ANNUAL REPORT & ACCOUNTS

2017

Chesnara

WELCOME TO THE

CHESNARA ANNUAL REPORT

for year ended
31 December 2017

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Lancashire, England, United Kingdom

SECTION A:
OVERVIEW

SECTION A • OVERVIEW

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Amsterdam, Netherlands

AN INTRODUCTION TO CHESNARA

Chesnara plc is a life assurance and pensions consolidator. It has operations in the UK, Sweden and the Netherlands.

Our primary focus is the efficient management of life assurance and pension policies to give good and fair outcomes to our customers, generating profits to provide attractive dividends and value growth to our investors. Periodically we seek to create further value and sustain our dividend policy by acquiring new companies or books of business. Our acquisition strategy primarily focuses on the territories in which we operate, though we will consider opportunities in other European countries where there is sufficient value and strategic and cultural fit.

The group comprises both open-book and closed-book operations. We write new business where we are confident that conditions will ensure the sales are value adding. The new business operations will always be based on realistic market share expectations and hence the writing of new business will not detract from our core objective of managing in-force books to provide good returns to policyholders and investors.

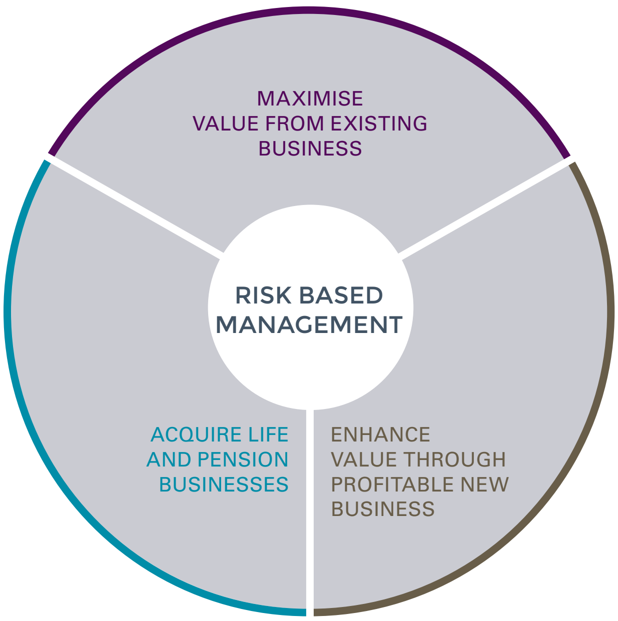
Chesnara's long established culture & values underpin the delivery of our core strategic objectives. Risk and solvency management are at the heart of our robust governance framework and the group is well capitalised. Throughout its history, Chesnara has aimed to deliver fair outcomes for policyholders whilst providing consistent returns for shareholders.

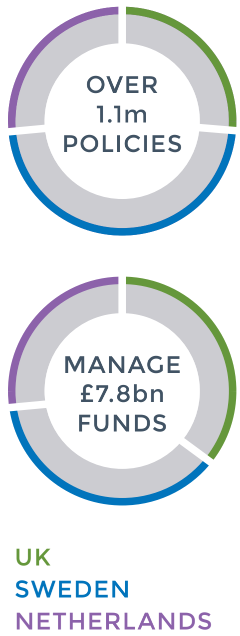
ABOUT CHESNARA

WHO WE ARE

- We are a responsible and profitable company engaged in the management of life and pension policies in the UK, Sweden and the Netherlands.
- Chesnara plc was formed in 2004 and 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, an open life and pensions business in Sweden and both a closed-book group and an open life and pensions business in the Netherlands. See page 6 for further detail on our history and businesses.

WHAT WE DO





HOW WE OPERATE

- Chesnara devolves management to its divisions which operate within a centrally defined governance and risk management framework.
- A central UK-based team has significant experience and a proven track record in governing, acquiring and successfully integrating life and pension businesses.
- In the UK, we adopt an outsourced operating model to the fullest extent possible, whereas our overseas divisions use outsourced services on a more limited basis.
- Acquisitions are assessed against stringent financial criteria adopting a robust risk-based due diligence process.
- We maintain strong solvency levels.

HOW WE CREATE VALUE

Policyholder

- Effective customer service operations, clear communication and competitive fund performance, with full regard to all regulatory matters, support our aim to ensure policyholders receive good returns and service in line with fair outcomes for customers.
- Provide security through strong solvency.

Shareholder

- Surpluses emerge from the in-force books of business through efficient management of the policy base and good capital management practices. These surpluses enable dividends to be paid from the subsidiaries to Chesnara, which fund the attractive dividend strategy and support our wish to be a share held for the long term by our shareholders.
- Growth from both the proven acquisition model and from writing profitable new business in Sweden and the Netherlands has a positive impact on the Economic Value of the business.

WE AIM TO PROVIDE **VALUE FOR MONEY** TO OUR CUSTOMERS AND INVESTORS IN A **COMPLIANT MANNER.**

DELIVERING OUR STRATEGY

Our company history has helped shape our business, which in turn enables us to deliver against our objectives.

COMPANY HISTORY

2004

Chesnara is born - Countrywide estate agency group divests its life insurance business and this becomes the inaugural portfolio of Chesnara plc with an opening Embedded Value of £126m.

2005

Chesnara makes its first acquisition City of Westminster Assurance, adding £30.3m of Embedded Value.

2007

Chesnara becomes established as an attractive dividend stock, after three years of dividend growth.

2009

Chesnara plc moves into Europe with the acquisition of a Swedish business now called Movestic. The group's Embedded Value reaches £263m. Unlike the UK operation, Movestic is open to new business which adds a further source of embedded value growth.

2010

The acquisition of Save and Prosper takes the group's assets under management to over £4bn.

2013

Direct Line's life assurance business is acquired and by the end of 2014, total group embedded value rises above £400m.

2015

Expansion into a new territory with the acquisition of the Waard Group (a closed book) in the Netherlands.

2016

Building upon our entry to the Dutch market we announce the acquisition of Legal & General Nederland, an open business.

2017

Completion of Legal & General Nederland acquisition renamed Scildon, at a 32% discount to its Economic Value of £202.5m.

WHAT WE'VE DONE

6 SUCCESSFUL ACQUISITIONS ACROSS **3** TERRITORIES.

Our deals **demonstrate flexibility and creativity** where appropriate:

- Tactical 'bolt-on' deals to more transformative deals
- Open minded regarding deal size
- Willingness to find value beyond the UK
- Flexible and efficient deal funding solutions
- Capability to find expedient solutions to de-risk where required.

We are **not willing to compromise** on **quality, value or risk**. All deals have:

- been at a competitive discount to value
- satisfied our dual financial requirements of generating medium-term cash and enhancing long-term value
- been within Chesnara's risk appetite
- been subject to appropriate due diligence
- been either neutral or positive in terms of customer outcomes
- supported Chesnara's position as an income investment.

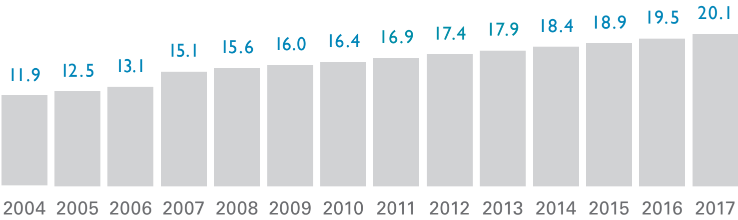
OUTCOMES

DIVIDEND HISTORY

13 SUCCESSIVE YEARS OF DIVIDEND GROWTH

We recognise the importance of providing stable and attractive dividends to our shareholders. A full year 2017 dividend of 20.07p per share represents an increase of 2.98% on the prior year, and is Chesnara's 13th successive year of dividend growth.

Dividend per share history
Pence per share

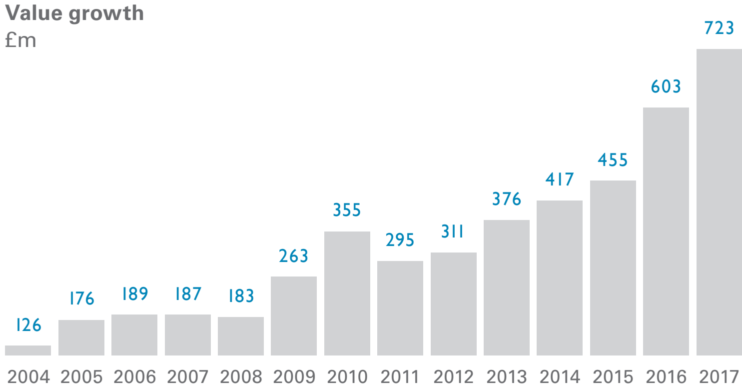


VALUE GROWTH

£723M OF ECONOMIC VALUE

Value growth* is achieved through a combination of efficient management of the existing policies, acquisitions and writing profitable new business. The growth includes £148m of new equity since 2004 but is net of £267m of cumulative dividend payments.

Value growth
£m



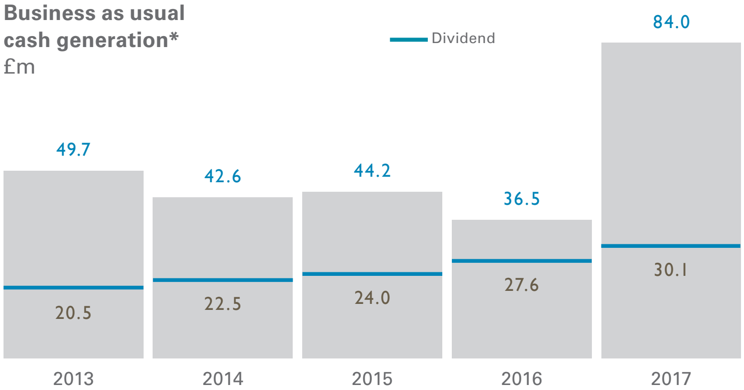
*Value is based on Embedded Value principles up until 2015, thereafter it is based on Economic Value (see page 39 for further information). The transition from Embedded Value to Economic Value resulted in only a modest change in valuation.

CASH GENERATION

CASH GENERATION CONTINUES TO SUPPORT DIVIDENDS

Ultimately the group needs to generate cash to service its dividends. Cumulative cash generation over the last five years represents c200% of the total dividends over the same period.

Business as usual cash generation*
£m



POLICYHOLDERS

OUR PRIMARY RESPONSIBILITIES REMAIN TO OUR POLICYHOLDERS

- Customers can be confident that they have policies with a well capitalised group where financial stability is central to our culture and values.
- Our investment returns remain competitive across the group.
- We deliver good customer service levels across the group.

*The chart to the left illustrates how business as usual cash generation compares to the total shareholder dividend. For this purpose the cash figure is based on divisional cash generation plus non-exceptional group items. To include exceptional items would mislead in terms of illustrating the effectiveness of the core business in funding the dividend.

2017 HIGHLIGHTS

FINANCIAL

IFRS

£89.6M

IFRS PRE-TAX PROFIT
2016 £40.7M

The 2017 result includes £20.3m gain on acquisition of Legal & General Nederland.

£86.9M

IFRS TOTAL COMPREHENSIVE INCOME
2016 £55.4M

The 2017 result includes foreign exchange gain of £8.3m (2016: £20.1m).

Financial review **p36**

SOLVENCY

146%

GROUP SOLVENCY
2016 158% (144% EXCLUDING EQUITY RAISE IMPACT)*

We are well capitalised at both group and subsidiary level and under Solvency II have not used any elements of the long term guarantee package, including transitional arrangements.

Capital management **p32**

*The 2016 closing ratio of 158% was enhanced by equity raised ahead of the purchase of Legal & General Nederland. The adjusted position at 31 December 2016, excluding this impact, was 144%. This figure represents a more logical comparison for assessing movements during 2017.

ECONOMIC VALUE

£723.1M

ECONOMIC VALUE
2016 £602.6M

Movement in the period is stated after dividend distributions of £29.5m.

Includes gain on acquisition of Legal & General Nederland of £65.4m.

Financial review **p39**

ECONOMIC VALUE EARNINGS

£139.5M

ECONOMIC VALUE EARNINGS
2016 £72.5M

Financial review **p38**

£12.4M

NEW BUSINESS PROFIT
2016 £11.7M

Business review **p26 to 29**

CASH GENERATION

£28.6M

GROUP CASH GENERATION
2016 £85.4M

A £48.9m one-off positive impact, in respect of equity raised ahead of completion of the acquisition of Legal & General Nederland, was included in the 2016 result. We highlighted this as a temporary impact in our 2016 accounts. As expected, on completion, the 2017 result includes a consequential negative impact of £55.3m. This explains the large year on year swing on the headline group cash generation metric. The end to end impact of the Legal & General Nederland acquisition is to reduce cash generation by £6.4m.

Financial review **p37**

£86.7M

DIVISIONAL CASH GENERATION
2016 £34.3M

Includes the cash generated post acquisition by Scildon of £16.2m.

Financial review **p37**

These financial highlights include the use of Alternative Performance Measures (APMs) that are not required to be reported under International Financial Reporting Standards. The definition for each of these items has been included in page 10 and in further detail within the Financial Review section on pages 34 to 35.

OPERATIONAL & STRATEGIC

DIVIDEND

FULL YEAR DIVIDEND INCREASE

Total dividends for the year increased by 2.98% to 20.07p per share (7.00p interim and 13.07p proposed final). This compares with 19.49p in 2016 (6.80p interim and 12.69p final).

ACQUISITIONS

COMPLETION OF LEGAL & GENERAL NEDERLAND ACQUISITION

With a purchase price of €161m, this acquisition was successfully completed on 5 April 2017 and the company renamed Scildon. Good progress has been made on integrating the business with the Chesnara group with benefits delivered slightly ahead of expectations.

ECONOMIC BACKDROP

EQUITY GROWTH, WEAKENING STERLING

Equity markets in all territories have performed positively during the year. The Swedish krona and euro have both strengthened against sterling, resulting in positive exchange gains being reported in the period.

DIVISIONAL DIVIDEND

£70.0M OF TOTAL PROPOSED DIVISIONAL DIVIDENDS

The results during the year, combined with associated solvency positions, have enabled the divisions to propose total dividends to Chesnara of £70.0m. As expected, the UK business dividend of £32m continues to be the largest contributor but it is equally encouraging to see the Dutch businesses of Scildon and Waard propose dividends of £22.2m and £13.0m respectively.
The fact that a growth business such as Movestic has proposed a dividend of £2.8m is also very positive.

SOLVENCY

SOLVENCY II IN ACTION

As planned, we have continued to enhance our understanding of the Solvency II figures during the year. This has resulted in a number of changes to the SCR. These changes consist of positive capital management actions such as de-risking Scildon's shareholder assets, improved asset analysis in Movestic and model enhancements which ensure the SCR better aligns to our business.

SYMBOL GUIDE

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

- IFRS
- Cash generation
- Economic Value
- Economic Value Earnings
- Solvency
- Dividend/Total Shareholder Return
- Part VII
- Operational performance
- Compliance
- New business market share
- Acquisitions
- Risk appetite

MEASURING OUR PERFORMANCE

HOW WE MEASURE PERFORMANCE WITHIN THESE REPORT & ACCOUNTS

Throughout our Report & Accounts, we use measures to assess and report how well we have performed. The range of measures is broad and includes many measures that are not based on IFRS. The financial analysis of a life and pensions business also needs to recognise the importance of Solvency II figures, the basis of regulatory solvency. In addition, the measures aim to assess performance from the perspective of all stakeholders.

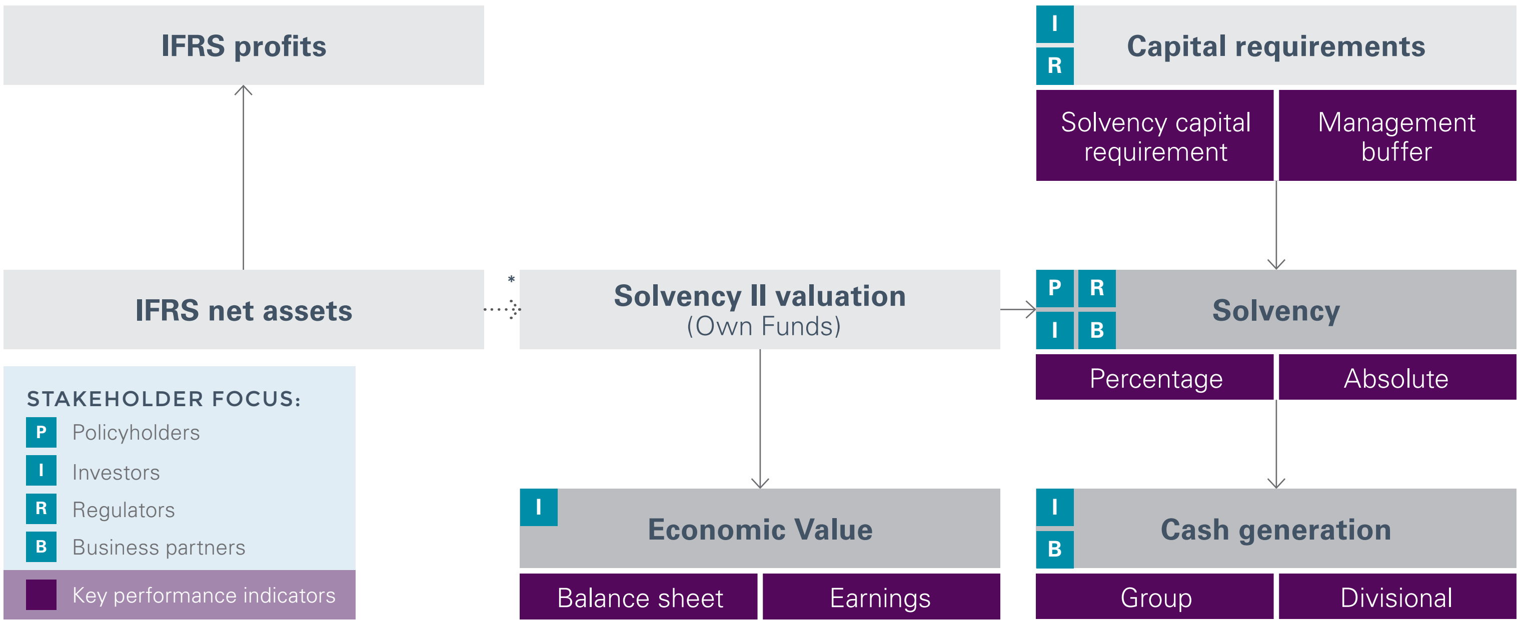
FINANCIAL ANALYSIS OF A LIFE AND PENSION BUSINESS

Whilst the IFRS results form the core of the Report & Accounts and hence retain prominence as a key financial performance metric, there is a general acceptance that the IFRS results in isolation do not adequately recognise the wider financial performance of a typical life and pensions business.

In light of the limitations of IFRS reporting, these Report & Accounts adopt several Alternative Performance Measures (APMs) to present a more meaningful view of the financial position and performance. The non-IFRS APMs have at their heart the Solvency II valuation known as Own Funds and as such, all major financial APMs are derived from a defined rules-based regime. The diagram below shows the core financial metrics that sit alongside the IFRS results, together with their associated KPIs and interested parties.

FINANCIAL STATEMENTS

ADDITIONAL METRICS



SOLVENCY

Solvency is a fundamental financial measure which is of paramount importance to investors and policyholders. It represents the relationship between the value of the business as measured on a Solvency II basis and the capital the business is required to hold – the Solvency Capital Requirement (SCR). Solvency can be reported as an absolute surplus value or as a ratio.

Solvency gives policyholders comfort regarding the security of their provider. This is also the case for investors together with giving them a sense of the level of potential surplus available to invest in the business or distribute as dividends (subject to other considerations and approvals).

Further details on p31 to 33

ECONOMIC VALUE

Economic Value (EcV) is deemed to be a more meaningful measure of the long term value of the group and it generally approximates to Embedded Value reporting, which was used before the introduction of SII. In essence, the IFRS balance sheet is not generally deemed to represent a fair commercial value of our business as it does not fully recognise the impact of future profit expectations of long term policies.

EcV is derived from Solvency II Own Funds and recognises the impact of future profit expectations from existing business.

Further details on p38 to 39

CASH GENERATION

Cash generation is a measure of how much distributable surplus has been generated in the period, which supports the ability of the group to pay its dividends. It is driven by the change in solvency surplus, taking into account board-approved capital management policies.

*See page 138 for a reconciliation between IFRS net assets and Solvency II own funds.

Further details on p37

OPERATIONAL AND OTHER PERFORMANCE MEASURES

In addition to the financial performance measures, the Report & Accounts include measures that consider and assess performance of all our key stakeholder groups. The diagram below summarises the performance measures adopted throughout the Report & Accounts.

Key: ■ Primary interest □ Secondary interest

Key stakeholders

Measure	Policyholder	Investor	Regulators	Business partner*	What is it and why is it important?	Page
Customer service levels	■	□	■	□	How well we service our customers is of paramount importance and so through various means we aim to assess customer service levels. The business reviews within the Report & Accounts refer to a number of indicators of customer service levels.	24-29
Broker satisfaction	■	□	□	■	Broker satisfaction is important because they sell new policies, provide ongoing service to their customers and influence book persistency. We include several measures within the Report & Accounts, including direct broker assessment ratings for Movestic and general assessment of how our brands fair in industry performance awards in the Netherlands.	26-29
Policy investment performance	■	□	■	□	This is a measure of how the assets are performing that underpin policyholder returns. It is important as it indicates to the customer the returns that their contributions are generating.	24-29
Industry performance assessments	■	□	□	□	This is a comparative measure of how well our investments are performing against the rest of the industry, which provides valuable context to our performance.	24-29
Funds under management	□	■	□	□	This shows the value of the investments that the business manages. This is important because scale influences operational sustainability in run-off books and operational efficiency in growing books. Funds under management are also a strong indicator of fee income.	26-27
Policy count	□	□	□	□	Policy count is the number of policies that the group manages on behalf of customers. This is important to show the scale of the business, particularly to provide context to the rate at which the closed book business is maturing. In our open businesses, the policy count shows the net impact of new business versus policy attrition.	4
Total shareholder returns		■	□		This includes dividend growth and yield and shows the return that an investor is generating on the shares that they hold. It is highly important as it shows the success of the business in translating its operations into a return for shareholders.	40
New business profitability		■			This shows our ability to write profitable new business which increases the value of the group. This is an important indicator given one of our core objectives is to 'enhance value through profitable new business'.	26-29
New business market share		□			This shows our success at writing new business relative to the rest of the market and is important context for considering our success at writing new business against our target market shares.	26-29
Gearing ratio		■	□		The gearing is a ratio of debt to IFRS net assets and shows the extent to which the business is funded by external debt versus internal resources. The appropriate use of debt is an efficient source of funding but in general Chesnara seek to avoid becoming overly dependent on permanent debt on the balance sheet.	40
Knowledge, skills and experience of the Board of Directors	□	■	■	□	This is a key measure given our view that the quality, balance and effectiveness of the board of directors has a direct bearing on delivering positive outcomes to all stakeholders.	50-51

* For the purposes of this key performance indicator assessment business partners refers to major suppliers and outsource partners.

CHAIRMAN'S STATEMENT

Our financial results have been achieved while remaining true to our well established culture and values.

2017 has been another good year for Chesnara during which we completed the acquisition of Legal & General Nederland, now successfully rebranded Scildon, and made good progress on integrating it into our business. The acquisition has contributed to an impressive set of results on all financial metrics, including IFRS, Economic Value and Solvency II.

In particular I am pleased to report an Economic Value growth, excluding the acquisition gain, of 9.1%.

All divisions have made significant contributions to cash and value generation. The UK business had again generated cash ahead of expectations and Movestic continues to deliver significant growth, which has resulted in further cash generation.

During the post acquisition period, Scildon has delivered Economic Value growth and solvency surplus broadly in line with our initial expectations. That said, we retain our view that the business would benefit from some focussed improvements and have initiated a development programme to improve the profitability of new business.

As a result of the positive performance in the year, Chesnara expects total dividends from its divisions of £70.0m, including an inaugural Scildon dividend of £22.2m.

PETER MASON,
CHAIRMAN

During 2017 we have delivered against each of our core strategic objectives thanks to economic tailwinds, good operational delivery and the successful completion of the acquisition of Legal & General Nederland. This has resulted in financial results which support the continuation of our dividend strategy and show continued Economic Value growth. This has been achieved whilst remaining true to our well established culture and values of treating customers fairly and adopting a robust approach to regulatory compliance. Importantly, the business growth has been achieved without compromising our risk appetite.

01 MAXIMISE VALUE FROM EXISTING BUSINESS

£86.7m of divisional cash generation representing 288% dividend cover.

See pages 24 to 29 for further information.

The profitability of our existing business remains at the heart of our business model. IFRS pre-tax profits, which predominantly flow from the in-force business, of £89.6m (2016: £40.7m) compare favourably to prior year and base case expectations.

In addition, all of our divisions, including Scildon, have made significant positive cash contributions totalling £86.7m.

