The Committee may amend the rules of the 2014 STI Scheme at any time. However, the provisions relating to eligibility requirements, individual participation limits, dilution limits, the basis for determining a participant's entitlement to benefits under the 2014 STI Scheme, the adjustments that may be made in the event of a variation of share capital and the amendment provisions themselves may not be made to the advantage of existing or future participants without the prior approval of shareholders of the Company in general meeting.

There are exceptions for minor amendments to benefit the administration of the 2014 STI Scheme or to take account of a change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for participants, the Company or another member of the Group. Additionally, no amendment can be made which would adversely affect the rights of existing participants without their consent.

The 2014 LTI Scheme

Introduction
The 2014 LTI Scheme will allow awards over shares in the Company ("Awards") to be made to selected employees or Directors of the Group.

The Committee will be responsible for the operation of the 2014 LTI Scheme.

Awards made under the 2014 LTI Scheme will normally be nil-cost options to acquire shares at no cost to the participant, although Awards may also be made as conditional share awards.

The vesting of Awards will be subject to the achievement of a performance target (which may comprise a combination of separate targets) measured over a specified period. Awards may be satisfied by the issue of new shares or by the transfer of shares held in treasury or by the trustee of an employee benefit trust.

Eligibility
A participant must be an employee or Director of the Group at the time an Award is made. Participation in the 2014 LTI Scheme will be at the discretion of the Committee.

Individual limits
As stated in the Directors' remuneration policy, the total market value of shares over which Awards or awards under any other discretionary employee share scheme operated by the Company (not including the 2014 STI Scheme) may be made to a participant during 2014 may not exceed 75% of the participant's salary. The Committee may specify another limit from time to time.

Dilution limits
An Award may not be made under the 2014 LTI Scheme if it would cause the number of shares issued or issuable under any employee share scheme operated by the Company in the preceding 10 years to exceed 10% of the Company's issued ordinary share capital at that time.

In addition, an Award may not be made under the 2014 LTI Scheme if it would cause the number of shares issued or issuable under any discretionary employee share scheme operated by the Company in the preceding 10 years to exceed 5% of the Company's issued ordinary share capital at that time.

The above limits exclude any share awards which lapse, as well as any share awards which are satisfied by the transfer of existing shares. However, for as long as is required by guidelines issued the Association of British Insurers, the transfer of treasury shares will be treated as an issue of new shares.

APPENDIX 1 – SCHEME SUMMARIES (CONTINUED)

Making of Awards
Awards may only be made during the period of 42 days beginning with the date of approval of the 2014 LTI Scheme by the shareholders of the Company, or during the period of 42 days beginning with the day after the announcement of the Company's results for any period, or at such other times that the Committee considers that exceptional circumstances exist.

An Award may not be made when prevented by restrictions on dealings in shares by directors or employees of the Group imposed by statute, order, regulation, Government directive or by the Model Code or the Company's own code on dealings in its securities by directors and employees.

An Award may not be made more than 10 years after the date of adoption of the 2014 LTI Scheme.

No payment will be required for the making of an Award and Awards are not transferable (except on death). Awards are not pensionable.

Vesting of Awards
Awards will normally vest 3 years after they are made, subject to the satisfaction of the applicable performance target. An Award which is a nil-cost option will lapse 10 years after the date on which it is made.

Performance targets
An Award will be subject to a performance target which will be set by the Committee at the time the Award is made and which must be satisfied before the Award can vest.

The Committee may vary or waive the performance target applying to an Award if an event occurs which causes the Committee to consider that the performance target is no longer appropriate, provided that such variation or waiver is reasonable in the circumstances and, except in the case of a waiver, produces a fairer measure of performance and is not materially less difficult to satisfy.

Details of the performance target which is intended to apply to Awards made in 2014 are set out in the directors' remuneration policy report.