A 7.1% growth in the Economic Value of the existing business, excluding the impact of new business and acquisitions, is also dominated by the impact of positive economic conditions. The group has reported a modest economic value operating profit of £3.3m. This consists of an underlying operating profit of £22.5m, offset by the negative impact of making provision to adopt a slightly more attractive pricing strategy on certain white label funds in Movestic and to cover the one-off costs of developing the Scildon business.

02 ACQUIRE LIFE AND PENSIONS BUSINESSES

Acquisition of Legal & General Nederland (now Scildon) created a positive Economic Value impact of £65.4m.

See page 30 for further information.

THE ECONOMIC VALUE OF THE GROUP HAS INCREASED BY 20.0% IN THE YEAR, OF WHICH 10.9% RELATES TO THE GAIN ON COMPLETION OF THE ACQUISITION OF LEGAL & GENERAL NEDERLAND.

The completion of the acquisition of Legal & General Nederland has delivered 'Day 1' financial benefits slightly ahead of expectations. Since completion, management has spent time working with our new colleagues in the Netherlands. Initial assessment confirms that the business is well managed and soundly governed. As expected we have also identified opportunities to make some process improvements over the next two years which we expect to increase the future financial returns from the business. We have completed a successful rebrand to the new company name, 'Scildon', and have made significant progress in integrating the business into the Chesnara group. The successful integration of Scildon means the group remain well positioned for any new opportunity that arises.

03 ENHANCE VALUE THROUGH PROFITABLE NEW BUSINESS

New business profits from Movestic of £11.8m plus a modest full year new business profit of £1.9m from Scildon.

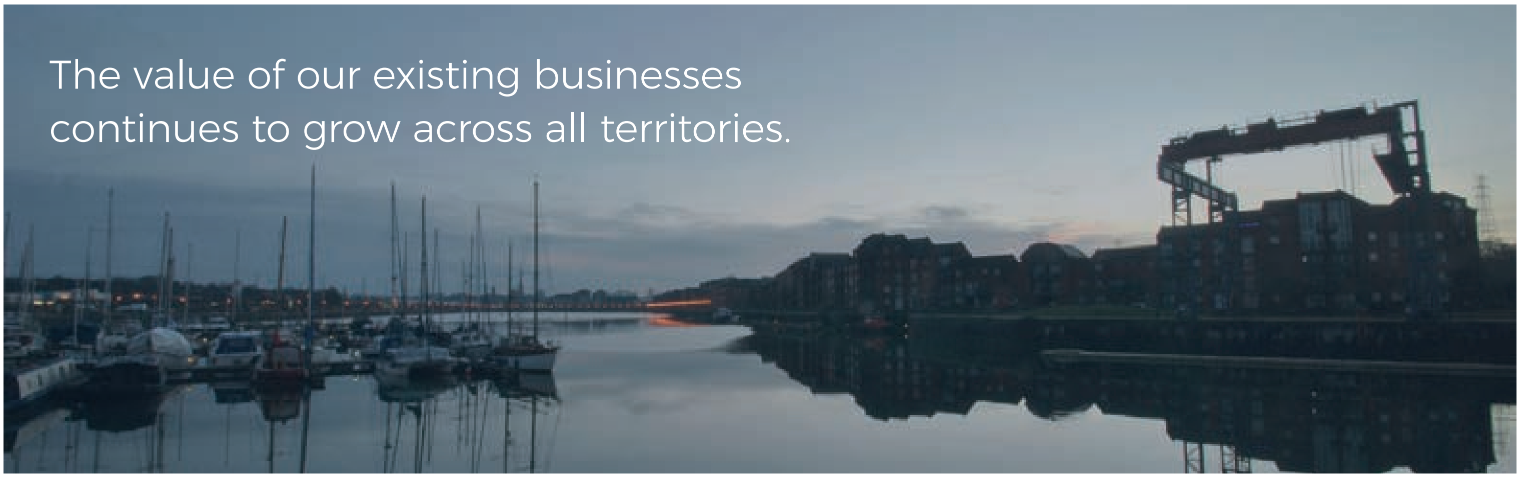
See pages 26 to 29 for further information.

Movestic has continued to operate within its market share target range and has generated £11.8m of new business profit representing a 5.2% growth on Movestic's opening Economic Value.

We acquired Scildon with an expectation that it was breaking even on writing new business. The fact that Scildon have reported a modest new business profit for the full year of £1.9m is encouraging but this level of profit is not deemed commercially acceptable. We have initiated changes, to be delivered over a two year timeframe, which we believe will improve market shares towards the upper end of our target 5% - 10% protection market share range and which would create more commercially meaningful levels of new business profit.

NEW BUSINESS PROFIT FROM MOVESTIC OF £11.8M AND AS EXPECTED SCILDON IS ONLY MARGINALLY PROFITABLE. A DEVELOPMENT PROGRAMME HAS BEEN INITIATED TO IMPROVE SCILDON'S PROFITABILITY OVER THE NEXT TWO YEARS.

CHAIRMAN'S STATEMENT



Solvency

At the end of 2016, the group solvency ratio, which includes no transitional adjustments, was 158% which translated to an absolute level of surplus of £185m. This position had the temporary benefit of holding £50m of surplus due to the equity raised in advance of funding the acquisition of Legal & General Nederland. The underlying solvency ratio of 144% equated to £135m of absolute surplus.

During 2017, the absolute level of surplus, over and above the SCR increased by £58m after accounting for the impact of dividends. Of this increase, £4.7m was the direct consequence of the acquisition of Legal & General Nederland. This relatively modest impact is in line with expectations and is consistent with the equity raise prospectus. The acquisition impact as reported includes the benefits of having reinvested shareholder assets shortly after completion from equities to fixed income investments, with lower capital requirements. This is consistent with Chesnara's investment policy and risk appetite regarding the investment of shareholder assets. The remainder of the surplus emerging is due to surpluses arising in all of our businesses. The UK provided the majority of the increase although Movestic and Waard continued to make meaningful positive contributions. Whilst it is still relatively early in the post acquisition period for Scildon, it was encouraging to see a surplus of £16.2m emerge during this time. On an annualised basis, this is broadly in line with expectations.

When expressed as a ratio, the closing solvency ratio as at 31 December 2017 of 146% is marginally improved compared to the end of 2016 (adjusted to exclude the temporary equity raise benefit).

AN INCREASED UNDERSTANDING OF THE DYNAMICS OF SOLVENCY II HAS, AS EXPECTED, CREATED CAPITAL OPTIMISATION BENEFITS IN THE YEAR. WE WILL CONTINUE TO IDENTIFY FURTHER CAPITAL OPTIMISATION BENEFITS OVER THE COMING YEARS

Solvency II and IFRS 17

After many years and much hard work, I am pleased to report the implementation stage of the transition to the Solvency II regime is now fully complete. During the year, we successfully produced our inaugural Solvency II narrative reports with the Solvency and Financial Condition Report being made available on our website. We believe Solvency II creates an improved focus on capital requirements and risk. This means we can better assess the impact of management decisions and also creates the potential for value adding management actions.

As Solvency II becomes embedded into day to day operations, the industry now faces the challenge of applying new accounting rules for insurance contracts, known as IFRS 17. It is not expected to have any direct bearing on the commercial assessment of Chesnara. That is, it is not expected to have an impact on Economic Value or cash generation, other than the direct impact of the cost of implementing the change.

Regulation

Compliance with regulation remains a priority for the group. We have continued to maintain a positive and constructive relationship with regulatory bodies across the group.

Following the final guidance from the FCA's review of the 'Fair treatment of long standing customers in the life insurance sector', we have been able to progress with the delivery of our Customer Strategy in the UK. The programme is now established and board approved budgets are recognised within our provisions. The work undertaken to date continues to support the level of provision made. The project does include enhancements to meet new regulatory standards.

The investigation into how Countrywide Assured disclosed exit fees to customers, initially announced on 3 March 2016, is ongoing. We have provided the FCA with all information requested. Discussions continue and given the narrow scope of the investigation we retain our opinion that the outcome from the investigation will not have a material impact on the company.

No significant regulatory issues have arisen in Sweden or the Netherlands during the year.

Investment proposition

Given Chesnara shares are primarily held by those requiring attractive income, I am pleased to report a 2.98% increase in our full year dividend.

I AM PLEASED TO REPORT A 2.9% INCREASE IN FULL YEAR DIVIDEND

Governance and risk management

We continue to place great importance on the ongoing enhancement of our risk and governance system, and have a number of developments underway. Embedding activity progresses, with significant focus in 2017 on continuing to increase the consistency of our approach across the group, including the newly acquired Scildon business.

In line with our implementation of a strong governance framework, we have carried out a tender process for our external audit during the second half of 2017. As a result of this, we recommend the reappointment of Deloitte and further details of the process are included in the Audit and Risk Committee Report.

AT CHESNARA WE HAVE ALWAYS MANAGED OUR BUSINESS IN A RESPONSIBLE WAY AND HAVE A STRONG SENSE OF ACTING IN A FAIR MANNER, GIVING FULL REGARD TO THE RELATIVE INTERESTS OF ALL STAKEHOLDERS. DURING THE YEAR, WE HAVE TAKEN THE OPPORTUNITY TO A STEP BACK TO REFLECT UPON OUR CORPORATE PURPOSE.

Corporate purpose
We have assessed our corporate purpose by considering eight aspects of our business and by looking at the business from the perspective of all stakeholders.

Business model
– Our acquisition strategy is built upon long term commitments to any markets we operate in. Our consolidation model therefore offers a genuine solution to the challenges certain insurance markets face.

The products and services we provide
– We help protect people and their dependants through the provision of life, health and disability cover or by providing savings and pensions which help customers with their financial needs in the future. We seek to provide customers and their advisers with helpful and reliable support.

Sustainability
– Driven in part by consumer demand, especially in our Swedish and Dutch operations, there is a continued positive shift towards an increased focus of sustainable fund investments.
– The nature of our business is such that in general we have a relatively low carbon footprint.

Shareholder proposition
– Investors, especially in a low interest rate environment do have a genuine need for income and hence our investor proposition, track record and responsible approach provides an investment opportunity for individuals seeking sustainable equity based income.

Taxation
– As per our tax strategy, we adopt a responsible and open approach to taxation and, as a consequence, pay the appropriate taxes.

Staff
– We provide high quality jobs with competitive remuneration and good working conditions both directly and through outsourced arrangements.

Suppliers and partners
– We seek mutually respectful and sustainable relationships with our suppliers. We believe that supplier relationships only work in the long term if the terms and conditions are mutually beneficial. Our instinct and natural preference is to maintain established long term supplier relationships where they remain commercially competitive and operationally viable.

Local community
– Investment and continued commitment to the North West and Preston in particular creates high quality financial services roles outside of London.
– All divisions support local community initiatives to the extent deemed appropriate given our financial responsibilities as a PLC.

In summary based on the above, our view is that Chesnara fulfils a positive corporate purpose.

OUR VIEW IS THAT CHESNARA FULFILS A POSITIVE CORPORATE PURPOSE.

Outlook and Brexit
I remain optimistic that Chesnara can continue to deliver against its strategic objectives, which in turn fund our well established dividend strategy.

In particular, the UK business remains a robust source of cash, with additional potential to take management actions to enhance the core cash if required. Movestic now has the scale to continue contributing to the cash position and provisions made during the year create the required capacity to react to any market driven fee pressures without adverse profit impact. Scildon has significant surplus capital and is also expected to be cash generative on an ongoing basis.

We now have sufficient scale and presence in both the UK and the Netherlands to continue our focus on acquisition activity in those territories. We also remain open minded about new territories but the benefits would need to outweigh the inherent challenge of adding another regulatory environment into our business model. Our balance sheet has further capacity for debt and we are nearing completion of a debt syndication process that will ensure we are in a strong position to take advantage of the balance sheet capacity. We have significant levels of surplus capital and recent experience suggests we retain shareholder support for further equity for the right deal. This together with operational capacity means we remain well positioned to act should an opportunity arise that meets our stringent price and risk profile criteria.

Movestic has become an established profitable new business operation and I see potential for Scildon to make improvements to their new business value in the medium term. We have provided for the expected cost of the improvement plan. I believe this will result in a meaningful level of recurring value growth from new business without a material shift from our core specialism of acquiring and managing in-force businesses.

The structure of the group, with established regulated entities in several European countries, together with the fact we do not trade or share resource across territories, means I remain of the view that whatever the outcome from the Brexit negotiations, we expect it to have little direct impact on our business model.

In light of the above I remain confident that Chesnara is well positioned to continue to provide value to policyholders and shareholders.

Peter Mason
Chairman

28 March 2018

SECTION B:
STRATEGIC REPORT

SECTION B • STRATEGIC REPORT

18 Overview of strategy, culture & values and business model
20 Our strategy
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34 Financial review
40 Financial management
42 Risk management
46 Corporate and social responsibility

Preston, England, United Kingdom

OVERVIEW OF OUR STRATEGY, CULTURE & VALUES AND BUSINESS MODEL

Our strategy focuses on delivering value to policyholders and shareholders. The strategy is delivered through a proven business model underpinned by a robust risk management and governance framework and our established culture & values.

OUR BUSINESS MODEL

Key stakeholders

- R REGULATORS
- C CUSTOMERS
- I INVESTORS

Stakeholder objectives

- Financial stability and regulatory compliance
- Fair outcomes
- Competitive return

Chesnara

Cash generation through divisional dividends and value generation through EcV growth

Division	UK	NETHERLANDS		SWEDEN
Operating company	Countrywide Assured	Waard Group	Scildon	Movestic
Strategic objectives	01 02	01 02	01 03	01 02 03
	Read more on **p24**	Read more on **p28**	Read more on **p28**	Read more on **p26**

Culture & values

Responsible risk-based management for the benefit of all of our stakeholders

OUR STRATEGIC OBJECTIVES

01 MAXIMISE THE VALUE FROM EXISTING BUSINESS

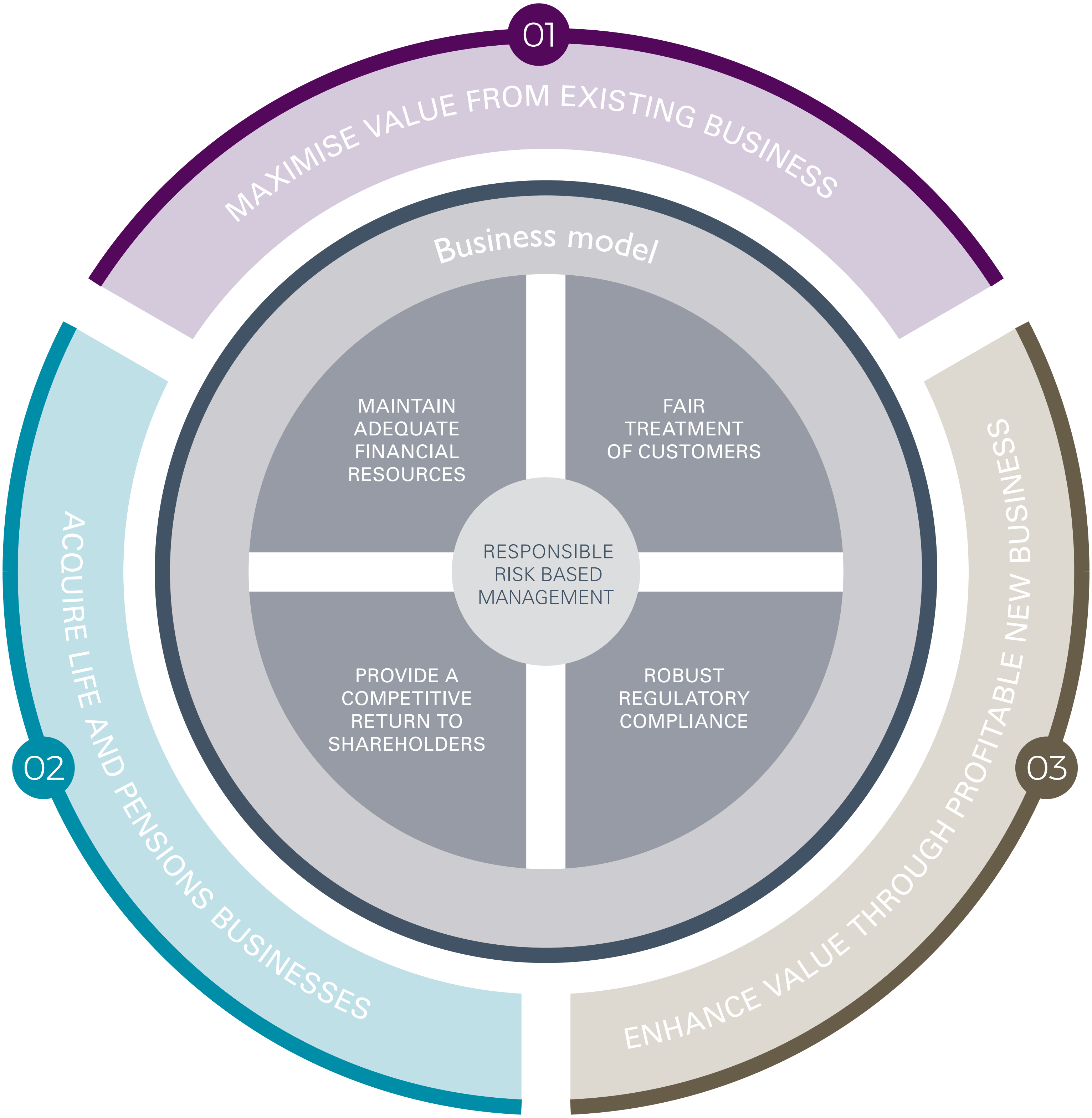
Managing our existing customers fairly and efficiently is core to delivering our overall strategic aims.

02 ACQUIRE LIFE AND PENSIONS BUSINESSES

Acquiring and integrating companies into our business model is key to continuing our growth journey.

03 ENHANCE VALUE THROUGH PROFITABLE NEW BUSINESS

Writing profitable new business supports the growth of our group and helps mitigate the natural run-off of our book.


01
MAXIMISE VALUE FROM EXISTING BUSINESS
Business model
MAINTAIN ADEQUATE FINANCIAL RESOURCES
FAIR TREATMENT OF CUSTOMERS
RESPONSIBLE RISK BASED MANAGEMENT
PROVIDE A COMPETITIVE RETURN TO SHAREHOLDERS
ROBUST REGULATORY COMPLIANCE
02
ACQUIRE LIFE AND PENSIONS BUSINESSES
03
ENHANCE VALUE THROUGH PROFITABLE NEW BUSINESS

OUR STRATEGY

STRATEGIC OBJECTIVE	WHY THIS MATTERS	HOW WE DELIVER OUR BUSINESS MODEL
01 MAXIMISE VALUE FROM OUR EXISTING BUSINESS	The existing in-force books are the principal source of cash generation and are hence at the heart of the investment case for our shareholders.	A centralised governance oversight and corporate management team ensures robust and consistent governance across the group. Operating autonomy is delivered to the divisions to ensure we benefit from our strong divisional management teams. In the UK, Chesnara adopts an outsourced business model. Core operations are not outsourced in Sweden or the Netherlands because it would not suit the business models in those territories.
02 ACQUIRE LIFE AND PENSIONS BUSINESSES	Well considered and appropriately priced acquisitions maintain the effectiveness of the operating model, create a source of value enhancement and sustain the cash generation potential of the group.	Identify potential deals through an effective network of advisers and industry associates. We assess deals applying well established criteria which consider the impact on cash generation and Economic Value under best estimate and stressed scenarios. We work cooperatively with regulators. The financial benefits are viewed in the context of the impact the deal will have on the enlarged group's risk profile. Transaction risk is minimised through stringent risk-based due diligence procedures and the senior management team's acquisition experience and positive track record. We fund deals with debt, equity or cash depending on the size and cash flows of each opportunity.
03 ENHANCE VALUE THROUGH PROFITABLE NEW BUSINESS	The primary focus of our operations is to ensure we manage the existing policy base in an efficient and compliant manner. That said, the Chesnara financial model supports modest incremental value generation through writing new business. New business profits are an important and welcome source of regular value growth which supplements the growth delivered from our existing policy base and periodic acquisitions.	Our two operating subsidiaries that are open to new business are Movestic in Sweden and Scildon in the Netherlands. Movestic primarily focuses on unit-linked pensions and savings business, distributed through IFAs, and targets a realistic share of our target market of between 10-15%. Scildon sells protection products, individual savings and group pensions contracts via a broker-led distribution model, and targets a market share of 5-10%. For both open businesses, we believe that to achieve higher volumes would require a pricing strategy that may compromise the keen focus on ensuring the business we write is profitable.

HOW WE MEASURE DELIVERY | RISKS – WHAT CAN STOP US MEETING THIS OBJECTIVE | RISKS – WHAT CAN WE DO ABOUT THIS | UPDATE

How we measure delivery

Cash generation

Cash generated by the existing business is an important measure for how the business is performing. It is defined as the movement in the surplus of capital resources over capital requirements set by the board. As such cash can be generated by either profits arising in the period or a reduction in capital requirements.

Value optimisation

Value generation is measured by reference to the movement in Economic Value over the period.

Customer outcomes

This is measured through monitoring:
- customer service metrics;
- policyholder fund performance against industry and market expectations;
- customer complaint levels; and
- our compliance with regards to regulatory conduct matters.

Risks – What can stop us meeting this objective

- Adverse investment market conditions can result in lower assets under management and hence lower fee income from unit-linked business. For products with guarantees, this can increase the cost of fulfilling the guarantees.
- Increased lapses on cash generative /value enhancing products.
- Loss of key brokers can result in increases in the level of transfers-out.
- Regulatory change can potentially impact the cash flows arising from the existing business.
- Expenditure levels could exceed those assumed.
- Foreign currency fluctuations can impact the sterling value emerging from overseas operations.

Risks – What can we do about this

- Where appropriate, active investment management with the aim of delivering competitive policyholder investment returns.
- Outsourcer service levels that ensure strong customer service standards.
- Expense assumptions are deemed to be realistic and the cost base is well controlled, predictable and within direct management influence.
- Close monitoring of persistency levels and strong customer service standards help manage lapse rates and ensure customers do not unknowingly exit when it is not in their interest to do so.

Update

UK Pages 24-25

Sweden Pages 26-27

Netherlands Pages 28-29

How we measure delivery

Cash generation

Collectively our future acquisitions must be suitably cash generative to continue to fund the Chesnara dividend strategy.

Value enhancement

Acquisitions are required to have a positive impact on the Economic Value per share under best estimate and certain more adverse scenarios.

Customer outcomes

Acquisitions must ensure we protect, or ideally enhance, customer interests.

Risk appetite

Acquisitions should normally align with the group's documented risk appetite. If a deal is deemed to sit outside our risk appetite the financial returns must be suitably compelling.

Risks – What can stop us meeting this objective

- There is the risk that if a lack of suitable acquisition opportunities come to market at a realistic valuation, the investment case for Chesnara diminishes over time.
- There is the risk that we make an inappropriate acquisition that adversely impacts the financial strength of the group.
- Our acquisition strategy includes both UK and non-UK markets.

Risks – What can we do about this

- Operating in three territories increases our options thereby reducing the risk that no further value adding deals are done.
- A broader target market also increases the potential for deals that meet our strategic objectives.
- Flexibility over the timing of subsequent capital extractions and dividend flows provide an element of management control over the sterling value of cash inflows.
- Each acquisition is supported by a financial deal assessment model which includes high quality financial analysis. This is reviewed and challenged by management and the board, mitigating the risk of a bad deal being pursued.

Update

Page 30

How we measure delivery

Value enhancement

We measure the amount of Economic Value added through the writing of new contracts. The value added takes full account of all costs incurred so as to ensure the profit represents true incremental value.

Risks – What can stop us meeting this objective

- The attractiveness of products can be influenced by economic conditions especially as some traditional products offer guaranteed returns in uncertain times.
- New business volumes are sensitive to the quality of service to intermediaries and the end customer.
- In Sweden, new business remains relatively concentrated towards several large IFAs.
- A competitive market puts pressure on new sales margins.

Risks – What can we do about this

- In Sweden, continue to extend the breadth of IFA support.
- Ensure high quality of service to existing network of intermediaries.
- Focus on other margin drivers beyond product pricing, for example the fund management operation.
- In the Netherlands, enhance our business processes and product offering to be attractive to brokers and consumers.

Update

Sweden Pages 26-27

Netherlands Pages 28-29

OUR CULTURE & VALUES

Our long established and proven culture & values underpin the delivery of our core strategic objectives. Risk management is at the heart of our robust governance framework. Our values are strongly influenced by the recognition of our responsibility to a range of key stakeholders including customers, regulators and our investors.