Malus
At any time before an Award or an award under the 2014 STI Scheme (a "Relevant Award") has vested the Committee may reduce the number of shares subject to the Relevant Award in the event of the discovery of a material misstatement in the accounts of the Company or another member of the Group, a regulatory breach by the Group resulting in material financial or reputational harm, the discovery of an error in the assessment of the extent to which a performance target applicable to any of the participant's Awards has been satisfied, or action or conduct of the participant amounting to fraud or gross misconduct.

Leaving employment
If a participant ceases to be employed within the Group for any reason before an Award made to him vests, then that award will lapse unless the Committee in its discretion determines that the participant may retain a time pro-rated proportion of the Award (according to the proportion of the performance period which has then elapsed) and it shall continue to vest, if at all, in accordance with its original terms. Alternatively, the Committee may determine that a time pro-rated proportion of the Award will vest immediately upon the cessation of employment, subject to the Committee's assessment of the extent to which the applicable performance target shall be deemed to be met at that time.

The Committee may vary the time pro-rating applied to allow a greater proportion of the Award to vest.

An Award which is a nil-cost option will ordinarily lapse if it has not been exercised within 6 months of cessation of employment or, if later, when it becomes exercisable.

Takeover, reconstruction etc.
In the event of a takeover, reconstruction, amalgamation or winding up of the Company or if the Committee determines where the Company is affected by a demerger or similar other event, a time pro-rated proportion of an Award (according to the part of the performance period which has then elapsed) will vest immediately, subject to the Committee's assessment of the extent to which the applicable performance target shall be deemed to be met at that time. The Committee may vary the time pro-rating applied to allow a greater proportion of the Award to vest.

The Award may be exchanged for an award over shares in an acquiring company if an offer to exchange is made and accepted by the participant or if the Committee, with consent of the acquiring company, determines that Awards should automatically be exchanged.

If the Committee is aware that an event described above is likely to occur and will result in Awards vesting in circumstances where the Company's entitlement to a corporation tax deduction may be lost, the Committee may determine that the time that Awards vest shall be immediately before such event takes place.

Variations of share capital
In the event of a variation of the share capital of the Company, including by way of a capitalisation issue, rights issue, demerger or other distribution, a special dividend or distribution, rights offer or bonus issue or any sub-division, consolidation, or reduction in the Company's share capital, either or both of the number of shares and the description of the shares subject to an Award may be adjusted in such manner as the Committee determines.

Rights attaching to shares
An Award will not confer any shareholder rights, such as the right to vote or to receive any dividend, where the record date is prior to the allotment or transfer of shares to the participant following the vesting of the Award. A participant will be entitled to receive a payment in cash or shares upon his acquisition of the shares subject to his Award in respect of dividends on those shares. The payment will be of an amount equal to any dividends paid on the number of shares acquired pursuant to the Award during the period from the date that the Award was made to the date that the participant acquires the shares.

A further payment may also be made in respect of interest on any such dividends from the date the dividend was paid to the date that the participant acquires the shares, at a rate determined by the Committee.

Share ownership requirements
A participant will be required to retain the shares he acquires following the vesting of an Award, subject to being permitted to sell sufficient of those shares to meet income tax and national insurance contributions liabilities arising on such acquisition, until he has met any share ownership requirements which apply to him.

Amendments
The Committee may amend the rules of the 2014 LTI Scheme at any time. However, the provisions relating to eligibility requirements, individual participation limits, dilution limits, the basis for determining a participant's entitlement to benefits under the 2014 LTI Scheme, the adjustments that may be made in the event of a variation of share capital and the amendment provisions themselves may not be made to the advantage of existing or future participants without the prior approval of shareholders of the Company in general meeting.

There are exceptions for minor amendments to benefit the administration of the 2014 LTI Scheme or to take account of a change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for participants, the Company or another member of the Group. Additionally, no amendment can be made which would adversely affect the rights of existing participants without their consent.

GLOSSARY

ABI Association of British Insurers – Represents the collective interests of the UK's insurance industry.