CULTURE & VALUES	WHY IS IT IMPORTANT?
RESPONSIBLE RISK-BASED MANAGEMENT FOR THE BENEFIT OF ALL OF OUR STAKEHOLDERS	Risk taking is a key part of our business model - taking the 'right risks' and managing them well is essential to our success. We achieve this by understanding the key risk drivers of the business plan and strategy, and by making sure we monitor these risks and take appropriate risk-based decisions in a timely fashion, for the benefit of all of our stakeholders.
FAIR TREATMENT OF CUSTOMERS	The fair treatment of customers across the group is our primary responsibility. It is also important to the Chesnara business strategy as it promotes stronger relationships with our customers, distributors and regulators. When applying the terms of our customer contracts, coupled with the developing guidance from local regulators on the application of policy conditions, we place a high priority on taking account of the fair treatment of our customers.
PROVIDE A COMPETITIVE RETURN TO OUR SHAREHOLDERS	As a public company it is imperative that we offer an attractive investment proposition. Given the majority of our investors hold our shares in 'income funds', it is important that we deliver an attractive and sustainable dividend. We also recognise the benefit of being an investment that offers clarity and consistency of performance.
ROBUST REGULATORY COMPLIANCE	Working constructively with our regulators and complying with regulatory requirements is imperative to the delivery of our objectives. The regulators' desire for robust and responsible governance is very much part of our culture and a principal aim of the Chesnara directors.

Maintaining adequate financial resources is at the heart of good business conduct. Effective capital management is a key requirement that underpins our cultural objectives. Further information regarding the group's solvency position is included on pages 31 to 33.

WHAT WE HAVE DONE	THE OUTCOMES
– Embedded governance maps across the group, and commenced governance map alignment within Scildon. – Strengthened the Scildon board with new appointments, including a new CEO and a new CFO. – Delivered against continuity plans in Sweden with internal appointment of new CEO. – Adopted SII across the group, showing a strong group and divisional solvency position throughout the year, and furthered our understanding of the complex capital dynamics of the regime, particularly ensuring the linkage to our risk-based decision making processes. – Delivered inaugural divisional and group SII regulatory narrative reporting to the relevant prudential regulators and continued to enhance our Own Risk and Solvency Assessments (ORSAs), further supporting the group and divisions in making informed risk-based decisions.	– Scildon has started to apply the governance and risk culture practices of Chesnara. – Strengthened controls reducing risk likelihood and impact of adverse outcomes for shareholders and policyholders. – Constructive dialogue with regulators across the different territories in which the group operates. – Better understanding of Solvency II balance sheet provides a stronger linkage between risk, capital and strategy aiding more risk-based decision-making.
– Across the group, we have continued to deliver a good standard of customer service. – The UK division is delivering to its customer strategy implementation in support of regulatory guidelines at the end of 2016. The UK's administrative outsource service partners have delivered within stringent service level requirements. – Service standards in Sweden remain strong, as evidenced by external surveys of brokers undertaken by independent organisations. – Unit-linked policy returns remain competitive based on both fund benchmarks and external unit-linked policy performance surveys. – Where complaints do arise across the group, we continue to manage them in accordance with best regulatory practice. – We closely monitor any regulatory developments to ensure we continue to treat our customers fairly in accordance with regulatory requirements.	– Generally low level of complaints across the group has continued. – For the UK business, preparatory work in the year leaves us in an excellent position to launch a new website and improve our written communications to our customers. – Service standards and customer outcomes in Sweden mean we continue to meet our targets for market share range. – In the Netherlands, Scildon has again received awards from Afdiz, the Dutch broker organisation, for 'Best occupational pension insurer' and 'Best annuity insurer' and was rated second for term insurance.
– Completed the acquisition of LGN at a discount to EcV of 32% and achieved an increase in EcV on acquisition of £65.4m and an IFRS gain of £20.3m. – Delivered EcV growth across the group. – Continued our dividend strategy.	– Dividend track record continues, with 2.98% dividend growth in 2017. – Over the past five years, £124.7m of dividends have been paid. – Total 2017 Economic Value growth of £120.5m, an increase of 20% on the 2016 position.
– Effective implementation of Solvency II and maintenance of robust levels of solvency across the group and all divisions throughout the year. – Positive relationship with the regulators as evidenced by working with the Dutch regulator, the DNB, on the successful LGN acquisition process. – Continued to fully support the work performed by the FCA in relation to its investigation into the disclosure of exit fees in customer correspondence.	– Ongoing constructive relationships with UK, Swedish and Dutch regulators. – Regarding the investigation by the FCA, given its narrow scope we retain our opinion that the outcome should not have a material impact on the company. – Continued adherence to internal governance policies and principles.

BUSINESS REVIEW • UK

The UK division manages c300,000 policies and is in run-off. The division follows an outsourcer-based operating model, with functions such as customer services, investment management and accounting and actuarial services being outsourced. A central governance team is responsible for managing all outsourced operations.

MAXIMISE VALUE FROM EXISTING BUSINESS

01

	BACKGROUND INFORMATION	INITIATIVES & PROGRESS IN 2017
CAPITAL & VALUE MANAGEMENT	– As a closed book, the division creates value through managing the following key value drivers: costs, policy attrition, investment return and reinsurance strategy. – In general, surplus regulatory capital emerges as the book runs off. The level of required capital is closely linked to the level of risk to which the division is exposed. Management's risk-based decision-making process seeks to continually manage and monitor the balance of making value enhancing decisions whilst maintaining a risk profile in line with the board's risk appetite. – At the heart of maintaining value is ensuring that the division is governed well from a regulatory and customer perspective.	– Economic Value growth of £45.9m (21.9%) in the year (before the impact of the dividend paid in the year), driven by the positive investment market experience gains in the year. – Cash of £34.5m has been generated by the division. This includes the positive benefit of £9.0m being transferred out of the S&P with-profit funds, while still ensuring suitable protection for with-profits customers. – Successful embedding of our Capital Optimisation Advisory Group, a sub-set of executive team members who focus on the division's solvency and value management initiatives. – Implemented a change to our assets backing the with-profit funds, focusing on seeking the appropriate balance from a customer and shareholder perspective.
CUSTOMER OUTCOMES	– Treating customers fairly is one of our primary responsibilities. We seek to do this by having effective customer service operations together with competitive fund performance whilst giving full regard to all regulatory matters. This supports our aim to ensure policyholders receive good returns, appropriate communication, and service in line with customer expectations. – During December 2016 the FCA issued a publication 'FG 16/8 Fair treatment of long-standing customers in the life insurance sector'. Our customer strategy incorporates plans to ensure the guidelines within this publication are fully complied with.	– A key focus has been the delivery of a three-year customer strategy plan, which is overseen by the customer committee. During 2017 the following has been delivered: • Designed a refreshed Countrywide Assured website ready for roll out in 2018; • Reviewed our key customer communications in the context of new guidelines issued by the FCA, ready for going live in 2018; • Developed a refreshed product governance framework, ready for the delivery of product reviews during 2018; and • Continued to perform work seeking to get back in touch with customers that we no longer have contact with. – The FCA's investigation into the level of disclosure of exit charges to customers, which was announced in March 2016, remains open. Full ongoing support has been provided to the FCA. We have had seven separate information requests to date. – The 1% exit fee cap on all pension products where the policyholder is over 55 was successfully implemented during the period.
GOVERNANCE	– Maintaining effective governance and a constructive relationship with regulators underpins the delivery of the division's strategic plans. – Having robust governance processes provides management with a platform to deliver the other aspects of the business strategy. As a result, a significant proportion of management's time and attention continues to be focused on ensuring that both the existing governance processes, coupled with future developments, are delivered.	– Strong solvency position has been maintained throughout the year. – Solid delivery of outsourced services. – Continued to develop our General Data Protection Regulation (GDPR) readiness programme in advance of the legislation being implemented in 2018. – Delivered our inaugural Solvency and Financial Condition Report (SFCR) and Regular Supervisory Report (RSR), reports required by Solvency II rules. – Planning commenced regarding the implementation of IFRS 17 'Insurance Contracts', a new insurance accounting standard which was issued in May 2017 and has an effective date of 1 January 2021.

The division has delivered against its objectives. The customer strategy plan is on track and delivering tangible benefits to our customers and the division has continued to deliver strong financial results.

FUTURE PRIORITIES

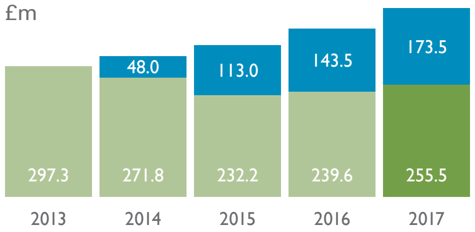
- Continue to identify, assess and subsequently deliver any appropriate actions associated with managing the solvency capital and valuation balance sheet of the division.

- Continuation of the customer strategy implementation plan. Key projects delivery in 2018 are:
  • Roll-out of a new Countrywide Assured website;
  • Roll-out first wave of refreshed key customer communications to ensure ongoing compliance with the most recent FCA guidelines;
  • Deliver our updated approach to performing product reviews.
- Continue to deliver competitive fund performance.

- Ensure we deliver our plans to meet the General Data Protection Regulation (GDPR) well within the timeframes of the regulatory deadline of 25 May 2018.
- Continue to support the FCA in its investigation.
- Continue to develop and start to deliver against implementation plans for 'IFRS 17 Insurance Contracts'. This will be a significant, multi-year project for both the UK division and the wider group.

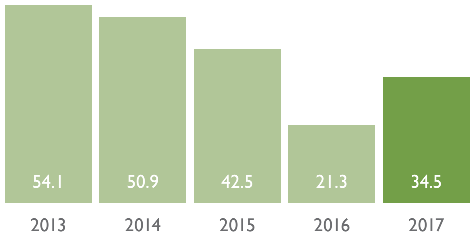
KPIs

Economic Value
Underlying value growth
£m



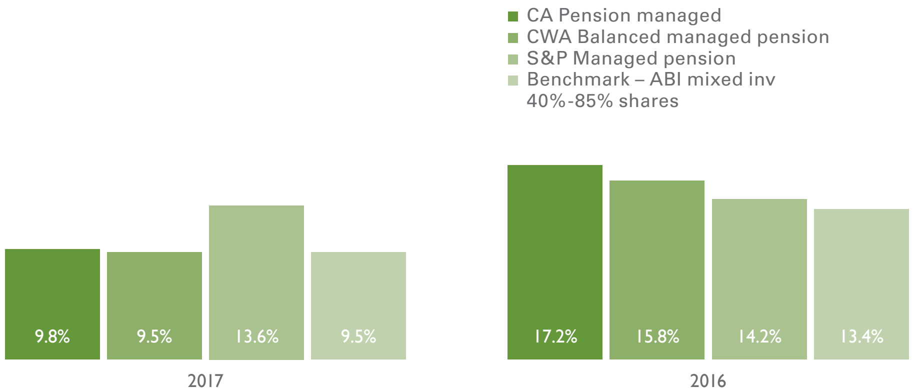
Continued underlying growth in economic value after removing the impact of dividends.

Cash generation
£m



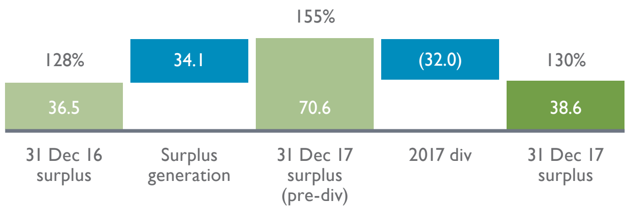
Cash generation of £34.5m continues to support the group's dividend strategy.

Policyholder fund performance:



Our main managed funds continue to be in line with or exceed relevant benchmarks.

SOLVENCY RATIO: **155%**



Solvency remains robust. The surplus generated in year increases the solvency position from 128% to 155%. After the dividend, due to be paid during 2018, the ratio is 130%.

BUSINESS REVIEW • SWEDEN

Movestic is a life and pensions business based in Sweden, and is open to new business. From its Stockholm base, Movestic operates as a challenger brand in the Swedish life insurance market. It offers transparent unit linked pension and savings solutions through brokers and is well-rated within the broker community.

01 MAXIMISE VALUE FROM EXISTING BUSINESS

	BACKGROUND INFORMATION	INITIATIVES & PROGRESS IN 2017
CAPITAL & VALUE MANAGEMENT	– Movestic creates value predominantly by generating growth in the unit linked assets under management (AuM) and by optimising the income that the assets generate, whilst assuring a high quality customer proposition. AuM growth is dependent upon positive client cash flows and positive investment performance. Capital surplus is a factor of both the value and capital requirements and hence surplus can also be optimised by effective management of capital.	– Economic value growth of £24.8m. This includes a £11.4m loss relating to changes in future charge assumptions. This change creates capacity to react, if commercial pressures were to drive fee changes in the future, without there being an adverse profit impact at the point of change. – Cash generation, on constant exchange rates, of £22.1m. – Growth in assets under management of 15.7% (£395m), driven by new business and strong investment market returns. – A new fund management company operating out of Luxembourg, Movestic Fund Management S.A., was established, and funds were migrated in June. – Optimised cost efficiency through the new management company by taking responsibility for additional parts of the value chain. – The life and health business has reported favourable claims development in the year. – Embedded a mass lapse reassurance arrangement.
CUSTOMER OUTCOMES	– Movestic places great importance on providing quality service to both customers and brokers, with simple, clear unit linked products, supported by an attractive and broad investment fund range. The aim of Movestic is to offer policyholders a range of the best funds and management services on the market.	– During the year, Movestic has improved its digital/web interfaces with its end-customers and brokers. The focus on further digitalisation will continue into 2018. – Movestic has continued to develop its in-house advisory service to take care of existing customers. – Average fund performance has exceeded the Swedish stock market. – Movestic has continued to focus on its sustainable investments proposition, and issued the industry's first sustainability guide to savers.
GOVERNANCE	– Movestic operates to exacting regulatory standards and adopts a robust approach to risk management. – Maintaining strong governance is a critical platform to delivering the various value-enhancing initiatives planned by the division.	– As part of its succession planning Movestic appointed a new CEO, Linnéa Ecorcheville, replacing Lars Nordstrand. – During the year, Movestic delivered its inaugural Solvency II narrative reports. – Movestic has continued to deepen its understanding and analysis of the Solvency II capital position. In particular, Movestic has refined its solvency capital requirement calculation models through improved investment data and more refined mass lapse modelling, resulting in a positive SCR benefit of c£10m.

03 ENHANCE VALUE THROUGH PROFITABLE NEW BUSINESS

PROFITABLE NEW BUSINESS	– As an 'open' business, Movestic not only adds value from sales but as it gains scale, it will become increasingly cash generative which will fund further growth or contribute towards the group's dividend strategy. Movestic has a clear sales focus and targets a market share of 10 -15% of the advised occupational pension market. This focus ensures we are able to adopt a profitable pricing strategy.	– New business profits of £11.8m have been generated in the year. – Market shares continue to be within the target range.

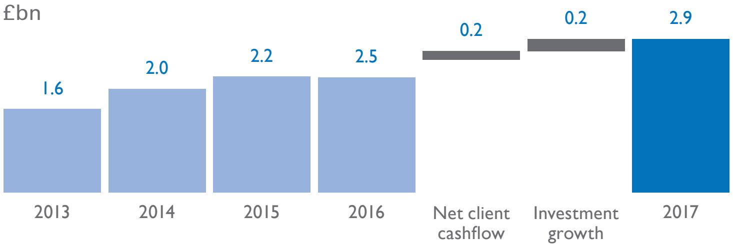
Movestic has delivered a positive set of results across key financial metrics. Its new business operation continues to add value to the group and assets under management growth continues to support the division in achieving its ambitions on scale. That said, the division is not complacent. MiFID II and the Insurance Distribution Directive (IDD) are causing uncertainty in the broker community, the market remains price competitive, and the management team has a busy period ahead in delivering its ongoing digitalisation programme.

FUTURE PRIORITIES

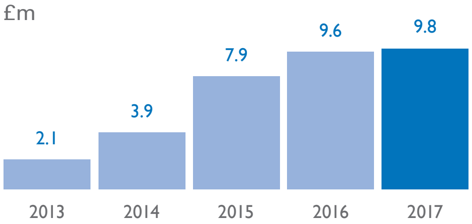
- Deliver against plans to continue to modernise and automate processes. This is designed to give better broker experience and deliver cost efficiencies.
- Provide a sustainable and predictable dividend to Chesnara.
- Continue to focus on generating positive client cash flows by:
  - maintaining lapse levels within valuation assumptions; and
  - strategic pricing to maintain transfers-in to 2017 levels or above.
- Optimise the pricing model to changing market conditions.

KPIs ALL COMPARATIVES HAVE BEEN PRESENTED USING 2017 EXCHANGE RATES

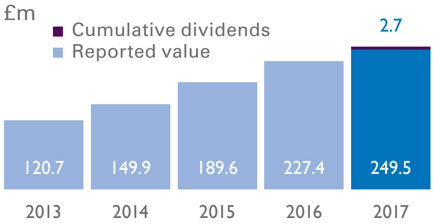
Growth in assets under management:
£bn



IFRS profit
£m

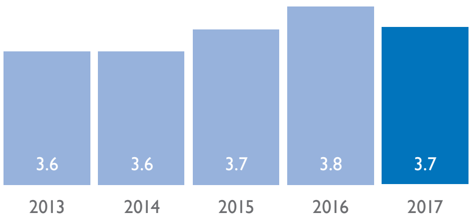


Underlying value growth
£m



- Fund range development in line with customer and market requirements.
- Deliver competitive unit linked fund returns.
- Improve digital business and the relationship with the end user.
- Relaunch Life & Health business.

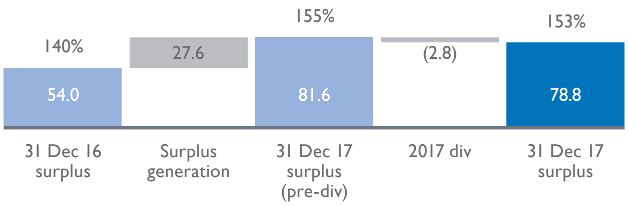
Broker assessment rating



2017 POLICYHOLDER AVERAGE INVESTMENT RETURN:
8.2%
(SWEDISH STOCK MARKET 6.4%)

- Continue to deepen the understanding of the Solvency II dynamics.
- Improve efficiency of regulatory reporting routines.
- Commence and deliver IFRS 17 'Insurance contracts' implementation programme.

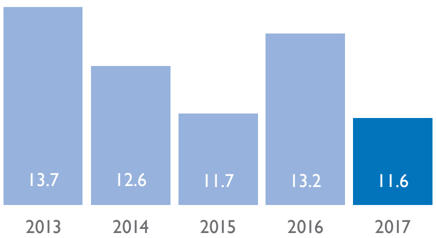
SOLVENCY RATIO: **155%**



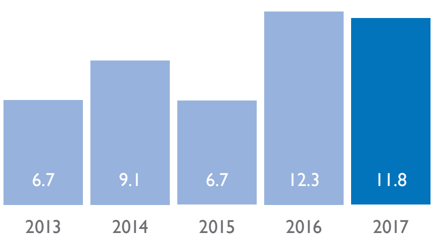
Solvency remains strong. Surplus of £27.6m in the year increases the solvency ratio from 140% to 155%. After the 2017 dividend, to be paid in 2018, the ratio is 153%.

- Continue to focus on writing new business within our target range.
- Ongoing digitalisation of processes to improve broker experience.
- Focus on increasing brand awareness.

Occupational pension market share %



New business profit
£m



BUSINESS REVIEW • NETHERLANDS

The Netherlands division includes the businesses of both Waard and Scildon, with Scildon being acquired during the year. Since acquisition the priority has been to integrate Scildon into the wider group, with significant progress in aligning the risk and governance frameworks, financial reporting processes and investment strategy. Scildon sold a number of indirect investments in equity holdings as part of aligning its investment strategy, resulting in a reduction in solvency capital requirements. Scildon has produced a solid set of results, including a modest new business profit, and Waard has continued to deliver in line with expectations. Both businesses have strong solvency ratios, supporting the payment of dividends to Chesnara.

01 MAXIMISE VALUE FROM EXISTING BUSINESS

	BACKGROUND INFORMATION	INITIATIVES & PROGRESS IN 2017
CAPITAL & VALUE MANAGEMENT	– Both Waard and Scildon have a common aim to make capital available to Chesnara to fund further acquisitions or to contribute to the dividend funding. Whilst their aims are common, the dynamics by which the businesses add value do differ: • Waard is in run-off and has the benefit that the capital requirements reduce over time in-line with the attrition of the book. • As an 'open business' Scildon's capital position does not benefit from book run-off. It therefore adds value and creates surplus capital through writing new business and by efficient operational management and capital optimisation.	– Post acquisition equity de-risk aligns the investment of shareholder funds with group policy and risk appetite. Consequence was a reduction in Scildon capital requirements. – Guarantees have been removed from new business. – Successful transfer of Hollands Welvaren Leven into Waard Leven, thereby releasing capital. – Waard and Scildon ended the period with healthy pre-dividend solvency ratios of 613% and 258% respectively before deducting the proposed 2017 year end dividends. – EcV growth of £17.1m, consisting of £5.1m for Waard and £12.0m for Scildon since acquisition. – Cash of £25.3m has been generated, with £10.5m from Waard and £14.8m from Scildon. – IFRS profits of £23.6m, including £18.4m earned by Scildon since acquisition, largely due to favourable investment conditions which have not been offset by reserve movements.
CUSTOMER OUTCOMES	– Great importance is placed on providing customers with high quality service and positive outcomes. – Whilst our ultimate priority is the end customer, in Scildon we also see the brokers who distribute our products as customers and developing processes to best support them is a key focus.	– Scildon received awards for 'Best occupational pension insurer' and 'Best annuity insurer', and was rated second for term insurance, according to the Dutch broker organisation, Adfiz. – The annual performance research for consumers shows high scores. – Scildon replaced some non-performing funds.
GOVERNANCE	– The Waard Group and Scildon operate in a regulated environment and comply with rules and regulations both from a prudential and from a financial conduct point of view.	– Both companies have successfully delivered their inaugural Solvency II reporting. – Progressed the alignment of the Scildon governance and risk management framework to Chesnara practices. – Scildon appointed Gert Jan Fritzsche as CEO and Rene Tuitert as CFO, who started in March 2018. – Waard appointed Lorens Kirchner and Andy Schaut as CEO and CFO respectively in 2017.

03 ENHANCE VALUE THROUGH PROFITABLE NEW BUSINESS

PROFITABLE NEW BUSINESS	– The acquisition of Scildon has added a 'New business' dimension to the Dutch business model. Scildon sells protection, individual savings and group pensions contracts via a broker-led distribution model. The aim is to deliver meaningful value growth from realistic market share. Having realistic aspirations regarding volumes means we are able to pursue a profitable pricing strategy. New business also helps the business maintain scale and hence contributes to unit cost management.	– LGN has been successfully rebranded to Scildon with no apparent adverse impact on new business levels or broker support, as shown by levels of Annual Premium Equivalent remaining consistent between 2016 and 2017. – There have been modest new business profits of £1.9m in the year. – Market share for the core protection business is towards the middle of our 5 - 10% range. – New business processes have been reviewed with improvement opportunities identified which will be mutually beneficial to brokers, customers and profits. These smart process changes aim to create more commercially meaningful levels of new business profit.

2018 will see further development of the Scildon business, with the business planning process helping to identify key strategic priorities to achieve this. These priorities include enhancing the profitable and scalable new business operations and refining the product offering to meet the needs and demands of the market. Underpinning this, system and process developments will be implemented to enhance the customer and broker experience thus developing an organisation with a structure and culture that supports value generation.

FUTURE PRIORITIES

- Both businesses will pay a dividend to Chesnara in spring 2018 in respect of the 2017 year end.
- In line with our integration plan, areas of Scildon requiring investment have been identified. This investment will strengthen future cash generation and value growth and one-off costs for these developments have been provided for. Plans include:
  - Process and value for money improvements such as increased levels of 'straight through' processing;
  - Continuation of existing IT infrastructure developments to facilitate efficient processes;
  - Enhancing new business profitability and launching appropriate products to market in a timely fashion; and
  - Continual assessment of the business model to ensure an optimal balance between returns generated versus the solvency capital requirements.

- Enhancing and developing existing processes and customer experiences and the underlying infrastructure.
- Organise discussions with brokers to support the development of our processes in conjunction with their requirements.
- Perform a customer assessment and use the outcome to improve quality of service.
- Introduce chat-function on new website, improve navigation to documents and disclose more relevant information on-line.
- Continue to improve Scildon's brand recognition.

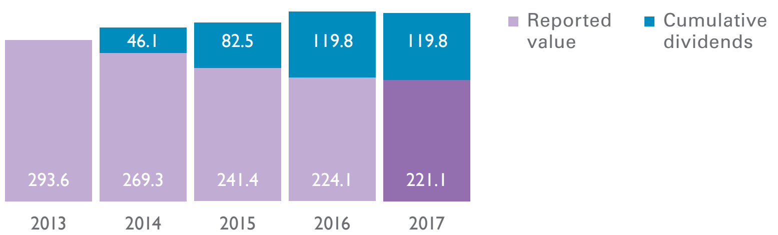
- The continued focus is to fully align and integrate the governance routines such as the Risk Management Framework, Business Planning, MI production and ensuring local processes conform to the Chesnara governance map where appropriate.

- With solid new business foundations, management actions are planned over the next two years to generate a more commercially meaningful level of new business profit.
- One of the objectives of the actions is to move the market share for protection business towards the top end of the 5-10% target range.
- Whilst maintaining the focus on protection, Scildon plan to increase the assets under management for pension business and remain market leader in the growing unit linked market.

KPIs ALL COMPARATIVES HAVE BEEN PRESENTED USING 2017 EXCHANGE RATES

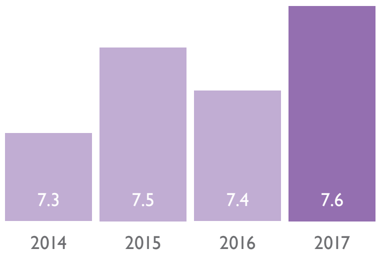
Scildon value growth

Underlying value growth £m



Scildon has a track record of delivering value growth enabling dividend distribution to the parent company and will pay its first dividend to Chesnara plc in April 2018.

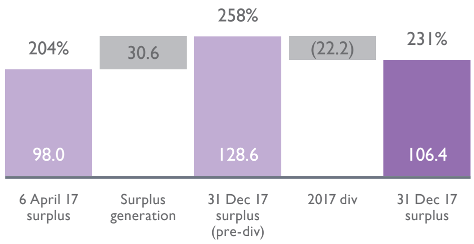
Scildon client satisfaction rating



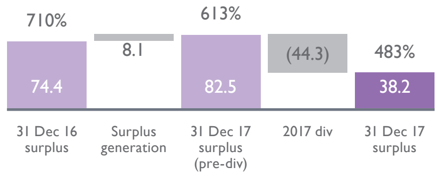
WINNAAR PARTICULIER LIJFRENTE

WINNAAR ZAKELIJK PENSIOEN

SOLVENCY RATIO SCILDON: 258%

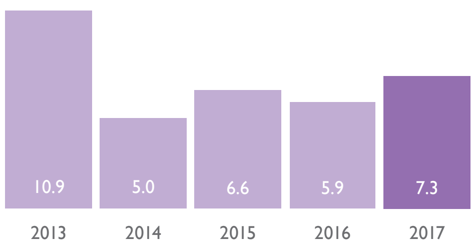


SOLVENCY RATIO WAARD: 613%



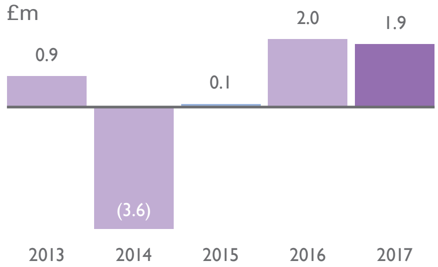
Solvency is strong in both businesses. £30.6m and £8.1m of surplus have been generated by Scildon and Waard respectively. After the 2017 dividend, including the interim dividend paid by Waard to fund the LGN acquisition, solvency ratios are 231% and 483%.

Term assurance market share %



New business profit

£m



02 ACQUIRE LIFE & PENSIONS BUSINESSES

On 5 April 2017 we completed the acquisition of Legal & General Nederland (subsequently renamed Scildon).

The completion of Scildon, which had an economic value of €237.5m at the point of acquisition, results in the group having 39% of its Economic Value in the Netherlands.

This acquisition continues our acquisition strategy in the Netherlands. We believe this deal leaves us with sufficient scale and presence to progress further value adding deals in the Dutch market.

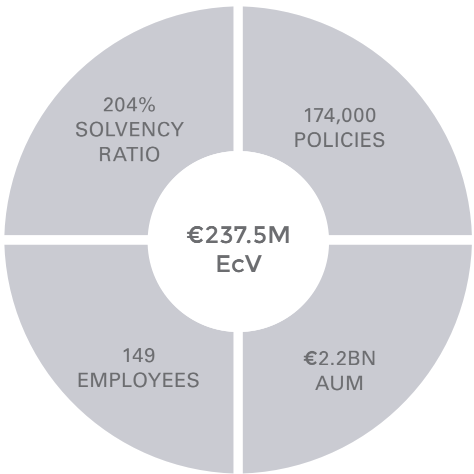
HIGHLIGHTS OF LGN ACQUISITION:

- Completion purchase price of €161.2m
- Economic value of €237.5m at acquisition, representing a purchase price discount of 32%
- The impact of the acquisition, after taking account of the equity de-risk programme, is to increase the solvency surplus of the group by £4.7m
- Integration plans progressing well, with equity de-risk programme completed

ACQUISITION OF LEGAL & GENERAL NEDERLAND

About Scildon

- A long established, award winning specialist insurer in the Netherlands.
- Policy base predominantly individual protection and savings contracts.
- Writes new business and sells protection, individual savings and group pensions contracts via a broker-led distribution model.
- Well-capitalised, with a solvency ratio of 204% at acquisition. It applies the standard formula with no transitional measures.



Our post acquisition integration work is progressing very well. For more information see the Netherlands Business Review on p28 to 29.

IMPACT ON THE GROUP

CASH GENERATION

- Post acquisition cash generation expected to emerge at levels which would more than cover incremental funding costs, thereby creating a net positive impact on group cash.

VALUE

- Scildon was purchased at a 32% discount to its economic value, resulting in a day 1 gain of £65.4m.
- The Netherlands now makes up 39% of group EcV.

CUSTOMER OUTCOMES

- Continuity of Scildon's operating model will ensure existing high quality customer outcomes are not compromised.

RISK APPETITE

- The risks associated with Scildon align with the appetite of the Chesnara group following the equity de-risk activity.
- Our integration plans include bringing Scildon within the group's risk management framework.

POLICY NUMBERS

- Scildon's 177,000 policies at 31 December 2017 result in the group now managing a policy base of over 1.1m, of which 27% are in the Netherlands.

SOLVENCY

- The acquisition gives rise to an increase in the absolute level of group capital above its capital requirements, after taking account of the equity de-risk programme.

FUNDING AND CAPITAL

- Deal financed through £66.7m of equity after costs, £49.0m of incremental debt and £21.9m of Chesnara's own cash.
- Our group gearing ratio, now 19.8%, remains well within our risk appetite.
- Further equity raising capacity is expected to be available for future deals.

ACQUISITION OUTLOOK

- Scildon contributes positively to the acquisition outlook due to increased scale and presence in the Netherlands. We believe we are well-positioned to take advantage of any future acquisition opportunities.
- Regarding the UK, we have seen a gradual increase in closed book market activity which, in our view, is driven in part by reduced uncertainty regarding Solvency II and regulatory developments.
- The environment in which European life insurance companies operate continues to increase in complexity. For example, 'IFRS 17 Insurance Contracts' was issued this year, which is a fundamental overhaul of the way in which insurance contracts are accounted for. We believe this additional complexity will potentially drive further consolidation as institutions seek to remove operational complexity and potentially release capital or generate funds from capital intensive life and pension businesses.
- Chesnara is a well-established life and pensions consolidator with a proven track record. Our financial foundations are strong, we have a proven and stringent acquisition assessment model, and we continue to have strong support from shareholders and lending institutions to progress our acquisition strategy. We believe our operating model has the flexibility to accommodate a wide range of potential target books. Our good network of contacts in the adviser community, who understand the Chesnara acquisition model, ensures we are aware of most viable opportunities in the UK and Western Europe. With this in mind, we are confident that we are well positioned to continue the successful acquisition track record in the future.
- To prepare for future deals, we have been working closely with our current debt provider, RBS, to convert our existing debt arrangement into a syndicated facility. This will provide access to higher levels of debt financing from a wider panel of lenders, which in turn will enable us to fulfill our appetite of financing future deals up to the maximum levels of gearing set out in our debt and leverage policy, without being restricted by the lending capacity of one individual institution. This new syndicated facility is expected to be operational during April 2018.

CAPITAL MANAGEMENT • SOLVENCY II

WHAT IS SOLVENCY AND CAPITAL SURPLUS?

- Solvency is a measure of how much the value of the company exceeds the level of capital it is required to hold.
- The value of the company is referred to as its 'Own Funds' (OF) and this is measured in accordance with the rules of the Solvency II regime.
- The capital requirement is also defined by Solvency II rules and the primary requirement is referred to as the Solvency Capital Requirement (SCR).
- Solvency is expressed as either a ratio: **OF/SCR** % or as an absolute surplus **OF less SCR**

SOLVENCY SURPLUS > CASH GENERATION

Subject to ensuring other constraints are managed, surplus capital is a useful proxy measure for liquid resources available to fund matters such as dividends, acquisitions or business investment. As such, Chesnara defines cash generation as the movement in surplus, above management buffers, during the period.

MORE ABOUT OWN FUNDS

WHAT ARE OWN FUNDS?

A valuation which reflects the net assets of the company and includes a value for future profits expected to arise from in-force policies.

The Own Funds valuation is deemed to represent a commercially meaningful figure with the exception of:

Contract boundaries
Solvency II rules do not allow for the recognition of future cash flows on certain policies despite a high probability of receipt.

Risk margin
The Solvency II rules require a 'risk margin' liability which is deemed to be above the realistic cost.

Restricted with-profit surpluses
Surpluses in the group's with-profit funds are not recognised in Solvency II Own Funds despite their commercial value.

We define Economic Value (EcV) as being the Own Funds adjusted for the items above. As such our Own Funds and EcV have many common characteristics and tend to be impacted by the same factors.

Transitional measures, introduced as part of the long-term guarantee package when Solvency II was introduced, are available to temporarily increase Own Funds. Chesnara does not take advantage of such measures.

HOW DO OWN FUNDS CHANGE?

Own Funds (and Economic Value) are sensitive to economic conditions. In general, positive equity markets and increasing yields lead to OF growth and vice versa. Other factors that improve Own Funds include writing profitable new business, reducing the expense base and improvements to lapse rates.

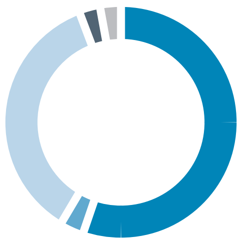
MORE ABOUT THE CAPITAL REQUIREMENT

WHAT IS CAPITAL REQUIREMENT?

The Solvency Capital Requirement can be calculated using a 'standard formula' or 'internal model'. Chesnara adopts the 'standard formula'.

The standard formula requires capital to be held against a range of risk categories. The following chart shows the categories and their relative weighting for Chesnara:

- Market risk
- Counterparty default risk
- Life underwriting risk
- Health underwriting risk
- Operational risk



THERE ARE THREE LEVELS OF CAPITAL REQUIREMENT:

Minimum dividend paying requirement
The board sets a solvency level above the SCR which creates a more prudent level applied when making dividend decisions.

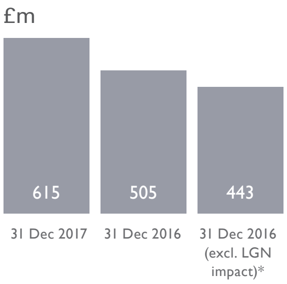
Solvency capital requirement
Amount of capital required to withstand a 1 in 200 event. The SCR acts as an intervention point for supervisory action including cancellation or the deferral of distributions to investors.

Minimum capital requirement (MCR)
The MCR is between 45% and 25% of the SCR. At this point Chesnara would need to submit a recovery plan which if not effective within three months may result in authorisation being withdrawn.

HOW DOES THE SCR CHANGE?

Given the largest component of Chesnara's SCR is market risk, changes in investment mix or changes in the overall value of our assets has the greatest impact on the SCR. For example, equity assets require more capital than low risk bonds. Also, positive investment growth in general creates an increase in SCR. Book run-off will tend to reduce SCR but this will be partially offset by an increase as a result of new business.

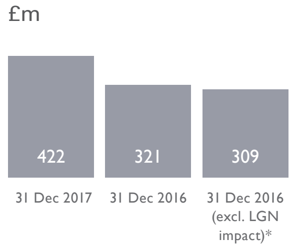
CHESNARA GROUP OWN FUNDS



	Group solvency ratio	Group solvency surplus
31 Dec 2017	146%	£193.4m
31 Dec 2016	158%	£184.7m
31 Dec 2016 (excl. LGN impact*)	144%	£134.8m

*Excluding impact of equity raise and acquisition costs for LGN acquisition.

CHESNARA GROUP SCR

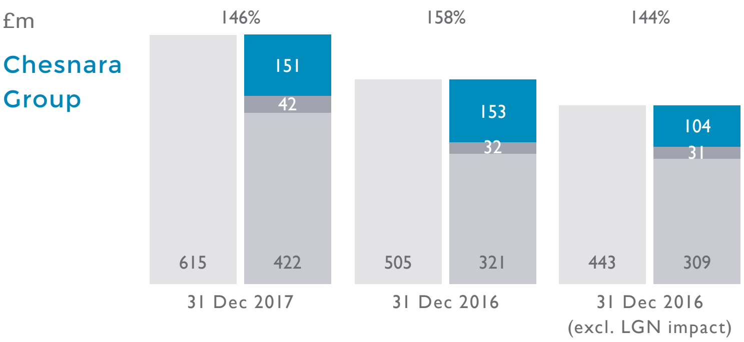


CAPITAL MANAGEMENT • SOLVENCY II

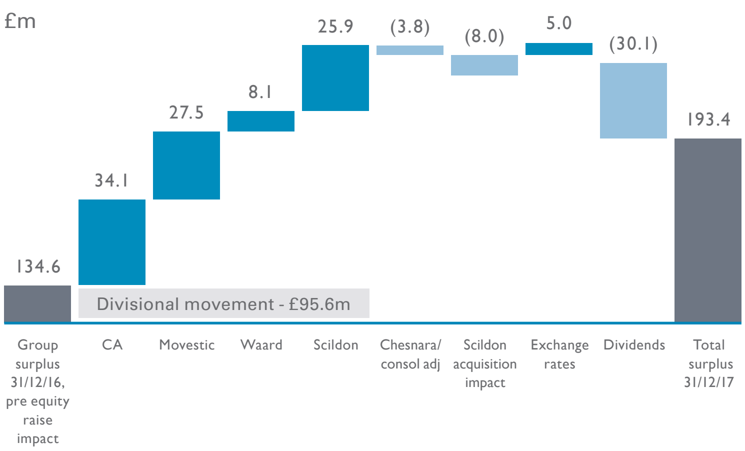
(CONTINUED)

We are well capitalised at both a group and subsidiary level, and we have not used any elements of the long term guarantee package.

SOLVENCY POSITION



SOLVENCY SURPLUS



THE COMMENTARY BELOW HIGHLIGHTS KEY POINTS IN THE YEAR, STARTING WITH THE PRE-LGN STARTING POSITION

Surplus: The solvency position of the group remains strong, at 146%. The group has £151m of distributable surplus over and above the internal capital management policy. Each division has contributed positively to group surplus. The graph shows that the Scildon acquisition has reduced the solvency surplus available at a group level by £8.0m. This was expected and does not include the impact of the equity de-risking, which was delivered post acquisition. Adjusting for this, the 'day 1' impact of the Scildon acquisition has resulted a small positive contribution to the overall group solvency position of £4.7m.

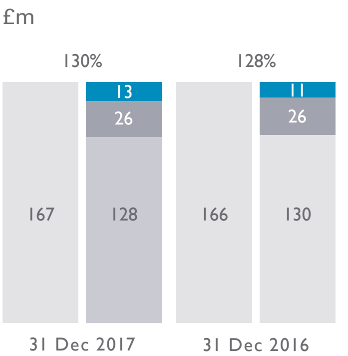
Dividends: The closing solvency position is stated after deducting the £19.6m proposed dividend (31 December 2016: £19.0m), and also reflects the payment of an interim dividend of £10.5m.

Own Funds: A large contributor to the Own Funds growth of £172m is a £54m 'day 1' gain arising on the acquisition of Scildon, coupled with the equity raise to support this acquisition of £62m. The operating companies have collectively generated £88m of additional own funds. The own funds movement recognises the full year dividend burden of £30.1m.

SCR: The SCR has increased by £111m in the year. £109m of this arose from the 'day 1' acquisition impact of Scildon.

The graphs on this page present a divisional view of the solvency position which may differ to the position of the individual insurance company(ies) within that division. Please note that prior year figures have been restated using 31 December 2017 exchange rates.

UK



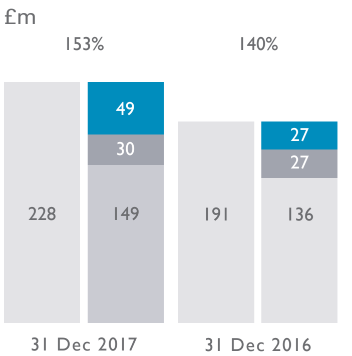
Surplus: £13m above board's capital management policy.

Dividends: The solvency position is stated after deducting £32.0m proposed dividend (31 December 2016: £30.0m).

Own Funds: Positive growth before dividends of £32.4m, driven largely by positive equity markets in the year.

SCR: Broadly flat for the year. Insurance risk capital has reduced in line with book run off, off-set by increases in market risk capital driven by equity growth.

SWEDEN



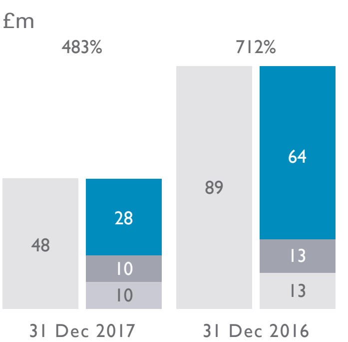
Surplus: £49m above board's capital management policy.

Dividends: The solvency position is stated after deducting £2.8m proposed dividend (31 December 2016: £2.7m).

Own Funds: Positive growth before dividends of £39.9m, driven largely by positive investment returns in the year, offset by the negative impact of changing assumptions regarding future fee income.

SCR: Increased by £13m, largely due to growth in assets under management.

NETHERLANDS – WAARD



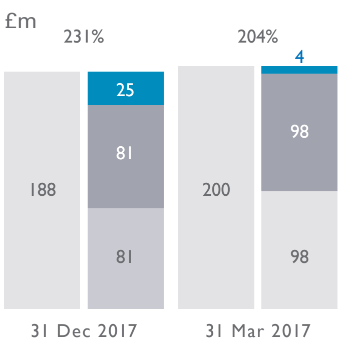
Surplus: £28m above board's capital management policy.

Dividends: The solvency position is stated after deducting £13.0m proposed year end dividend and £32.1m paid in the year (31 December 2016: £nil).

Own Funds: Positive growth before dividends of £6.8m, driven by solid investment returns in the year and refined assumptions.

SCR: SCR has reduced slightly, largely due to decreased counterparty exposure through reduced cash holdings.

NETHERLANDS – SCILDON



Surplus: £25m above board's capital management policy.

Dividends: The solvency position is stated after deducting £22.2m proposed dividend (31 December 2016: £nil).

Own Funds: Positive post acquisition growth before dividends of £10.0m. Underlying growth owing to favourable returns from fixed interest assets, offset by some one-off post acquisition expense strengthening.

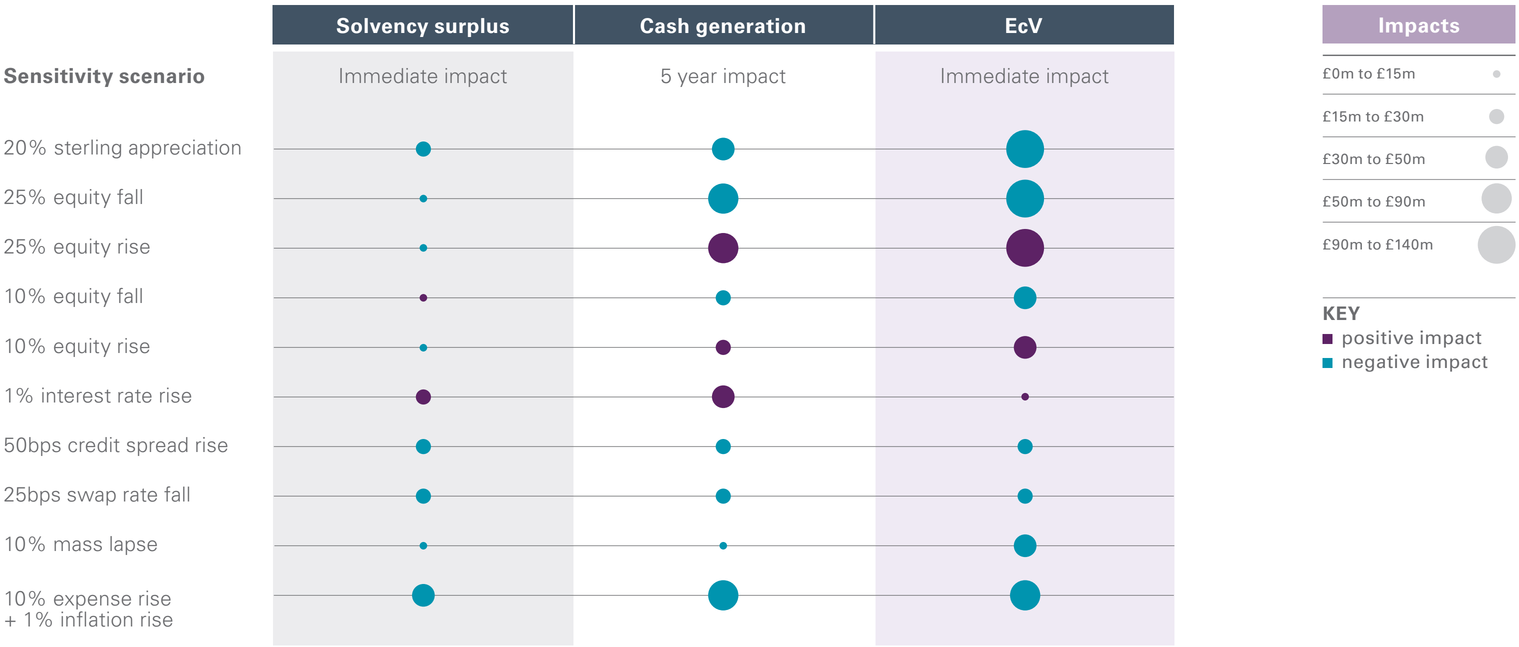
SCR: Fall largely driven by reduction in equity holdings.

KEY ■ Own Funds (Post Div) ■ SCR ■ Buffer ■ Distributable surplus above buffer

CAPITAL MANAGEMENT • SENSITIVITIES

The group's solvency position can be affected by a number of factors over time. As a consequence, the group's EcV and cash generation, both of which are derived from the group's solvency calculations, are also sensitive to these factors.

The diagram below provides some insight into the immediate and longer term impact of certain sensitivities that the group is exposed to, covering solvency, cash generation and economic value. As can be seen, EcV tends to take the 'full force' of adverse conditions whereas cash generation is often protected in the short term and to a certain extent in the longer term due to compensating impacts on our required capital.



INSIGHT*

20% sterling appreciation

A material sterling appreciation reduces the value of surplus in our overseas divisions, and hence has an immediate material day 1 impact on group cash generation. It also reduces the value of projected Own Funds growth in our overseas divisions and also reduces the value of overseas investments CA holds in its linked funds.

Equity sensitives

The impact of an equity fall causes the Own Funds to fall and the SCR also falls as the value of the funds exposed to risk is lower. Since the two movements largely offset each other, the net impact on surplus is small. In an equity rise, the Own Funds and SCR both rise and, again, the impact on balance sheet surplus is small. The impacts are not symmetrical due to the use of management actions and differences in the application of tax depending on the direction of the stress. The EcV impacts are more intuitive as they are more directly linked to the Own Funds impact. The impact on future growth builds on the immediate impact as future returns are directly impacted by the rise/fall in fund values under the sensitivity. The divisions that most contribute to equity sensitivities are CA and Movestic due to their large amounts of unit-linked business.

1% interest rate rise

An interest rate rise is generally positive across the group. The total cash generation impact across the group of £42.1m is broadly equal across CA, Movestic and Scildon.

50bps credit spread rise

A credit spread rise has a notable adverse impact on day 1 cash surplus and future cash generation in Scildon, largely as a result of the extent of corporate bond holdings that form part of the asset portfolios backing non-linked insurance liabilities. The impact on the other divisions is far less severe.

25bps swap rate fall

This sensitivity measures the impact of a fall in the swap discount curve with no change in the value of assets. The result is that liability values increase in isolation. The most material impacts are on CA and Scildon due to the size of the non-linked books.

10% mass lapse

For this sensitivity, there is only a small immediate impact on surplus as any the reduction in Own Funds is negated by a reduction in the SCR. However, with fewer policies on the books there is less potential for future profits. The division most affected is Movestic, largely because as a unit-linked business the loss in future AMCs following a mass lapse hits Own Funds by more than the associated reduction in SCR.

10% expense rise + 1% inflation rise

The expense sensitivity hits the solvency position immediately as the increase in future expenses and inflation is capitalised into the balance sheet. CA is affected more than the other divisions owing to the governance structure of the business.