AGM Annual General Meeting.

ALM Asset Liability Management – management of risks that arise due to mismatches between assets and liabilities.

APE Annual Premium Equivalent – an industry wide measure that is used for measuring the annual equivalent of regular and single premium policies.

ASB Accounting Standards Board.

CA Original business of Countrywide Assured plc.

CWA Original business of City of Westminster Assurance Company Limited.

CA plc Countrywide Assured plc;

CALH Countrywide Assured Life Holdings Limited and its subsidiary companies.

Directors or Board The Directors of the Company as at the date of this document whose names are set out on page 53 of this document.

DPF Discretionary Participation Feature – A contractual right under an insurance contract to receive, as a supplement to guaranteed benefits, additional benefits whose amount or timing is contractually at the discretion of the issuer.

EEV European Embedded Value

FCA the Financial Conduct Authority.

FI Finansinspektionen, being the Swedish Financial Supervisory Authority.

Form of Proxy The form of proxy relating to the General Meeting being sent to Shareholders with this document.

FRS Financial Reporting Standards.

FSA the Financial Services Authority.

FSMA the Financial Services and Markets Act 2000 of England and Wales, as amended.

GCR Group Capital Resources – in accordance with the UK's regulatory regime for insurers it is the sum of the individual capital resources for each of the regulated related undertakings less the book-value of investments by the Group in those capital resources.

GCRR Group Capital Resource Requirement – in accordance with the UK's regulatory regime for insurers it is the sum of individual capital resource requirements for the insurer and each of its regulated undertakings.

Group The Company and its existing subsidiary undertakings.

Guardian Guardian Assurance plc.

HCL HCL Insurance BPO Services Limited.

IAS International Accounting Standards.

IFRIC International Financial Reporting Interpretations Committee.

IFRS International Financial Reporting Standards.

IFA Independent Financial Adviser.

IGD Insurance Groups Directive – The European directive setting out the current capital adequacy regime for insurance groups.

KPI Key performance indicator.

London Stock Exchange London Stock Exchange plc.

LTICR Long-Term Insurance Capital Requirement – Capital required to be held for regulatory purposes in respect of investment, expense and insurance risks.

LTI Long-Term Incentive scheme – A reward system designed to incentivise employees' long-term performance.

MCEV Market Consistent Embedded Value.

MECR Mortgage Endownment Complaints Reserve.

Movestic Movestic Livförsäkring AB.

Modernac Modernac SA , an associated company which is 49% owned by Movestic.

Official List The Official List of the Financial Conduct Authority.

Ordinary shares Ordinary shares of five pence each in the capital of the Company.

ORSA Own Risk and Solvency Assessment.

PRA the Prudential Regulation Authority.

PL Protection Life Company Limited.

RCR Resilience Capital Requirement – additional amounts of capital required to be held for regulatory purposes as a result of two stress tests.

Resolution The resolution set out in the notice of General Meeting set out in this document.

Shareholder(s) Holder(s) of Ordinary Shares.

Solvency II A fundamental review of the capital adequacy regime for the European insurance industry. Solvency II aims to establish a set of EU-wide capital requirements and risk management standards that will replace the current Solvency I requirements.

STI Short-Term Incentive scheme – A reward system designed to incentivise employees' short-term performance.

Swedish Business Movestic and its subsidiaries and associated companies.

S&P Save & Prosper Insurance Limited and Save & Prosper Pensions Limited.

SPI Original business of Save & Prosper Insurance Limited.

SPP Original business of Save & Prosper Pensions Limited.

TCF Treating Customers Fairly – a central FCA principle that aims to ensure an efficient and effective market and thereby help policyholders achieve a fair deal.

TSR Total Shareholder Return , measured with reference to both dividends and capital growth.

UK or United Kingdom the United Kingdom of Great Britain and Northern Ireland.

UK Business CA, CALH, S&P and PL.

VIF Value of In-force business.

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