*BASIS OF PREPARATION ON REPORTING

Although it is not a precise exercise, the general aim is that the sensitivities modelled are deemed to be broadly similar (with the exception that the 10% equity movements are naturally more likely to arise) in terms of likelihood. Whilst the sensitivities provide a useful guide, in practice, how our results react to changing conditions is complex and the exact level of impact can vary due to the interactions of events and the starting position.

FINANCIAL REVIEW

The key performance indicators are a reflection of how we have performed in delivering our three strategic objectives and our core culture and values. 2017 has delivered strong results across all metrics, with cash generation, pre-tax EcV earnings and IFRS profits all in excess of prior year and plan, with a closing EcV of £723.1m.

IFRS PRE-TAX PROFIT

£89.6M 2016: £40.7M

What is it?

The presentation of the results in accordance with International Financial Reporting Standards (IFRS) aims to recognise the profit arising from the longer-term insurance and investment contracts over the life of the policy.

Why is it important?

IFRS profit is an indicator of the value that has been generated within the long-term insurance funds of the divisions within the group, and is a statutory measure used both internally and by our external stakeholders in assessing the performance of the business. IFRS profit is an indicator of how we are performing against our stated strategic objective of 'maximising value from the existing business' and can also be impacted by one-off gains arising from delivering against our stated objective of 'acquiring life and pensions businesses'.

Risks

The IFRS profit can be affected by a number of our principal risks and uncertainties as set out on p43 to 45. In particular, volatility in equity markets and bond yields can result in volatility in the IFRS pre-tax profit, and foreign currency fluctuations can affect total comprehensive income.

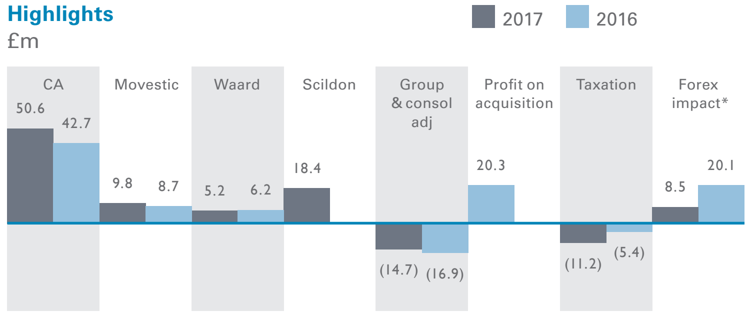
IFRS TOTAL COMPREHENSIVE INCOME

£86.9M 2016: £55.4M

Further detail on page 36

Highlights

£m



*includes other comprehensive income

- Strong pre-tax results across all segments.
- IFRS pre-tax profit of £89.6m significantly ahead of prior year and plan. Pre-tax profit, excluding the profit on acquisition of LGN, was £69.3m and still represents a 70% uplift on prior year.
- Operating profits of £38.4m are the foundation of the result, supported by economic earnings of £30.9m driven largely by equity markets.
- Total comprehensive income includes a foreign exchange gain of £8.3m (2016: £20.1m gain) relating to sterling's depreciation against both the euro and Swedish krona.

CASH GENERATION

£28.6M 2016: £85.4M*

What is it?

Cash generation is a measure of how much distributable cash has been generated in the period. Cash generation is driven by the change in solvency surplus in the period, taking into account board-approved capital management policies.

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-paying capacity and acquisition strategy. Cash generation can be a strong indicator of how we are performing against our stated objective of 'maximising value from the existing business'. However, our cash generation is always managed in the context of our stated value of maintaining strong solvency positions within the regulated entities of the group.

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 43 to 45. Whilst cash generation is a function of the regulatory surplus, as opposed to the IFRS surplus, they are impacted by similar drivers, 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.

*Includes one-off impact of £48.9m in respect of LGN equity raise

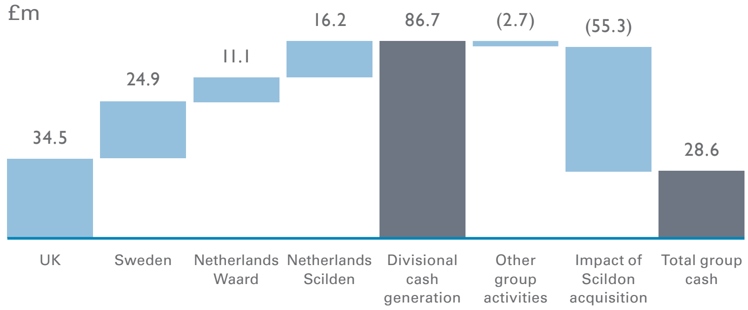
DIVISIONAL CASH GENERATION

£86.7M 2016: £34.3M

Further detail on page 37

Highlights

£m



Divisional cash

- Significant cash contributions from all businesses in the year.
- Overall divisional cash generation is in excess of prior year and plan, underpinned by performance in the UK and Sweden.

Total cash generation

- The completion of the Scildon deal in isolation had a £55.3m negative cash impact, because consideration exceeded the surplus acquired. This is largely offset by the equity raised to fund the acquisition recognised as a positive in the 2016 cash figures, resulting in an adverse end to end impact of £6.4m.

These two pages provide a 'snapshot' of our key financial measures and some insight into what's driving the outcome in 2017. Further analysis can be found on pages 36 to 39.

ECONOMIC VALUE (ECV)

£723.1M 2016: £602.6M

Further detail on page 39

What is it?

Economic Value (EcV) was introduced following the introduction of Solvency II at the start of 2016, with EcV being derived from Solvency II Own Funds. Conceptually, EcV is broadly similar to EEV in that both reflect a market-consistent assessment of the value of existing insurance business, plus adjusted net asset value of the non-insurance business within the group.

Why is it important?

EcV aims to reflect the market-related value of in-force business and net assets of the non-insurance business and hence is an important reference point by which to assess Chesnara's intrinsic value. A life and pensions group may typically be characterised as trading at a discount or premium to its economic value. Analysis of EcV provides additional insight into the development of the business over time.

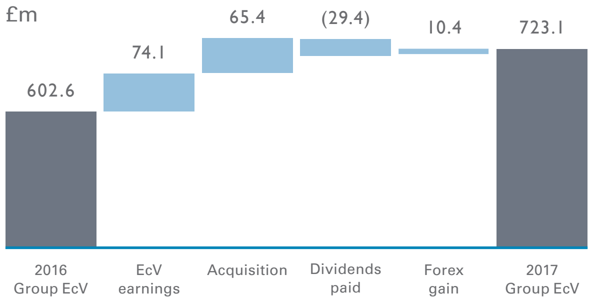
The EcV development of the Chesnara group over time can be a strong indicator of how we have delivered to our strategic objectives, in particular the value created from acquiring life and pensions businesses and enhancing our value through writing profitable new business. It ignores the potential of new business to be written in the future (the franchise value of our Swedish and Dutch businesses) and the value of the company's ability to acquire further businesses.

Risks

The Economic Value of the group is affected by economic factors such as equity and property markets and yields on fixed interest securities. In addition, the EcV position of the group can be materially affected by exchange rate fluctuations. For example a 20.0% weakening of the Swedish krona and euro against sterling would reduce the EcV of the group by 18.5%, based on the composition of the group's EcV at 31 December 2017.

Highlights

£m



- Economic value at the end of the year in excess £723m, having increased by £120.5m during the period.
- Strong underlying earnings of £74.1m generated in the year.
- Overall growth includes a gain of £65.4m realised on the acquisition of LGN in April.
- Foreign exchange gains also contribute to the overall growth, offset by dividend payments.
- EcV earnings were underpinned by significant economic results and the gain delivered on the acquisition of LGN.

ECV EARNINGS NET OF TAX

£139.5M 2016: £72.5M

Further detail on page 38

What is it?

In recognition of the longer-term nature of the group's insurance and investment contracts, supplementary information is presented that provides information on the Economic Value of our business.

The principal underlying components of the Economic Value 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; and
- The impact of acquisitions.

Why is it important?

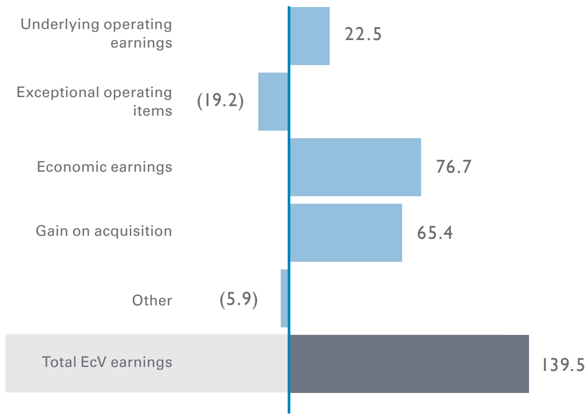
By recognising the market-related value of in-force business (in-force value), a different perspective is provided in the performance of the group and on the valuation of the business. Economic Value earnings are an important KPI as they provide a longer-term measure of the value generated during a period. The Economic Value earnings of the group can be a strong indicator of how we have delivered against all three of our core strategic objectives. This includes new business profits generated from writing profitable new business, Economic Value profit emergence from our existing businesses, and the Economic Value impact of acquisitions.

Risks

The EcV earnings of the group can be affected by a number of factors, including those highlighted within our principal risks and uncertainties and sensitivities analysis as set out on pages 43 to 45 and 33 respectively. In addition to the factors that affect the IFRS pre-tax profit and cash generation of the group, the EcV 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 EcV affect our long-term view of the future cash flows arising from our books of business.

Highlights

£m



- EcV earnings of £139.5m in the year, driven by a combination of strong underlying economic earnings supported by the substantial gain realised on the acquisition of LGN in April.
- Strong underlying operating profits were adversely affected by two non-recurring items. The Movestic result includes an £11.4m impact relating to changes in future charge assumptions if, as expected, commercial pressures were to drive fee changes in the future. In addition, we have provided £7.8m to cover the Scildon development programme.
- Economic earnings primarily driven by strong equity market performance and returns on assets across Europe in the period.

IFRS

IFRS PRE-TAX PROFIT

£89.6M 2016: £40.7M

IFRS TOTAL COMPREHENSIVE INCOME

£86.9M 2016: £55.4M

Executive summary

The group IFRS results reflect the natural dynamics of the segments of the group, which can be characterised in three major components:

(1) Stable core: At the heart of surplus, and hence cash generation, are the core CA and Waard Group segments. The requirements of these books are to provide a predictable and stable platform for the financial model and dividend strategy. As closed books, the key is to sustain this income source as effectively as possible. The IFRS results below show that the stable core continues to deliver against these requirements.

(2) Variable element: Included within the CA segment is the Save & Prosper book. This can bring an element of short-term earnings volatility to the group, with the results being particularly sensitive to investment market movements due to product guarantees. The IFRS results of Scildon are potentially relatively volatile although this is primarily due to reserving methodology rather than 'real world' value movements.

(3) Growth operation: The long-term financial model of Movestic and Scildon is based on growth, with levels of new business and premiums from existing 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.

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

	2017 £m	2016 £m	Note
CA	50.6	42.7	1
Movestic	9.8	8.7	2
Waard Group	5.2	6.2	3
Scildon	18.4	–	4
Chesnara	(12.1)	(9.7)	5
Consolidation adjustments	(2.6)	(7.2)	6
Profit before tax and profit on acquisition	**69.3**	**40.7**	
Profit on acquisition of Scildon	20.3	–	4
Profit before tax	**89.6**	**40.7**	
Tax	(11.2)	(5.4)	
Profit after tax	**78.4**	**35.3**	
Foreign exchange translation differences	8.3	20.1	7
Other comprehensive income	0.2	–	8
Total comprehensive income	**86.9**	**55.4**	

Note 1: The CA segment has reported results for the year in excess of those in 2016. Positive economic conditions contributed £22.2m to the result, of which £11.9m related to a reduction in the cost of guarantees within the S&P book. This was mainly driven by favourable equity returns in the year and to a lesser extent valuation interest rate movements.

Note 2: Movestic has reported a strong trading result, improving on the previous year. This was principally driven by strong growth in assets under management which in turn generated increased fund rebates and investment related fee income within the Pensions and Savings division. This was further boosted by higher premium volumes and favourable claims experience within the Life and Health division, offset slightly by an expense overrun, due to the higher than expected use of consultant resource in the year.

Note 3: The Waard Group result is in line with expectations. The reduction in profit year on year is primarily due to the fact that the 2016 result benefited from a one-off profit arising on the sale of an investment asset. After taking this into consideration, the profit emergence is in line with the run-off book profile.

Note 4: The Scildon division has posted a strong result for the nine months since acquisition. Favourable economic factors have driven strong investment related returns. This arises from the fact that the Scildon division measures the majority of its insurance contract liabilities using historical rates of interest, as is customary in the Netherlands. This can lead to increased volatility in IFRS profits by virtue of the assets that back the liabilities being reported and measured on a fair value basis. In addition to the strong trading result, the Scildon purchase also generated a profit on acquisition of £20.3m in the year.

Note 5: The Chesnara result represents holding company expenses. The 2017 result reflects the adverse impact of creating a £2m provision in respect of the expected costs of delivering the implementation of IFRS 17 at group level. It also reflects a foreign exchange loss of £2.6m in respect of the Euro denominated loan taken out to part-fund the Scildon acquisition.

Note 6: Consolidation adjustments relate to items such as the amortisation of intangible assets. These are lower than previously reported, due to an increase in the write-back of deferred acquisition costs arising from the Scildon acquisition and a one-off impairment of acquisition costs within Movestic.

Note 7: As a result of sterling weakening against both the euro and Swedish krona in the period, the IFRS result includes a large foreign exchange gain, albeit smaller sizeable than the prior period.

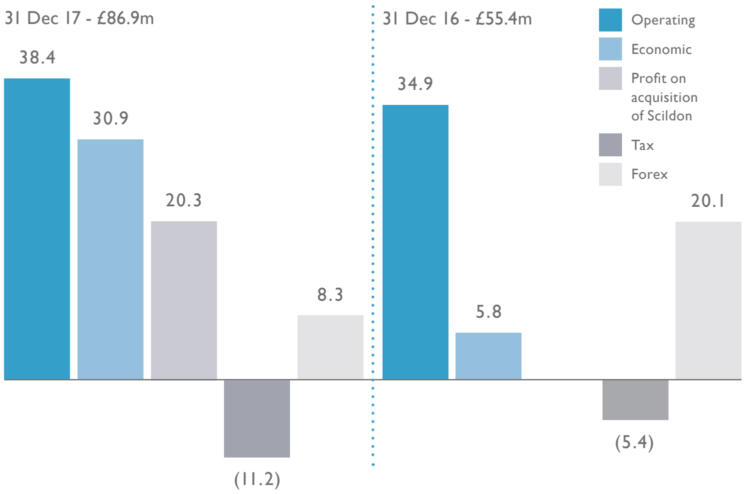
Note 8: Other comprehensive income includes movements relating to the revaluation of a defined benefit pension scheme and an investment property, both of which are held within the Scildon division.

	2017 £m	2016 £m	Note
Operating profit	38.4	34.9	9
Economic profit	30.9	5.8	10
Profit before tax and profit on acquisition	**69.3**	**40.7**	
Profit on acquisition of LGN	20.3	–	4
Profit before tax	**89.6**	**40.7**	
Tax	(11.2)	(5.4)	
Profit after tax	**78.4**	**35.3**	
Foreign exchange translation differences	8.3	20.1	7
Other comprehensive income	0.2	–	7
Total comprehensive income	**86.9**	**55.4**	

Note 9: The operating result demonstrates the strength and stability of the underlying business, driving the generation of profit. Product based income and favourable movements in operating experience in the UK, were offset slightly by the strengthening of expense reserves to support future developments. Strong premium growth and favourable claims experience supported the Movestic operating result, whilst Waard and Scildon produced operating results broadly in line with expectations.

Note 10: Economic profit represents the components of the earnings that are directly driven by movements in economic variables, e.g. the impact of yield movements on the cost of guarantees reserves. During 2017, the economic profit is mainly driven by the impact of positive equity markets.

Analysis of IFRS total comprehensive income (£m)



CASH GENERATION

GROUP CASH GENERATION

£28.6M 2016: £85.4M*

DIVISIONAL CASH GENERATION

£86.7M 2016: £34.3M

* The LGN acquisition had an adverse total end to end impact of £6.4m. A £48.9m one-off impact in respect of the equity raise was included in the 2016 result, with a subsequent negative impact of £55.3m on completion in 2017.

The three territories have generated £86.7m cash in the period, with all four businesses making significant contributions to the cash generation. Cash in the business is generated from increases in the group's surplus funds. Surplus funds represent the excess of assets held over management's internal capital needs, as in the capital management policies across the group. These are based on regulatory capital requirements, with the inclusion of additional 'management buffers'.

GROUP

- Before taking into account the 'day 1' impact of the acquisition of LGN, cash of £83.9m has been generated across the group, partly due to favourable economic conditions and the positive impact of some non-recurring management actions.
- Other group activities reflect the residual group expenses and the impact of consolidation routines, specifically movements in capital requirements determined at a group level. From a capital requirement perspective, this is driven by movements in required capital at a Chesnara holding company level coupled with consolidation adjustments. At a Chesnara holding company level, capital is principally required to be held for the currency risk associated with the Movestic, Scildon and Waard Group surplus assets.
- In line with expectations, the end to end impact of the acquisition of Legal & General Nederland is to reduce surplus cash by £6.4m. The £6.4m cash impact consists of an increase in own funds of £116.2m (£62.1m of equity raised net of deal costs; £191.6m of own funds acquired; less purchase price of £137.6m) offset by an increase in capital requirement of £122.6m (£88.4m of capital required in Scildon itself, including management group buffer, plus additional capital at group level of £34.3m). The £88.4m of capital required for Scildon includes the reduction due to the equity de-risk post acquisition, which amounted to £12.7m. Of the total impact, cash reduced by £55.3m in 2017, consisting of the Own Funds acquired less the capital required and the purchase price. The 2016 positive impact of £48.9m represents the element of the equity raised before the 2016 year end.

£m	2017 Movement in own funds	2017 Movement in management's capital requirement	2017 Forex impact	2017 Cash generated	2016 Cash generated
UK	32.4	2.1	–	**34.5**	**21.3**
Sweden	37.3	(15.3)	2.8	**24.9**	**(2.7)**
Netherlands – Waard Group	5.4	5.1	0.6	**11.1**	**15.7**
Scildon	10.5	4.3	1.4	**16.2**	–
Divisional cash	**85.6**	**(3.8)**	**4.9**	**86.7**	**34.3**
Other group activities	(12.7)	10.0	–	**(2.7)**	**2.2**
Group cash pre-Scildon acquisition	**72.9**	**6.2**	**4.9**	**83.9**	**36.5**
Impact of Scildon acquisition	54.1	(109.4)	–	**(55.3)**	**48.9**
Total group cash generation	**127.0**	**(103.2)**	**4.9**	**28.6**	**85.4**

UK

- The UK continues to generate significant levels of cash, ahead of plan, supporting the dividend payment.
- Own funds growth is the main driver of cash generation in the UK, which has benefitted from a reduction in the cost of guarantees and increased investment return.
- Cash generation includes the benefit of a £9.0m release of restricted surplus from the with-profit funds.
- There has also been a reduction in required capital due to changes in investment portfolio and reduced counterparty default risk.

SWEDEN

- Sweden had a positive cash generation of £24.9m due to strong Own Funds growth.
- Own Funds have benefitted from growth in assets under management, particularly in equity markets.
- Conversely, growth in assets has also had an adverse impact on the level of capital the business is required to hold, driving the increase in management capital requirement.
- Cash generation includes a one-off benefit of enhancing our modelling for commission clawbacks amounting to £7.0m.
- 2016 included a one-off capital increase from a modelling change for mass lapse risk.

NETHERLANDS – WAARD & SCILDON

- The **Waard Group** has continued the solid cash generation witnessed in the prior year with positive underlying movements in both Own Funds and capital requirements.
- Movement in Own Funds was driven by mortality experience and assumption changes.
- A fall in counterparty default risk underpins the reduction in the capital requirement.
- 2016 cash generation benefitted from an exchange rate gain of £8.5m.

- **Scildon** has reported positive cash generation of £16.2m since acquisition.
- Positive economic experience, including euro exchange gains against sterling, support the increase in own funds.
- The movement in capital requirement has benefitted from the continuing capital management programme that has been initiated post acquisition.

ECV EARNINGS

ECV EARNINGS

£139.5M 2016: £72.5M

Driven by generally beneficial investment markets throughout the year, with sterling depreciation and volatile yet growing equity markets, the group has reported significant underlying EcV earnings, reflecting the resilience and diversity of the business. In addition, there has been a one-off gain and post acquisition gains from Scildon.

Analysis of the EcV result in the period by earnings source:

	31 Dec 2017 £m	31 Dec 2016 £m	Note
Expected movement in period	12.0	6.0	
New business	12.4	11.9	
Operating variances	1.2	22.7	
Operating assumption changes	(3.6)	0.6	
Other operating variances	0.5	(7.3)	
Total underlying operating earnings	**22.5**	**33.9**	
Exceptional operating variances	(19.2)	–	2
Total operating earnings	**3.3**	**33.9**	
Economic experience variances	74.6	77.9	1
Economic assumption changes	2.2	(38.3)	
Total economic earnings	**76.8**	**39.6**	
Other non-operating variances	1.2	0.8	
Risk margin movement	4.0	(3.8)	
Gain on acquisition	65.4	–	3
Tax	(11.1)	2.0	
Total EcV earnings	**139.5**	**72.5**	

Analysis of the EcV result in the year by business segment:

	31 Dec 2017 £m	31 Dec 2016 £m	Note
UK	54.5	42.2	4
Sweden	24.0	30.8	5
Netherlands	21.8	5.9	6
Gain on acquisition	65.4	–	
Group and group adjustments	(15.1)	(8.4)	7
EcV earnings before tax	**150.6**	**70.5**	
Tax	(11.1)	2.0	8
EcV earnings after tax	**139.5**	**72.5**	

Note 1 – Economic conditions: As with our previously reported EEV metric, the EcV result is sensitive to investment market conditions. Key investment market conditions in the period are as follows:

- The FTSE All share index has increased by 9.0%;
- The Swedish OMX all share index has increased by 5.7%; and
- 10 year UK gilt yields have fallen from 1.28% to 1.26%.

Note 2 – Exceptional operating items: The Movestic result includes an £11.4m impact relating to changes in future charge assumptions if, as expected, commercial pressures were to drive fee changes in the future. Also included was a £7.8m provision to cover the future Scildon development programme.

Note 3 – Gain on acquisition of LGN: The acquisition of LGN resulted in a 'day 1' gain of £65.4m, representing the difference between the purchase price of £137.6m and the EcV of LGN at the point of acquisition of £203.0m.

Note 4 – UK: The UK reported significant pre tax earnings of £54.5m for the year. Solid operating earnings were supported by lower attrition rates and lower payments in respect of with-profit contracts with guarantees. This offset the adverse impact of the strengthening of assumptions in relation to the expense base during the year. Economic profits of £41.1m underpin the result, supported by market conditions. Key items driving the economic result include the investment return on shareholder and non-linked assets and returns driven by the impact of the higher unit prices versus static guarantees on claims and AMCs. The interaction of changing yields and inflation also contributed to this. The result also benefited from a £9.0m release of previously trapped surplus from the with-profit funds.

Note 5 – Sweden: The Swedish division has reported another solid EcV return in the year. Underlying operating earnings of £15.3m were underpinned by strong new business performance, owing to transfer volumes and increased average policy premiums. This was partially offset by a non-recurring adverse movement in future charge assumptions (see note 2). An economic profit of £20.0m was reported, driven by equity market performance and strong returns on the unit linked investment portfolio, closing on a considerable total annual return of 8.7% for 2017.

Note 6 – Netherlands: The Dutch division has reported earnings of £21.8m in the period. Underlying operating earnings of £9.0m are offset by an exceptional non-recurring item in respect of Scildon expense assumptions (see note 2). Strong economic earnings underpin the result.

Note 7 – Group: In line with expectations, a loss has been reported in the group component. This is includes the impact of costs incurred in relation to the LGN acquisition, underlying group level expenses and consolidation activities.

Note 8 – Tax: The business is reporting a tax expense of £11.1m in the year. This is driven by a combination of current tax on the profit in the period and movements in deferred tax relating to group level activities.

ECV

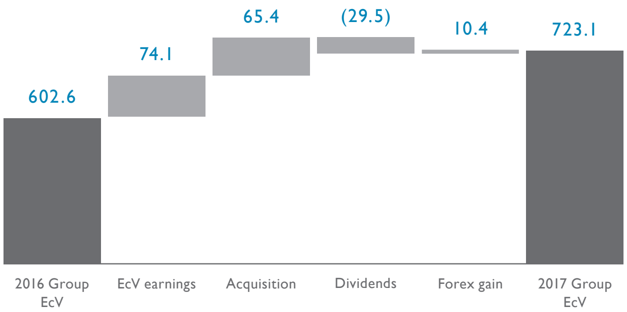
ECV

£723.1M 2016: £602.6M

The Economic Value (EcV) of Chesnara represents the present value of future profits of the existing insurance business, plus the adjusted net asset value of the non-insurance business within the group. EcV is an important reference point by which to assess Chesnara's intrinsic value.

Value movement: 1 Jan 2017 to 31 Dec 2017

£m



EcV earnings: Positive EcV earnings have been reported in the year, a result of solid underlying operating profits and significant economic profits, driven by the net impact of equity market growth and return on assets. Further detail can be found on page 38.

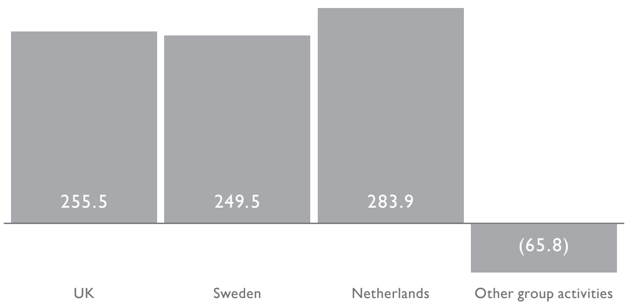
Acquisition: In April 2017, the group successfully completed the purchase of LGN, delivering a 'day 1' acquisition gain of £65.4m. This is reflected in the group closing EcV.

Dividends: Under EcV, dividends are recognised in the period in which they are paid. Dividends of £29.5m were paid during the 2017, being the final dividend from 2016 and interim 2017 dividend.

FX gain: The EcV of the group benefited from foreign exchange gains that were reported in the period as a result of sterling deprecation against both the euro and Swedish krona.

EcV by segment at 31 Dec 2017

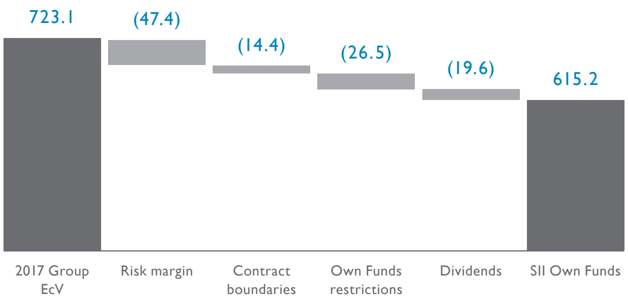
£m



The above graph shows that the EcV of the group is diversified across its different markets, demonstrating that we are well-balanced and not over-exposed to one particular geographic market.

EcV to Solvency II

£m



Our reported EcV is based on a Solvency II assessment of the value of the business, but adjusted for certain items where it is deemed that Solvency II does not reflect the commercial value of the business. The above waterfall graph shows the key difference between EcV and SII, with explanations for each item below.

Risk margin: Solvency II rules require a significant 'risk margin' which is held on the Solvency II balance sheet as a liability, and this is considered to be materially above a realistic cost. We therefore reduce this margin for risk for EcV valuation purposes from being based on a 6% cost of capital to a 2.75% cost of capital (2016: 3.00%).

Contract boundaries: Solvency II rules do not allow for the recognition of future cash flows on certain in-force contracts, despite the high probability of receipt. We therefore make an adjustment to reflect the realistic value of the cash flows under EcV.

Ring-fenced fund restrictions: Solvency II rules require a restriction to be placed on the value of certain ring-fenced funds. These restrictions are reversed for EcV valuation purposes as they are deemed to be temporary in nature.

Dividends: The proposed final dividend of £19.6m is recognised for SII regulatory reporting purposes. It is not recognised within EcV until it is actually paid.

FINANCIAL MANAGEMENT

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

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 aim to:

- 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 TO OUR OBJECTIVES

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

1. Monitor and control risk & solvency
2. Longer-term projections
3. Responsible investment management
4. Management actions

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 146%	2015-2017 TSR 33.6% 2017 dividend yield 5.3% Based on average 2017 share price and full year 2017 dividend of 20.07p.	Gearing ratio of 19.8% This does not include the financial reinsurance within the Swedish business.	Policyholders' reasonable expectations maintained Asset liability matching framework operated effectively in the year Sufficient liquidity in the Chesnara holding company	Group remains a going concern (see page 41)

OUTCOMES FROM IMPLEMENTING OUR FINANCIAL MANAGEMENT OBJECTIVES

1. Capital structure

The group is funded by a combination of share capital, retained earnings and debt finance, with the debt gearing (excluding financial reinsurance in Sweden) being 19.8% at 31 December 2017 (13.4% at 31 December 2016).

The level of debt that the board is prepared to take on is driven by the group's 'Debt and leverage policy' which incorporates the board's risk appetite in this area.

Over time, the level of gearing within the group will change, and is a function of:

- funding requirements for future acquisitions (i.e. debt, equity and internal financial resources); and
- repayment of existing debt that was used to fund previous acquisitions.

As referred to above, acquisitions are funded through a combination of debt, equity and internal cash resources. The ratios of these three funding methods vary on a deal-by-deal basis and are driven by a number of factors including, but not limited to:

- size of the acquisition;
- current cash resources of the group;
- current gearing ratio and the board's risk tolerance limits for additional debt;
- expected cash generation profile and funding requirements of the existing subsidiaries and potential acquisition;
- future financial commitments; and
- regulatory rules.

In addition to the above, Movestic uses a financial reinsurance arrangement to fund its new business operation.

2. Maintain the group as a going concern

The directors have considered the ability of the group to continue on a going concern basis. As such the board has performed an assessment as to whether the group can meet its liabilities as they fall due for a period of at least twelve months from which the Report & Accounts have been signed.

In performing this work, the board has considered the current cash position of the group and company, coupled with the group's and company's expected cash generation as highlighted in its recent business plan, which covers a three-year period. The business plan considers the financial projections of the group and its subsidiaries on both a base case and a range of stressed scenarios, covering projected IFRS, EcV and solvency. These projections also focus on the cash generation of the life insurance divisions and how these flow up into the Chesnara parent company balance sheet, with these cash flows being used to fund debt repayments, shareholder dividends and the head office function of the parent company.

The information set out on page 32 indicates a strong solvency position as at 31 December 2017 as measured at both the divisional and group levels. As well as being well-capitalised, the group also has a healthy level of cash reserves to be able to meet its debt obligations as they fall due, and does not rely on the renewal or extension of bank facilities to continue trading. The group's subsidiaries do, however, rely on cash flows from the maturity or sale of fixed interest securities which match certain obligations to policyholders, which brings with it the risk of bond default. 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 reinsurers. We monitor their financial position and are satisfied that any associated credit default risk is low.

In light of the above information, the board has concluded that the group and company has a reasonable expectation that the group and company have adequate resources to continue in operational existence for the foreseeable future, and, as stated in the Directors Report on page 86, the Financial Statements have continued to be prepared on a going concern basis.

3. Assessment of prospects

An understanding of the group's strategy and business model is central to assessing its prospects, and details can be found on pages 18 and 19.

Our business model provides resilience that is relevant to any consideration of our prospects and viability. In CA in the UK and in both Waard and Scildon in the Netherlands, we benefit from a largely predictable and well understood source of cash generation. In addition, Movestic and Scildon, provide a source of new business growth.

Our strategy of maximising value from our existing business, acquiring life and pensions businesses and enhancing value through profitable new business, is designed to support long-term and sustainable cash generation.

We assess our prospects on a regular basis through our financial planning process. Our three year medium term group business plan forecasts the group's profitability, cash generation, economic value and solvency position and is reviewed by the board during the year. The business plan is built from the bottom up forecasts of each of our business segments, supplemented by items managed at group level and assumptions to be used in the basis of preparation. The performance of the group and our business segments against these forecasts is monitored quarterly through a series of quarterly business reviews performed by the group executive and internal management information which is reviewed by the board.

The group also makes investments, such as life and pensions business acquisitions and longer term business development programmes that have a business case beyond our core three year planning horizon. Significant expenditure of this nature is subject to a detailed business case being prepared and approved by the board.

4. Longer-term viability statement

In accordance with provision C.2.2 of the 2014 revision of the UK Corporate Governance Code, the directors have assessed the prospects of the company over a longer period than the twelve months required by the going concern provision. The board conducted this review for a period of three years because the group's business plan covers a three year period and includes an assessment of group cash generation and group solvency margins over that time period.

The group business plan considers the group's cash flows, the group's ability to remain above target solvency levels and other key financial measures over the period, assuming continuation of the group's established dividend payment strategy. These metrics are subject to scenario analysis representing the principal risks to which the group is most sensitive, both individually and in unison. Where appropriate this analysis is carried out to evaluate the potential impact of adverse economic and other experience effects, including, but not limited to:

i. Equity market declines
ii. Reduction in yield curves
iii. Credit spread rise
iv. Swap rate fall
v. Adverse mortality and lapse experience
vi. Adverse expense experiences
vii. Reduced new business volumes
viii. Adverse exchange rate experience

Based on the results of this analysis, the directors have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the three year period of their assessment.

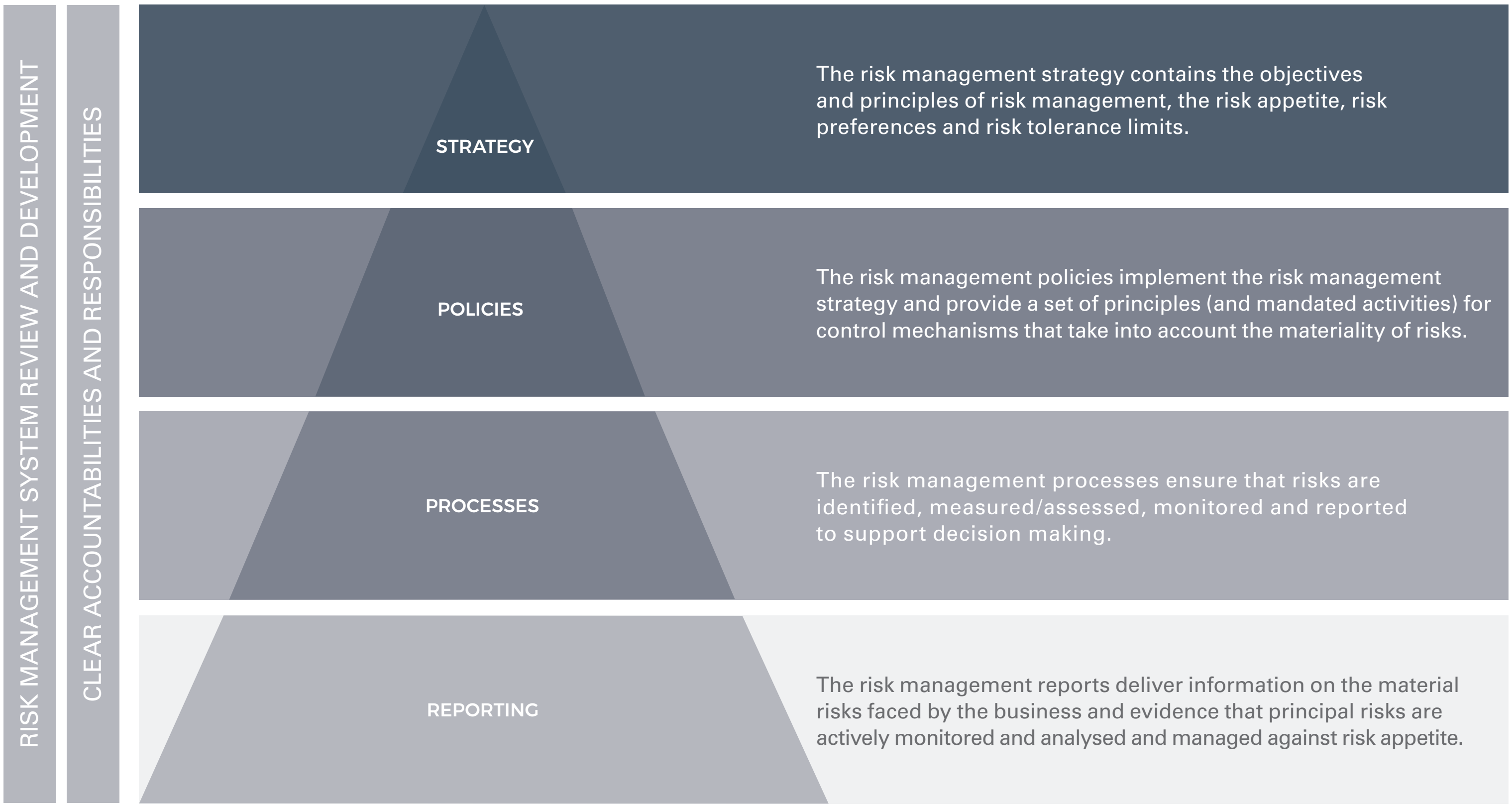
RISK MANAGEMENT

Managing risk is a key part of our business model. We achieve this by understanding the current and emerging risks to the business, mitigating them where appropriate and ensuring they are appropriately monitored and managed at all times.

HOW WE MANAGE RISK

RISK MANAGEMENT SYSTEM

The risk management system supports the identification, assessment, and reporting of risks along with coordinated and economical application of resources to monitor and control the probability and/or impact of adverse outcomes within the board's risk appetite or to maximise realisation of opportunities



RISK PROCESS

Risk management processes are applied at a group, divisional and business unit level and are documented within a set of board approved risk policies, for each category of risk.

Chesnara adopts the 'three lines of defence' model across the group taking into account size, nature and complexity, with a single set of risk and governance principles applied consistently across the business.

In all divisions, we maintain processes for identifying, evaluating and managing all material risks faced by the group, which are regularly reviewed by the divisional and group Audit & Risk Committees. Our risk assessment processes have regard to the significance of risks, the likelihood of their occurrence and take account of the controls in place to manage them. The processes are designed to manage the risk profile within the board's approved risk appetite.

Group and divisional 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. The results, conclusions and any recommended actions are included within divisional and group ORSA Reports to the relevant boards. There is a strong correlation between these adverse events and the risks identified in 'Principal risks and uncertainties' (see p43 to p45). The outcome of this testing provides context against which the group can assess whether any changes to its risk appetite or to its management processes are required.

CHESNARA RISK PREFERENCES

The Chesnara board has approved a set of risk preferences which articulate, in simple terms, the desire to increase, maintain, or reduce the level of risk taking for each main category of risk. The risk position of the business is monitored against these preferences using risk tolerance limits, where appropriate, and they are taken into account by the management teams across the group when taking strategic or operational decisions that affect the risk profile.

PRINCIPAL RISKS AND UNCERTAINTIES

The table overleaf outlines the principal risks and uncertainties of the group and the controls in place to mitigate or manage their impact. It has been drawn together following regular assessment performed by the Audit and Risk Committee of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity. Given that the Scildon business risk profile is similar to that of the Chesnara businesses prior to acquisition of Scildon, the description of the group's risk profile at this level is unchanged as a result of the integration of Scildon.

The impacts have not been quantified however by virtue of the risks being defined as principal, the impacts are potentially large. Although this is a matter of judgement the risks and impacts are ordered based on probabilities and impacts, putting the largest first.

RISK MANAGEMENT • PRINCIPAL RISKS AND UNCERTAINTIES

RISK	IMPACT	CONTROL
Exposure to financial losses or value reduction arising from adverse movements in investment markets, counterparty defaults, or through inadequate asset liability matching	Market risk results from fluctuations in asset values, foreign exchange rates and interest rates and has the potential to affect the group's ability to fund its commitments to customers and other creditors, as well as pay a return to shareholders. Chesnara and each of its subsidiaries have obligations to make future payments, which are not always known with certainty in terms of timing or amounts, prior to the payment date. This includes primarily the payment of policyholder claims, reinsurance premiums, debt repayments and dividends. The uncertainty of timing and amounts to be paid gives rise to potential liquidity risk, should the funds not be available to make payment. Other liquidity issues could arise from counterparty failures/credit defaults, a large spike in the level of claims or other significant unexpected expenses.	Chesnara performs regular monitoring of movements in the market and maintains matching programmes to ensure that exposure to any mismatching is at an acceptable level, forecasting cash requirements and adjusting investment management strategies to meet those requirements. Chesnara seeks to limit the impacts of exposure to Market risks by: – Maintaining a well-diversified asset portfolio; – Holding a significant amount of surplus in highly liquid 'Tier 1' assets such as cash and gilts; – Utilising a range of investment funds and managers to avoid significant concentrations of risk; – Having an established investment governance framework to provide review and oversight of external fund managers; – Carrying out regular liquidity forecasts and asset and liability modelling; and – Monitoring exchange rate movements. The group would consider the cost/benefit of hedging the currency risk on cash flows when appropriate. In respect of a significant exposure to one major reinsurer, ReAssure (formerly known as Guardian), the group has a floating charge over the reinsurer's related investment assets, which ranks the group equally with ReAssure's policyholders.
Adverse changes in industry practice/ regulation, or inconsistent application of regulation across territories	Chesnara currently operates in four regulatory domains and is therefore exposed to inconsistent application of regulatory standards across divisions, such as the imposition of higher capital buffers over and above regulatory minimum requirements. Potential consequences of this risk for Chesnara is the constraining of efficient and fluid use of capital within the group, or creating a non-level playing field with respect to future new business/acquisitions. The jurisdictions which Chesnara operates in are currently subject to significant change arising from political, regulatory and legal change. These may either be localised or may apply more widely, following from EU-based regulation and law, or the potential unwinding of this following the UK's decision to leave the EU. The group is therefore exposed to the risk of: – incurring one-off costs of addressing regulatory change as well as any permanent increases in the cost base in order to meet enhanced standards; – erosion in value arising from pressure or enforcement to reduce future policy charges; – erosion in value arising from pressure or enforcement to financially compensate for past practice; and – regulatory fines or censure in the event that it is considered to have breached standards, or fails to deliver changes to the required regulatory standards on a timely basis.	Through the Risk Management Framework, regulatory risk is monitored and scenario tests are performed to understand the potential impacts of adverse political, regulatory or legal changes, along with consideration of actions that may be taken to minimise the impact, should they arise. Chesnara seeks to limit any potential impacts of regulatory change on the business by: – Having processes in place for monitoring changes, to enable timely actions to be taken, as appropriate; – Maintaining strong open relationships with all regulators; – Being a member of the ABI and utilising other means of joint industry representation; – Performing internal reviews of compliance with regulations; and – Utilising external specialist advice and assurance, when appropriate. In extremis, Chesnara could consider the re-domiciling of subsidiaries or legal restructure of the business, should this result in a more commercially acceptable business model in a changed operating environment.
Failure to source acquisitions that meet Chesnara's criteria or the execution of acquisitions with subsequent unexpected financial loses or value reduction	Chesnara's inorganic growth strategy is dependent on the availability of attractive future acquisition opportunities. Hence, the business is exposed to the risk of a reduction in the availability of suitable acquisition opportunities within Chesnara's current target markets, for example arising as a result of a change in competition in the consolidation market or from regulatory change influencing the extent of life company strategic restructuring. Through the execution of acquisitions, Chesnara is also exposed to the risk of erosion of value or financial losses arising from risks inherent within businesses or funds acquired which are not adequately priced for or mitigated as part of the transaction.	Chesnara's financial strength, strong relationships and reputation as a 'safe hands acquirer' via regular contact with regulators, banks and target companies enables the company to adopt a patient and risk-based approach to assessing acquisition opportunities. Operating in multiple territories provides some diversification against the risk of changing market circumstances in one of the territories. Chesnara seeks to limit any potential unexpected impacts of acquisitions by: – Applying a structured board approved risk-based acquisition process including CRO involvement in the due diligence process and deal refinement processes; – Having a management team with significant and proven experience in mergers and acquisitions; and – Adopting a cautious risk appetite and pricing approach.

RISK	IMPACT	CONTROL
Adverse demographic experience compared with assumptions	In the event that demographic experience (rates of mortality, morbidity, persistency etc.) varies from the assumptions underlying product pricing and subsequent reserving, more or less profit will accrue to the group. If mortality or morbidity experience is higher than that assumed in pricing contracts (i.e. more death and sickness claims are made than expected), this will typically result in less profit accruing to the group. If persistency is significantly lower than that assumed in product pricing and subsequent reserving, this will typically lead to reduced group profitability in the medium to long-term, as a result of a reduction in future income arising from charges on those products. The effects of this could be more severe in the case of a one-off event resulting in multiple withdrawals over a short period of time (a 'mass lapse' event).	Chesnara ensures close monitoring of persistency levels across all groups of business to support best estimate assumptions and identify trends. There is also partial risk diversification in that the group has a portfolio of annuity contracts where the benefits cease on death. Chesnara seeks to limit the impacts of adverse demographic experience by: – Aiming to deliver good customer service and fair customer outcomes; – Having effective underwriting techniques and reinsurance programmes, including the application of 'mass lapse reinsurance', where appropriate; – Carrying out regular investigations, and industry analysis, to support best estimate assumptions and identify trends; – Active investment management to ensure competitive policyholder investment funds; and – Maintaining good relationships with brokers which is independently measured via yearly external surveys that considers brokers attitude towards different insurers.
Significant operational failure / business continuity event	The group and its subsidiaries are exposed to operational risks which arise through daily activities and running of the business. Operational risks may, for example, arise due to technical or human errors, failed internal processes, insufficient personnel resources or fraud caused by internal or external persons. As a result, the group may suffer financial losses, poor customer outcomes, reputational damage, regulatory intervention or business plan failure. Part of the group's operating model is to outsource support activities to specialist service providers. Consequently, a significant element of the operational risk arises within its outsourced providers.	The group perceives operational risk as an inherent part of the day-to-day running of the business and understands that it can't be completely eliminated. However, the group's objective is to always control or mitigate operational risks, and to minimise the exposure when it's possible to do so in a convenient and cost effective way. Chesnara seeks to reduce the impact and likelihood of operational risk by: – Monitoring key performance indicators and comprehensive management information flows; – Effective governance of outsourced service providers including a regular financial assessment. 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; – Regular testing of business continuity plans; – Promoting the sharing of knowledge and expertise; and – Complementing internal expertise with established relationships with external specialist partners.
Expense overruns and unsustainable unit cost growth	The group is exposed to expenses being higher than expected as a result of one-off increases in the underlying cost of performing key functions, or through higher inflation of variable expenses. For the closed funds, the group is exposed to the impact on profitability of fixed and semi-fixed expenses, in conjunction with a diminishing policy base. For the companies open to new businesses, the group is exposed to the impact of expense levels varying adversely from those assumed in product pricing.	For all subsidiaries, the group maintains a regime of budgetary control: – Movestic and Scildon assume growth through new business such that the general unit cost trend is positive; – The Waard Group pursues a low cost-base strategy using a designated service company. The cost base is supported by service income from third party customers; – Countrywide Assured pursues a strategy of outsourcing functions with charging structures such that the policy administration cost is more aligned to the book's run off profile; and – The group has an ongoing expense management programme in place to monitor and manage the overall expense base.
IT/data security failures or cyber crime	Cyber risk is a growing risk affecting all companies, particularly those who are custodians of customer data. The most pertinent risk exposure relates to information security (i.e. protecting business sensitive and personal data) and can arise from failure of internal processes and standards, but increasingly companies are becoming exposed to potential malicious cyber attacks, organisation specific malware designed to exploit vulnerabilities, phishing attacks etc. The extent of Chesnara's exposure to such threats also includes third party service providers. The potential impact of this risk includes financial losses, inability to perform critical functions, disruption to policyholder services, loss of sensitive data and corresponding reputational damage or fines.	Chesnara seeks to limit the exposure and potential impacts from IT/ data security failures or cyber crime by: – Embedding the Information Security Policy in all key operations and development processes; – Seeking ongoing specialist external advice, modifications to IT infrastructure and updates as appropriate; – Delivering regular staff training and attestation to the information security policy; – Conducting penetration and vulnerability testing, including third party service providers; and – Having established Chesnara and supplier business continuity plans which are regularly monitored and tested. Chesnara has undertaken further work during 2017 to deliver an enhanced information security environment commensurate with the increase in risk exposure and in preparation for the new General Data Protection Regulation that applies from May 2018.

CORPORATE AND SOCIAL RESPONSIBILITY

Making a positive contribution to our policyholders and shareholders, whilst taking seriously social and environmental issues.

OUR MAIN OBJECTIVE IS TO ENSURE WE CONTINUE TO MANAGE THE BUSINESS RESPONSIBLY AND FOR THE LONG-TERM BENEFIT OF ALL STAKEHOLDERS, INCLUDING OUR CUSTOMERS, SHAREHOLDERS, EMPLOYEES, REGULATORS, OUTSOURCERS AND LOCAL COMMUNITIES.

Equal opportunities
Our people are our greatest assets. We recognise that to be able to meet the expectations that we have set ourselves, we need to ensure, in a competitive market, we continue to attract, promote and retain the best candidates. Our approach is to be open, entrepreneurial and inclusive in how we operate. 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:

	2017		2016	
	Male	Female	Male	Female
Directors of Chesnara plc	5	2	5	2
Senior management of the group	7	2	3	–
Heads of business units and group functions	20	6	14	5
Employees of the group	169	161	89	83
Total	**201**	**171**	**111**	**90**

The Hampton-Alexander report recommends a board diversity target of 30% for FTSE 350 companies. Gender diversity forms an important part of the board appointment process.

Chesnara are committed to diversity and, over the last two years, five out the six senior executive and non-executive appointments have been filled by females. Our group Audit and Risk Committee and group Remuneration Committee both have female chairmen and Movestic is now headed up by a female CEO.

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. Chesnara has only three members of staff who meet the Companies Act definition of senior management. We therefore provide 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 given an analysis of diversity which shows 'Heads of business units and group functions' separately from the remainder of employees within the group.

The principal reason for the movement in employee numbers during 2017 was the impact of the acquisition of LGN.

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. The group will make reasonable adjustments to give the disabled person as much access to any services and ability to be employed, trained, or promoted as a non-disabled person.

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. In addition, as multinational group, we actively use video-conferencing throughout our interactions.

'OUR PEOPLE ARE OUR GREATEST ASSETS. WE RECOGNISE THAT TO BE ABLE TO MEET THE EXPECTATIONS THAT WE HAVE SET OURSELVES, WE NEED TO ENSURE, IN A COMPETITIVE MARKET, WE CONTINUE TO ATTRACT, PROMOTE AND RETAIN THE BEST CANDIDATES'.

Whistleblowing
Across the group, we have in place whistleblowing policies, which comply with local regulatory requirements. In the UK, the Audit & Risk Committee Chairman is appointed as Whistleblowing Champion, whose responsibilities meet the requirements of the Senior Insurance Managers Regime. Similar arrangements are in operation within our overseas divisions.

Modern Slavery Act 2015
The Modern Slavery Act 2015 (Slavery Act) requires a commercial organisation over a certain size to publish a slavery and human trafficking statement for each financial year. This statement can be found on the Chesnara plc website. The group welcomes the act and is committed to the eradication of human trafficking and slavery. Slavery and human trafficking are abuses of a person's freedom and rights. We are totally opposed to such abuses in our direct operations, our indirect operations and our supply chain as a whole.

The operating model of Chesnara's UK business is directed towards maintaining shareholder value by outsourcing all support activities to professional specialists. The activities typically include policy administration, systems management, accounting, actuarial and investment management. This has been provided by long-term contracts held with only reputable suppliers, and as these are significant, the responsibility of oversight has remained with the central governance.

We consider that the greatest risk of slavery and human trafficking would be in our supply chain where operational and managerial oversight is out of our direct control and we expect our partners to operate in line with our corporate values.

Anti-Bribery and Corruption Policy
Chesnara has in place an Anti-Bribery and Corruption Policy which is reviewed annually or more frequently by exception. Its scope includes all directors, employees and third-parties operating on its behalf and the company has a zero tolerance to all such matters. Controls operated in the period include the maintenance and review of a Gifts & Hospitality Register, the disallowance of any political contributions or inducements and careful consideration of any charitable donations. The internal financial control environment acts as a further monitoring and prevention system. There were no instances of bribery or corruption in the period.

'OUR APPROACH IS TO BE OPEN, ENTREPRENEURIAL AND INCLUSIVE IN HOW WE OPERATE'.

Greenhouse gas reporting

Disclosure of emissions
Global GHG emissions data for the year to 31 December 2017:

	Tonnes of CO_2e	
	2017	**2016**
Emissions from:		
Combustion of fuel and operation of facilities (scope 1)	–	–
Electricity, heat, steam and cooling purchased for own use (scope 2)	193.8	94.7
Travel (scope 3)	229.3	132.4
Company's chosen intensity measurement = tonnes of CO_2e per square metre of office space occupied	0.063	0.074
Emissions reported above normalised to per tonne of product output		

The emission figures above reflect the inclusion of Scildon from the date of acquisition. This has resulted in an overall increase in our total emissions when compared with the prior year. The overall measure for tonnes of CO_2e per square metre of office space has reduced slightly from the prior year.

Methodology used to calculate emissions
We have followed the requirements of the GHG Protocol Corporate Accounting and Reporting Standard (revised edition) and the Defra 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 in the UK, 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 above.

There are 34 company-leased vehicles in total across the group 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.

Energy Saving Opportunity Scheme Regulations 2014
The company has also committed to fully engaging with the Energy Saving Opportunity Scheme Regulations 2014 (ESOS). As part of the ESOS, the company submitted and was externally assessed for the energy usage, in the UK, for the period 31 December 2014 to 31 December 2015. Energy usage examined was in relation to any energy consumed by the company, lighting, heating, fuel to name a few. ESOS operates on a four year compliance phase with the next reporting / compliance date being December 2019.

Approved by the board on 28 March 2018 and signed on its behalf by:

Peter Mason
Chairman

John Deane
Chief executive officer

SECTION C: CORPORATE GOVERNANCE

SECTION C • CORPORATE GOVERNANCE

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Värmdö, Sweden

BOARD PROFILE AND BOARD OF DIRECTORS

One key role for the Chesnara Board of Directors is to provide leadership and maintain the highest possible standards of corporate governance.

The skills, knowledge and experience of our board members ensure we continue to deliver against our strategic objectives. We continue to disclose a board competency profile, as summarised on the right. This summary is based on the core competencies that have been identified as being key to the board discharging its responsibilities and shows the collective score based on the current board make-up.

To provide further insight into the skills, knowledge and experience of each board member, the biographies below show the specific areas of specialism each member provides, with each letter correlating to the competency matrix on the right Where a board member has a competency in blue this indicates a primary specialism. A light grey colour indicates that this competency is a secondary specialism for that board member.

THE BOARD

PETER MASON
CHAIRMAN

Non-executive Chairman of the board, Peter is responsible for the leadership of the board, setting the agenda and ensuring the board's effectiveness in all aspects of its role.

Appointment to the board: Appointed to the board in March 2004 and as Chairman in January 2009.

Committee membership: Nomination & Governance (Chairman) and a member of the Remuneration Committee. Peter attends the Audit & Risk Committee by invitation.

Current directorships/business interests:
- Movestic Livförsäkring AB, Chairman
- Chesnara Holdings BV, Chairman
- Countrywide Assured plc, Chairman
- Countrywide Assured Life Holdings Limited, Chairman

Skills and experience: A B C D E F G H I

JANE DALE
NON-EXECUTIVE DIRECTOR AND CHAIRMAN OF THE AUDIT & RISK COMMITTEE

Appointment to the board: Appointed to the Chesnara plc board in May 2016 and as Chairman of the Audit & Risk Committee in December 2016.

Committee membership: Audit & Risk and Nomination & Governance.

Current directorships/business interests:
- Countrywide Assured plc, Chairman of the Audit & Risk Committee
- Covea Insurance plc, Chairman of the Audit Committee
- Covea Life Limited, Chairman of the Audit Committee
- British Gas Services Limited, NED

Skills and experience: A B D E F G H I J K

MIKE EVANS
SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR

Appointment to the board: Appointed to the Chesnara plc board in March 2013. Mike became senior independent director in May 2013.

Committee membership: Nomination and Governance, Audit & Risk and Remuneration.

Current directorships/business interests:
- ZPG plc, Chairman
- Just Eat plc, Chairman Elect
- Chesnara Holdings BV, NED
- Countrywide Assured plc, NED

Skills and experience: A B C D E F G H I K

JOHN DEANE
CHIEF EXECUTIVE

Appointment to the board: Appointed to the board in December 2014 and as chief executive in January 2015.

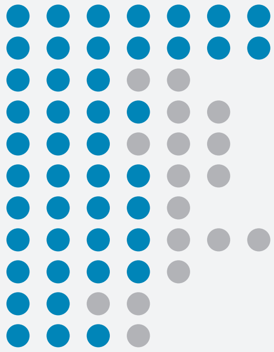
Career, skills and experience: John is a qualified actuary and has over 30 years' experience in the life assurance industry. John joined Century Life, a closed book acquisition company in 1993. As CEO, he oversaw the creation of the outsourcing company Adepta in 2000. He joined Old Mutual plc in 2003 becoming their corporate development director later that year. In 2007, he joined the board of Royal London with responsibility for its open businesses in the UK, Ireland and Isle of Man.

Skills and experience: A B C D E F G H I J K

BOARD KNOWLEDGE, SKILLS AND EXPERIENCE SUMMARY

KEY	KNOWLEDGE/SKILL/EXPERIENCE
A	Chesnara company knowledge
B	Industry knowledge – UK
C	Industry knowledge - Sweden/Netherlands
D	Governance – actuarial
E	Governance – financial
F	Audit and risk management
G	Investment management
H	M & A and business development
I	Commercial management
J	Operational change management
K	Operational management

SUMMARY



Annual assessment confirms that our board continues to hold significant experience in the insurance sector and also have a range of specialisms which ensure all aspects of our competency profile are well covered.

In the above diagram, a blue symbol represents the number of individuals with a primary specialism in that area, with a grey symbol reflecting a secondary area of expertise. Where board members are not deemed to have a level of specialism regarding a specific competency, they clearly contribute constructively to those matters through their general level of board and business experience.

VERONICA OAK
NON-EXECUTIVE DIRECTOR, CHAIRMAN OF THE REMUNERATION COMMITTEE

Appointment to the board: Appointed to the Chesnara plc board in January 2013.

Committee membership: Nomination & Governance, Audit & Risk and Remuneration.

Current directorships/business interests:
- Hanley Economic Building Society, Chairman of the Risk Committee
- Hanley Mortgage Services Limited, NED
- Hanley Financial Services Limited, NED
- Sanlam Investment Holdings Limited, NED
- Sanlam UK Limited, NED
- Investment & Life Assurance Group Limited, NED
- Countrywide Assured plc, NED

Skills and experience: A B H I J K

DAVID RIMMINGTON
GROUP FINANCE DIRECTOR

Appointment to the board: Appointed as group finance director with effect from May 2013.

Career, skills and experience: David trained as a chartered accountant with KPMG, has over 20 years' experience in financial management within the life assurance and banking sectors and has delivered 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.

Skills and experience: A B C D E F H J

DAVID BRAND
NON-EXECUTIVE DIRECTOR

Appointment to the board: Appointed to the Chesnara plc board and the board of Movestic Livförsäkring AB in January 2013.

Committee membership: Nomination & Governance and Audit & Risk.

Current directorships/business interests:
- Exeter Friendly Society, Chairman of the Audit Committee and Investment Committee
- Exeter Cash Plan Holdings Limited, NED
- Exeter Cash Plan Limited, NED
- Movestic Livförsäkring AB, Chairman of the Audit & Risk Committee
- Countrywide Assured plc, NED

Skills and experience: A B C D E F G H

GOVERNANCE OVERVIEW FROM THE CHAIRMAN

GOOD GOVERNANCE IS THE FOUNDATION FOR HOW WE SHOULD OPERATE.

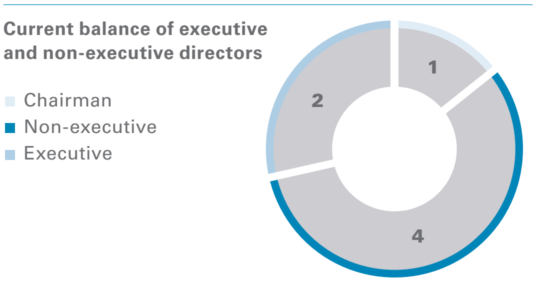
Dear Shareholder,

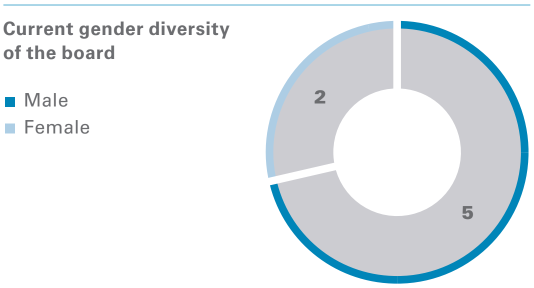
On behalf of the board, I am very pleased to present our Corporate Governance Report for the year ended 31 December 2017.

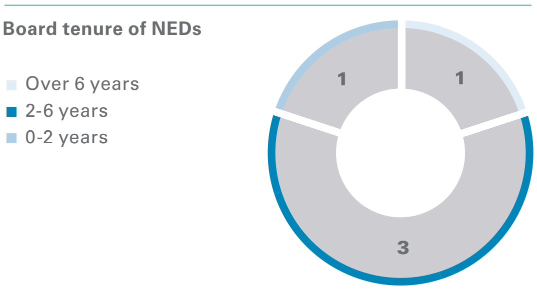
In 2016, the Company reported against the 2014 version of the UK Corporate Governance Code. The revised Code published by the Financial Reporting Council in April 2016 (the 'Code') took effect for companies with accounting periods beginning on or after 17 June 2016 and has applied to the company for the financial year ending 31 December 2017. I am delighted to be able to report that the board considers that the company has complied fully throughout the year with the provisions of the Code.

The board is accountable to our shareholders and wider stakeholders for generating and delivering sustainable value through good management of the group's business. The board plays a critical role in ensuring that the tone for the group's culture and values is set from the top. I firmly believe that a robust, and effective, governance framework is essential to support management in delivering the company's strategy. We understand that good governance is fundamental to the effective management of the business and its sustainability in both the short and the long-term.

This section of the Annual Report & Accounts sets out our governance policies and practices, and includes details of how the company has, during 2017, applied the Code.







The board is cognisant of the corporate governance reforms and proposed changes in legislation that are intended to encourage responsible corporate behaviour. The board is also mindful of the company's wider purpose, responsibilities and decision making processes to a broader stakeholder group. In delivering sustainable performance, the board is aware of the need to consider and engage with the interests of its employees, customers and suppliers. In 2017, the board continued to engage with its shareholders to promote effective governance through open and constructive two-way dialogue, and we place great value on this engagement.

Significant progress has been made by managers and employees during the year, not only in the delivery of the day-to-day business, but also the integration of the newly acquired Scildon business. We remain mindful of the strong relationship between ethics and governance and the role the board plays in demonstrating these. The group's Governance Map, which sets out the governance approach and framework, continues to be developed and embedded across all divisions of the business including Scildon.

In the year under review, the Audit & Risk Committee undertook an external audit tender process, which resulted in the recommendation by the committee of the re-appointment of Deloitte LLP. Detail of the full tender process is described on pages 82 to 83 in the Audit & Risk Committee Report. Appointment of Deloitte LLP remains subject to shareholder approval at the 2018 AGM.

This report demonstrates how the board and its committees have fulfilled their governance responsibilities.

Peter Mason
Chairman

28 March 2018

CORPORATE GOVERNANCE REPORT

IT IS ESSENTIAL TO HAVE A WELL DESIGNED AND EFFECTIVE GOVERNANCE FRAMEWORK TO ENSURE THAT STAKEHOLDERS' INVESTMENTS ARE SAFEGUARDED.

The following statement, together with the Directors' Remuneration Report on pages 62 to 79, the Nomination & Governance Committee Report on pages 58 to 59, and the Audit & Risk Committee Report on pages 80 to 85 describes how the principles set out in the UK Corporate Governance Code 2016 (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 2017.

Compliance with the Code

The company has complied throughout the year with all of the relevant provisions of the Code. The UK Corporate Governance Code is available at www.frc.org.uk

The board

At 31 December 2017, the board comprised of a non-executive Chairman, four other non-executive directors and two executive directors.

Biographical details of directors are given on pages 50 and 51 and a board profile, which assesses the core competencies required to meet the group's strategic objectives, is provided on page 51. The board, which plans to meet at least 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 were also directors of Countrywide Assured plc, a UK-based life and pensions subsidiary within the group;

ii) three directors of the company, being Messrs Mason, Deane and Evans, were also directors of Chesnara Holdings BV throughout the year; and

iii) four directors of the company, being Messrs Mason, Deane, Brand and Rimmington, were also directors of Movestic Livförsäkring AB throughout the year.

Under local legislation or regulation for all divisions of the group, the directors 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. The Prudential Regulatory Authority is the group supervisor and maintains oversight of all divisions of the group through the college of supervisors.

The responsibilities that the board has delegated to the respective executive management teams of the UK, Dutch 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.

The roles of the Chairman and group chief executive

The division of responsibilities between the Chairman of the board and the group chief executive 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 group chief executive has direct charge of the group on a day-to-day basis and is accountable to the board for the strategic, financial and operational performance of the group.

Senior independent director

The board has designated Mike Evans as senior independent director. The senior independent director supports the Chairman in the delivery of the board's objectives and to ensure that the view of all shareholders and stakeholders are conveyed to the board. Mike Evans 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. The senior independent director also meets with the non-executive directors, without the Chairman present, at least annually, and conducts the annual appraisal of the Chairman's performance and provides feedback to the Chairman and the board on the outputs of that appraisal.

Directors and directors' independence

The board considers that all non-executive directors are independent. The Chairman was independent at the date of his appointment and that he was free from any business or other relationship with the company which could have materially influenced his judgement and he continues to represent a strong source of advice and independent challenge. There are currently four independent non-executive directors on the board: Mike Evans, Veronica Oak, David Brand and Jane Dale.

Other than their fees, and reimbursement of taxable expenses which are disclosed on page 63, the non-executive directors receive no remuneration from the company during the year. 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.

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.

CORPORATE GOVERNANCE REPORT (CONTINUED)

THE BOARD DIRECTORS RECEIVE REGULAR UPDATES AS WELL AS SPECIFIC SPECIALIST AND REGULATORY TRAINING.

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, their responsibilities and duties which is contained within the group's Governance Map, which covers 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 updated on the group's business and on the competitive and regulatory environment in which it operates. During the year, specific specialist areas of training have also been provided to the board, in particular IFRS17 and European governance regulations. Through their membership of the CA plc board, all of the directors who served during the period under review have considerable knowledge and experience of the UK-based businesses of the group. Similarly, Messrs Mason, Deane, Evans, Brand and Rimmington, through their membership of the divisional boards, between them have considerable knowledge and experience of both the Swedish and Dutch based businesses 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 subsidiaries within the UK, Dutch and Swedish divisions. These boards hold scheduled meetings, at least quarterly, which are serviced by regular reports and information, which cover all of the key areas relevant to the direction and operation of those subsidiary entities, including business development, key projects, financial performance and position, actuarial assumptions setting and results analysis, compliance, investments, operations, customer care and communication, internal audit, all aspects of the risk function and own risk and solvency assessment.

All divisional entities monitor risk management procedures, including the identification, measurement and control of risk through the auspices of a Risk Committee. These committees are accountable to and report 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.

In addition, the divisions are required to submit a quarterly risk report and an annual report on risk management and internal control systems.

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.

Board effectiveness and performance evaluation

As part of the annual performance, an internal effectiveness evaluation process of the board and its committees was undertaken in the year. This was through an anonymous questionnaire and individual meetings with each director to obtain their views on what was working well and what could be improved.

The discussions were wide-ranging, covering how well the board operates, the process of decision making, the balance between the focus on risk, fair customer outcomes and running the business, the culture and dynamics of the board ensuring its composition and that of its committees are aligned. In addition, using similar methods to those described above, the non-executive directors, led by Mike Evans as senior independent director, met to conduct a formal performance evaluation of the Chairman.

The outcome of the review of the board and its committees indicated that they continue to be effective and that each of the directors demonstrates commitment to his or her role, along with sufficient time to meet the required time commitment to the company. A number of improvements have been made in the year as a result of the actions emanating from the effectiveness review undertaken in 2017. In summary, the principal outputs of the review were that:

- the board should increase its employee and stakeholder engagement;
- the board should keep under close review, across all territories, the evolution of, and emerging trends in legislation and regulation across, the life insurance industry;
- IFRS17 regulation should continue to receive focus and monitoring of the implementation project; and
- focus should remain on the potential impact of the UK leaving the European Union.

Directors' conflicts of interest
The board has a policy and effective procedures in place for managing and, where appropriate, approving conflicts or potential conflicts of interest. This is a recurring agenda item at all board meetings, giving directors the opportunity to raise any conflicts of interest they may have or to update the board on any changes to previously lodged interests.
A director may be required to leave a board meeting whilst such matters are discussed.

The company secretary holds a register of interest, and a log of all potential conflicts raised is maintained and updated. Whenever a director takes on additional external responsibilities, the Chairman considers any potential conflicts that may arise and whether or not the director continues to have sufficient time to fulfil his or her duties. The board is empowered to authorise potential conflicts and agree what measures, if any, are required to mitigate or manage them. No new material conflicts of interest are noted in 2017.

Company secretary
Zoe Kubiak is the company secretary and is responsible for advising the board, through the Chairman, on all governance matters. The directors have access to the advice and services of the company secretary. Al Lonie will take over from Zoe Kubiak as company secretary on 1 April 2018.

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.

Remuneration Committee
Full details of the composition and work of the Remuneration Committee are provided on pages 60 to 61.

Audit & Risk Committee
Full details of the composition and work of the Audit & Risk Committee are provided on pages 80 to 85.

Nomination & Governance Committee
Full details of the composition and work of the Nomination & Governance Committee are provided on pages 58 to 59.

CORPORATE GOVERNANCE REPORT (CONTINUED)

The attendance record of each of the directors at scheduled board and committee meetings for the period under review is:

	Scheduled board	Nomination & Governance Committee	Remuneration Committee	Audit & Risk Committee
Peter Mason - Non-executive Chairman	11 (11)	5 (5)	4 (4)	8 (9)
John Deane - Executive director	11 (11)	5 (5)	4 (4)	8 (9)
Veronica Oak - Non-executive director	10 (11)	4 (5)	4 (4)	9 (9)
David Brand - Non-executive director	11 (11)	5 (5)	n/a	9 (9)
David Rimmington - Executive director	11 (11)	n/a	n/a	9 (9)
Jane Dale - Non-executive director	11 (11)	5 (5)	n/a	9 (9)
Mike Evans – Senior independent non-executive director	11 (11)	5 (5)	4 (4)	9 (9)

The figures in brackets indicate the maximum number of scheduled meetings in the period during which the individual was a board or committee member.

Relations with shareholders

The group chief executive and the group finance director meet with institutional shareholders 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 group chief executive and the group finance director with shareholders and is responsible for ensuring that the views of shareholders are known to the board. This includes twice yearly feedback prepared by the company's brokers on meetings the executive directors have held with institutional shareholders. The company has a programme of meetings with its larger shareholders which provides an opportunity to discuss, on the basis of publicly available information, the progress of the business.

Annual and interim reports are published 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**

All shareholders 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 2018 can be found in the notice of the meeting on pages 177 to 178.

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 the FRC's guidance on Risk Management, Internal Control and Related Financial and Business Reporting, the board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the group. This process has been in place for the year under review and up to the date of approval of the Annual Report and 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 and SII, the relevant business divisions have maintained and enhanced their 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 Audit & Risk Committee regularly reviews and reports quarterly on risks to the board.

The group also maintains a principal risk register which ensures identification, assessment and control of the significant risks subsisting within the company, CA, Waard Group, Movestic and Scildon. The principal risks and uncertainties of the group can be found on pages 43 to 45.

The maintenance of the principal risk registers is the responsibility of senior management, who report on them quarterly to the respective divisional Audit and Risk Committees and to each Chesnara Audit & Risk Committee meeting. The divisions maintain a risk and responsibility regime which ensures that:

– the boards and group 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 boards have responsibility for the satisfactory management and control of risks through the specification of internal procedures; and

– there is an explicit risk function, which is supported by compliance and internal audit functions.

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

All 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 the Waard Group, Scildon and Movestic, such oversight is exercised by way of the membership of a number of the Chesnara directors on their boards, together with quarterly reporting 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 2017, and that it has taken account of material developments between that date and the date of approval of the Annual Report and Accounts. The board confirms that these reviews took account of reports by the Internal Audit and Compliance 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. Conclusions of the Audit & Risk Committee annual review of effectiveness of the group's risk management and internal control systems is reported in more detail in the Audit & Risk Committee Report, set out on page 84. The board is not aware of any significant deficiencies in the effectiveness of the group's systems of internal control and risk management for the year under review. There has been no change of status to this up to the date of approval of this report.

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 are 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 Chesnara Audit & Risk Committee reviews the application of financial reporting standards and any significant accounting judgements made by management.

Going Concern and Viability Statement

The directors' Statement on Going Concern is included in the Directors' Report on page 88 and the Long-Term Viability Statement is set out on page 41.

NOMINATION & GOVERNANCE COMMITTEE REPORT

The main focus of the Nomination & Governance Committee considers the mix of skills and experience that the board requires to be effective and with focus on talent development and succession planning across the group.

Nomination & Governance Committee
During the period under review, the committee comprised Peter Mason, who also served as Chairman of the committee, David Brand, Veronica Oak, Jane Dale and Mike Evans, all of whom served throughout the period. The Chairman does not chair or attend when the committee is considering matters relating to his position, in which circumstances the committee is chaired by an independent non-executive director, usually the senior independent director. No individual participates in discussion or decision making when the matter under consideration relates to him or her.

The committee Chairman reports material findings and recommendations at the next board meeting.

The terms of reference for the committee can be found on the company website, **www.chesnara.co.uk**

The role of the Nomination & Governance Committee is to:

- keep under review the balance, structure, size 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;
- keep under review the leadership needs of, and succession planning for, the group in relation to both its executive directors and other senior management;
- identify and nominate, for the approval of the board, candidates to fill board vacancies as and when they arise;
- manage the search process for new directors, recommending appointments to the board; and
- evaluate the balance of skills, knowledge, experience and diversity of the board.

This includes consideration of recommendations made by the group chief executive officer for changes to the executive membership of the board.

During the period, the committee met four times and attendance at those meetings is shown on page 56 of the Corporate Governance Report.

The composition of the board
After a number of director changes in recent years, the committee has continued to focus on succession planning, with a view to identifying the best composition for the board and its committees for the next phase of development for the business. In reviewing board composition, it was noted that a number of directors were approaching six years on the board and accordingly some changes would be likely in the medium term. The review also identified areas where the board should evolve to meet any expected future business and strategic direction of the group.

The committee is mindful of the corporate governance developments in the areas of diversity and gender balance including the changes to the Disclosure and Transparency Rules. This will be kept under review during 2018, and any changes to the existing policies and objectives for board and management diversity will be reported in the next annual report.

The Nomination & Governance Committee agrees the importance of having diversity on the board, including female representation and individuals with different experiences, skills, background and expertise, to ensure an appropriate board balance is maintained. During the year, the Nomination & Governance Committee reviewed and recommended the approval of the Chesnara Diversity Policy. The board currently comprises five men and two women (28.5%). The key objective of the policy is stated below:

Chesnara plc recognises and embraces the benefits of having diversity at its board table in order to achieve and optimise competitive advantage. The board will aim to include and utilise directly, or through the board subsidiaries, differences in the skills, background, ethnicity, gender, regional and industry experience along with other qualities brought by its directors and those of its subsidiaries. Such differences will be considered in determining the optimum composition of the board and will be re-balanced as appropriate and when possible to ensure optimal and efficient stewardship.

The organisation also recognises the benefits of behavioural diversity, such as temperament and approach of individual directors and seeks to build the right mix of such independent character and judgement.

All board appointments are made on merit, in the context of the skills and experience required for the board to operate effectively as a unit and taking account of succession planning. Candidates are assessed against pre-defined and professional profile criteria. Chesnara remains committed to meritocracy in the boardroom, which requires a diverse and inclusive culture where directors believe that their view are heard, their concerns are attended to and they serve in an environment where bias, discrimination and harassment on any matter are not tolerated.

The development of talent below board level is extremely important and an area of focus for the board. The company continues to build an internal leadership pipeline for senior roles. The board believes by focusing on creating a pool of internal talent that there is an increased probability of employee retention and the building of internal capabilities needed to support the growth of the business.

The biographical details of the board and the committee membership for each director who served during 2017 can be found on pages 50 and 51.

Board appointment process
The committee adopts a formal and transparent procedure for the appointment of new directors to the board.

The board's process is to use independent external recruitment consultants for appointing directors. The company will provide a brief of the candidate desired, along with a role profile to the recruitment consultant. As part of the appointment process external recruitment consultants are asked to provide candidates from a diverse range of backgrounds. Candidates, who are deemed suitable, based on merit and against objective criteria, are submitted to the committee as a potential candidate. The committee will review a short list of suitable candidates against the criteria, and put forward for interview by the board and the executive management team suitably qualified candidates. Any candidate deemed suitable for appointment will, if necessary, first have to go through the fit and proper process as outlined in the Senior Insurance Managers Regime (SIMR) which came into full force on 7 March 2016.

Diversity
The board recognises the benefits of having diversity across all areas of the group. When considering the make-up of the board, the benefits of diversity are appropriately reviewed and balanced where possible and appropriate, including in terms of difference in skills, sector experience, gender, race, disability, age, nationality and other contributions that individuals may make. In identifying suitable candidates, the committee will seek candidates from a range of backgrounds, with the final decision being based on merit against the role criteria set. The board maintains its practice of embracing diversity and has therefore chosen, at this time, not to set any measurable gender based targets.

The board and its committees undertook annual effectiveness reviews and the respective Chairmen discussed the findings in each forum. Other standard processes were also undertaken, including Fit & Proper assessments, Board Diversity Policy Review, NED succession planning and the review of the effectiveness of the Chairman. Any areas where increased focus was considered to be of potential value will be taken into account as appropriate during 2018.

Succession planning
Succession planning is an important element of good governance, ensuring that Chesnara is fully prepared for planned or sudden departures from key positions throughout the group. The committee, in the year, has reviewed the succession plans for the board, the group executive committee and senior executives across the group. During the year, increased focus was given to talent and succession development throughout the group and new CEOs were appointed in Movestic, Scildon and Waard.

Non-executive director engagement
It is important to the board that non-executive directors are provided with training and development both within the business and at a group level. The board believes that ongoing training is essential to maintaining an effective and knowledgeable board. The company secretary supports the Chairman in ensuring that all new directors receive a tailored and comprehensive induction programme on joining the board. Continuing education and development opportunities are made available to all board members throughout the year. In 2017, a number of development initiatives have continued, these included one-to-one sessions with key members of the senior management team and training sessions given by external providers.

Directors standing for re-election
In accordance with the Code, all directors will offer themselves for re-election at the Company's 2018 AGM. Following the annual board effectiveness reviews of individual directors, as applicable and subject to re-election, the Chairman considers that each non-executive director remains independent and that each director:

– continues to operate as an effective member of the board;
– has the necessary skills, knowledge and experience to enable them to discharge their duties and contribute to the continued effectiveness of the board; and
– has sufficient time available to fulfil their duties.

The board, on the advice of the committee, recommends the re-election of each director proposed for re-election at the 2018 AGM. The full 2018 AGM notice can be found on page 177.

Peter Mason
Chairman of the Nomination & Governance Committee

28 March 2018

REMUNERATION COMMITTEE CHAIRMAN'S ANNUAL STATEMENT

Dear Shareholder,

I am pleased to present the 2017 Directors' Remuneration Report, for which we seek your support at our forthcoming Annual General Meeting (AGM), in May 2018.

The remuneration policy, which for ease of reference is appended to the remuneration report, was put to shareholders for a binding vote at our AGM on 17 May 2017 and approved by 97.93% of the votes cast, making it effective from that date and no changes are proposed this year. For shareholders' information, we have taken the opportunity to update the illustration of the application of the policy with data for 2018 (see page 71).

2017 – Another year of delivery
Chesnara has a very clear focus, to recap:

1. Maximise value from existing business;
2. Acquire life and pension businesses that meet the investment criteria of the company; and
3. Enhance value through profitable new business.

This clear strategic focus is underpinned by the culture, values and risk environment of the group, which looks to deliver solid investment returns and value for money for our customers. From a remuneration perspective we seek to achieve strong alignment between the interests of shareholders and executive directors, and continue to operate two executive incentive schemes: the Short-Term Incentive Scheme (STI) and Long-Term Incentive Scheme (LTI).

In 2017 we have seen delivery against all three strategic objectives at a level that has significantly enhanced shareholder value. The full results are set out on page 8, of note is:

1. Cash generation of £77.5m exceeding the funding requirements of the dividend.
2. Completion of the acquisition of LGN at a 32% discount to Economic Value, increasing the Economic Value of Chesnara by 31.0% as shown in the half year results issued in August 2017.
3. Movestic has delivered new business profits broadly in line with the prior year. Importantly the profit of £11.8m is within the challenging target range and represents a commercially attractive return. Movestic has provided to Chesnara a SEK31.5m (£2.8m) dividend payment which is a 5% increase compared to 2016.

Executive performance in 2017
In light of the performance of the executive team in 2017 relative to the financial targets and strategic objectives set, the Remuneration Committee is satisfied that the reward outcomes are appropriate. Our assessment of the performance outcomes in 2017 under the STI can be found on page 64.

The second awards made under the 2014 LTI are due to vest in April 2018 and apply to John Deane (GCEO) and David Rimmington (GFD). The targets, performance outcome and estimated value of awards can be found in the table on page 66. Following shareholder feedback, disclosure of the embedded value outcome now enables comparison with opening values.

Changes to the directors' salary
In line with our remuneration policy, it is our normal practice to award executive directors, and indeed all employees, an annual salary increase broadly in line with inflation.

UK employees received an average salary increase of 2% in 2017 and 2.5% in 2018. The salary of John Deane (GCEO) has been increased in line with these. David Rimmington, (GFD) has continued to develop in his role and has been awarded an increase of 2.4% above the average (total 4.9%) which the committee considers to be a merited increase, resulting in a salary which is neither excessive relative to pay internally or the market generally. The executive directors remuneration for 2018 can be found on page 63.

In line with the average salary increase to staff, the board has increased the base fee and committee chairmanship fees for non-executive directors by 2.5%. The Chairman's role has expanded following the acquisition of Scildon in the Netherlands and, in recognition of this extra time commitment, the Chairman's fees have increased by £9,500 to £120,000, which includes an inflationary increase of 2.5%. By comparison with businesses of a similar size, it is our assessment that fees to the Chairman remain modest.

Review of incentive scheme performance measures
As noted in my report last year, we have considered the performance targets used within the short-term and long-term incentive schemes to ensure that they remain effective and appropriate.

Short-Term Incentive Scheme – under this scheme, the committee has discretion to determine with each award the performance criteria in accordance with the remuneration policy. No changes have been considered necessary and consequently continue to be assessed against financial targets and strategic objectives – see full details on page 71.

The Long-Term Incentive Scheme aims to align executive and shareholder interests via two equally weighted metrics: (1) Total Shareholder Return (TSR); and (2) Embedded Value (EEV) / Economic Value (EcV) – these latter being a measure of shareholder value. Following the advent of Solvency II, EEV has been replaced with Economic Value (EcV). Therefore, for performance years starting before 1/1/2016 the measure used is EEV, whilst EcV is the measure used for performance years starting on or after 1/1/2016.

Shareholder engagement
The Directors' Remuneration Report for the year ended 31 December 2017 comprises my Annual Statement as Chairman of the Remuneration Committee and our Annual Remuneration Report, which together are subject to an advisory shareholder vote at the AGM in May 2018.

The voting outcome at the 2017 AGM in respect of the Directors' Remuneration Report for the year ended 31 December 2016 is set out on page 63 and reflects the support of both private and institutional shareholders. The committee will continue to be mindful to the interests of shareholders and other stakeholders and I welcome shareholder feedback.

Future developments
We have continued to monitor developments in the area of remuneration, whether that is via enhancements to accepted best practice, regulatory guidance or legal requirements. Following publication of the Government's response to the Green Paper on Corporate Governance and Executive Pay in autumn 2017, we are reviewing the reform proposals and will consider changes as appropriate in line with the reforms coming into effect. One of the proposals we have already adopted is to present in our remuneration report a comparison between the total pay received by our chief executive and the average of total pay for our UK workforce. This is set out on page 70.

I hope my annual statement, together with our remuneration report, provides a clear account of the operation of the Remuneration Committee during 2017 and how we have put our remuneration policy into practice. I'm very happy to talk to shareholders to discuss any aspect of our activities or decisions.

Veronica Oak
Chairman of the Remuneration Committee

28 March 2018

ANNUAL REMUNERATION REPORT

This section sets out how the Remuneration Committee has implemented its remuneration policy for executive directors during 2017.

Other than the single total figure of remuneration for each director tables on page 63, payments for loss of office and statement of directors' shareholding and share interests on pages 67 and 68, the information contained within this report has not been subject to audit.

Composition and activities of the Remuneration Committee
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 2017. Members of the Remuneration Committee during the course of the year were:

Committee Members	Role on the committee	Committee member since	Attendance in 2017	Maximum possible meetings in 2017
Veronica Oak	Committee Chairman	January 2013	4	4
Peter Mason	Committee member	March 2004	4	4
Mike Evans	Committee member	March 2013	4	4

Peter Mason was not present when the Chairman's fees were discussed. By invitation, the group chief executive attends Remuneration Committees, but was not present when matters relating to his own remuneration were discussed.

The committee does not retain the services of external advisers.

Highlights 2017/2018
In 2017 the committee met four times and dealt with the following matters:

Area of focus	Matter considered
Executive director remuneration and reward	The committee considered the scheme awards and performance targets for the awards made in 2017 under the 2014 STI Scheme and the 2014 LTI Scheme for executive directors. A half-year evaluation was also undertaken.
All employee and executive remuneration	A review of remuneration trends across the group revealed that pay remains at appropriate levels and is not adversely affecting staff turnover or the ability to recruit new members of staff with the required skills and experience.
Terms of Reference	The committee's Terms of Reference were reviewed and it was concluded that they continue to be appropriate for the activities of the committee.
Review of the remuneration policy	The committee reviewed and updated the remuneration policy and recommended to the board that the policy be put to shareholders at the 2017 AGM. Following approval at the AGM, the company's remuneration policy continued to be monitored during the course of the year and no changes were deemed necessary.
Committee evaluation	An evaluation of the committee's performance by way of an internal questionnaire suggested that the committee continued to operate well. To ensure adequate time allocation was provided to the meetings in 2017, the committee changed to hold meetings on a separate day to all other meetings.
Annual salary review	The committee reviewed the salaries of the executive directors and made changes in line with its remuneration policy.
Directors' remuneration reporting	The committee reviewed the draft Directors' Remuneration Report for the 2017 Report & Accounts and recommended their approval by the Chesnara board.
Performance against strategic targets	The committee reviewed the executive directors' performance against targets set. It was the view of the committee that executives have performed well against targets set – see page 65.
Directors' minimum shareholding	The committee reviewed and agreed that no changes be made at present in relation to the quantum of shares required to be held by executive directors. The committee also reviewed the value of shares held by executives relative to the minimum requirement.
Shareholder engagement	The chairman addressed various queries from shareholders in advance of the 2017 AGM. The committee sought feedback from institutional investors in relation to the direction of voting at the 2017 AGM.
Chairman's fees	The committee reviewed the level of fees payable to the Chairman and took into account the increased time commitment arising from the Scildon acquisition as well as inflation and made its recommendation to the board.
Remuneration principles	The committee reviewed the Group Remuneration Principles, which guide the remuneration policies throughout the group.
Solvency II	The committee reviewed the PRA's Solvency II remuneration requirements and assessed the implications for Chesnara.
Review against UK Governance Code	A review was conducted by the committee and revealed that the Code had been complied with.

Statement of voting at general meeting

The following table sets out the voting in respect of the Directors' Remuneration Report and remuneration policy at the 2017 AGM:

Report	Number of votes cast for	Percentage of votes cast for	Number of votes cast against	Percentage of votes cast against	Total votes cast	Number of votes withheld
Remuneration report	93,524,042	99.06%	884,070	0.94%	94,408,112	32,919
Remuneration policy	92,417,545	97.93%	1,958,029	2.07%	94,375,574	65,457

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

The remuneration of the executive directors for the years ended 31 December 2017 and 31 December 2016 is made up as follows:

Executive directors' remuneration as a single figure - year ended 31 December 2017

Name of director	Salary and fees £000	All taxable benefits £000	Non-taxable benefits £000	Annual bonuses £000	LTI £000	Pension £000	Total for 2017 £000
John Deane	428	27	5	373	261	41	1,135
David Rimmington	264	17	4	206	169	25	685
Total	**692**	**44**	**9**	**579**	**430**	**66**	**1,820**

Executive directors' remuneration as a single figure - year ended 31 December 2016

Name of director	Salary and fees £000	All taxable benefits £000	Non-taxable benefits £000	Annual bonuses £000	LTI[3] £000	Pension[2] £000	Total for 2016 £000
John Deane	420	27	2	413	–	40	902
David Rimmington	250	14	4	222	103	24	617
Frank Hughes[1]	212	18	7	167	120	20	544
Total	**882**	**59**	**13**	**802**	**223**	**84**	**2,063**

Notes:

1. Frank Hughes stepped down from the board effective 31 December 2016.
2. The pension component in the single figure table represents employer contributions. No directors were members of a defined benefit scheme.
3. These figures have been re-stated to reflect the actual share price at the date of vesting of 383.0 pence.

The remuneration of the non-executive directors for the years ended 31 December 2017 and 31 December 2016 is made up as follows:

Non-executive directors' remuneration as a single figure - year ended 31 December 2017 and 2016

Name of director	2017			2016		
	Fees £000	Benefits[3] £000	Total £000	Fees £000	Benefits[3] £000	Total £000
Peter Mason	111	1	112	108	–	108
Peter Wright[1]	–	–	–	65	–	65
Veronica Oak	58	1	59	55	1	56
David Brand	58	1	59	55	–	55
Mike Evans	58	1	59	55	1	56
Jane Dale[2]	63	1	64	34	–	34
Total	**348**	**5**	**353**	**372**	**2**	**374**

Notes:

1. Peter Wright stepped down from the board effective 31 December 2016.
2. Jane Dale was appointed to the board effective 19 May 2016.
3. Benefits shown here relate to expenses grossed up for income tax, which is settled by the company for travel to Chesnara's head office in Preston, which, for tax purposes, is deemed to be the NEDs normal place of work.

ANNUAL REMUNERATION REPORT (CONTINUED)

Salary and fees

The Remuneration Committee usually reviews basic salaries annually. 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 remuneration policy for the executive directors is designed with regard to the policy for employees across the group as a whole. Our ability to meet our growth expectations and compete effectively is dependent on the skills, experience and performance of all our employees. Our employment policies, remuneration and benefit packages for employees are regularly reviewed. There are some differences in the structure of the remuneration policy for the executive directors and senior management team compared to other employees, reflecting their differing responsibilities, with the principal difference being the increased emphasis on performance related pay for the more senior employees within the organisation.

Employee share ownership is encouraged and facilitated through participation in the SAYE Scheme (subject to minimum service requirement).

Although the committee does not consult directly with employees on directors' pay, the committee does take into consideration the pay and employment conditions of all employees when setting directors' remuneration, including the average level of salary increase being budgeted for the UK workforce. The committee is also mindful of any changes to the pay and benefit conditions for employees more generally when considering directors' pay.

Payments in respect of salary and pension benefits amounting to £47,392 were made to Frank Hughes who remained an employee until 30 April 2017, following the cessation of his role as director on 31 December 2016. In addition, he received taxable benefits during this period of £5,574.

Taxable benefits

The taxable benefits for executive directors relate to the provision of a car, fuel allowance and medical insurance. For non-executive directors, the taxable benefits represent the reimbursement of travelling expenses incurred in attending board meetings at the Preston head office. These amounts also include an amount to compensate for the personal tax burden incurred.

Annual bonuses

The amounts reported as annual bonuses in 2017 derive from awards made under the 2014 STI. The amounts awarded to the executive directors under this scheme are based on performance against three core measures; IFRS pre-tax profit, EcV operating profit and group strategic objectives. The table below shows the outcome of each measure, the target set and the resulting award.

	Upper threshold for minimum performance	Percentage award for min performance	On target performance	Percentage award for on target performance	Minimum threshold for maximum performance	Percentage award for maximum performance	Actual result	Actual percentage total award	Actual percentage award, as %age of salary	Total award (£)
John Deane										
IFRS pre-tax result*	£27.230m	0%	£36.307m*	15.0%	£72.614m	50.0%	£74.683m	50.0%	50.0%	214,200
EcV operating result**	£14.059m	0%	£15.621m	12.8%	£23.432m	30.0%	£18.500m	19.1%	19.1%	81,996
Group strategic objectives	75% of max	0%	100% of max	10.0%	100%	20.0%	89.1% of max	17.9%	17.9%	76,341
Total				**37.8%**		**100.0%**		**87.0%**	**87.0%**	**372,537**
David Rimmington										
IFRS pre-tax result*	£27.230m	0%	£36.307m*	13.5%	£72.614m	45.0%	£74.683m	50.0%	45.0%	118,800
EcV operating result**	£14.059m	0%	£15.621m	11.5%	£23.432m	27.0%	£18.500m	19.1%	17.2%	45,444
Group strategic objectives	75% of max	0%	100% of max	9.0%	100%	18.0%	88.7% of max	17.8%	16.0%	42,160
Total				**34.0%**		**90.0%**		**86.9%**	**78.2%**	**206,404**

For results between the performance thresholds, a straight-line basis applies.

* **Note** – this is stated after certain adjustments, such as consolidation adjustments. The actual results are also adjusted in the same manner.

** **Note** – the EcV operating earnings before exceptional items on page 38 has been adjusted in line with the basis of the target. The result has been reduced to reflect the exceptional item in Movestic but no adjustment has been made for investment in the Scildon development programme (see note 2 on page 38).

The following table details the requirements for delivery of the strategic objectives for 2017 and actual outcomes:

Objectives area	Objectives and performance	Outcome
John Deane		
Governance (20%)	Ensure a robust strategy and management reporting process is in place.	Board papers consistently of a high standard and enhanced through the year, including improvements to integration with the strategy development process, actions on customer communications and monitoring. Risk Management Framework further developed.
Regulator management (20%)	Maintain strong and constructive relationships with regulators.	Strong relationships maintained with all regulators. Scildon capital plan and new plan for Waard agreed with the DNB in the Netherlands and delivered all FCA information requests.
Acquisition and capital management (30%)	Support the investigation of acquisitions within risk appetite. Improve the consideration of capital management within the divisions and across the group.	Acquisitions that have been investigated have followed a defined risk based approach, with working parties established to oversee that process. Progressed in 2017 with further work identified for 2018.
Integration of Scildon (20%)	Ensure that Scildon is integrated into Chesnara in line with the governance map.	Good progress on the integration of Scildon in governance, financial reporting and cost saving initiatives with Waard.
People (10%)	Support divisional CEOs in their roles.	Appointment of new CEOs for Waard and Scildon in March and in Movestic in April with very smooth transitions.
David Rimmington		
Divisional oversight (20%)	Develop and embed with the 3 divisions.	2017 saw a significant expansion of the group but no reduction in the effectiveness of reporting and oversight with enhancements as necessary, delivered.
Expense management (15%)	Develop enhanced group wide expense analysis and reporting to enable appropriate management decisions regarding expenses.	Established a working group to drive out opportunities along with a review and revision of delegated authority levels that will be embedded in 2018.
Acquisition funding (10%)	Develop multi bank consortium facilities to support acquisition.	Negotiations successfully completed and effective from April 2018.
Reporting (35%)	Further development of MI for the group and divisions and production of SII reports.	Solvency II reporting delivered on time and to the quality required. Group MI packs enhanced and have driven agendas at Chesnara and board level.
Integration of Scildon (20%)	Integrate Scildon into Chesnara in line with the governance map.	Good progress on the integration of Scildon in governance, financial reporting and cost saving initiatives with Waard.

ANNUAL REMUNERATION REPORT (CONTINUED)

Annual bonuses (continued)

In converting performance against the measures assessed for 2017 set out in the previous tables, the directors' annual bonus awards are specified below:

Name of director	Salary on which award based £	Maximum potential award as %age of salary	Actual award as %age of salary	Total value of award £
John Deane	428,400	100%	86.96%	372,537
David Rimmington	264,000	90%	78.18%	206,404
Total				**578.941**

35% of the above awards are granted as deferred share awards that will vest at the end of a three-year deferred period.

Long-Term Incentive Scheme Awards

The following table sets out the amounts that are due to vest on 28 April 2018 under the 2014 LTI, for which performance conditions were satisfied during the year.

Individual	Measure	Weight	Ranges and targets			Actual outcome				
			Minimum achievement (as % of target)	Target achievement	Max achievement	Opening EcV	Closing EcV (Note 1)	Performance achieved	% of award vesting	Value of award £
John Deane	TSR	50%	=Median	21.28%	46.36%			33.62%	30.95%	100,412
	EcV	50%	=89.0%	£478.6m	£545.8m	£417.2m	£733.4m	153.2%	50.0%	160,650
David Rimmington	TSR	50%	=Median	21.28%	46.36%			33.62%	30.95%	56,622
	EcV	50%	=89.0%	£478.6m	£545.8m	£417.2m	£733.4m	153.2%	50.0%	91,473

The estimated value of the awards vesting disclosed above has been determined using the average share price over the three-month period prior to the year-end (383.31p). The actual amounts upon vesting will be determined using the share price upon the vesting date.

Note 1: The closing value for EcV is based on that shown on page 39 with the addition of dividends paid out and the deduction of equity raised in the performance period which is consistent with basis upon which the targets are set.

The table below sets out potential LTI interests that have accrued during the year, and each directors' interest in that scheme:

Name of executive director	Name of scheme	Date award was granted	Amount of options awarded[1]	Face value on the date of grant[2]	% of award vesting for minimum performance	Length of vesting period – 3 years Date of vesting
John Deane	2014 LTI	28 April 2017	111,781	£428,400 based on share price (383.25p)	12.5%	28 April 2020
	2014 LTI	28 April 2016	133,017	£415,013 based on share price (312.00p)	12.5%	28 April 2019
	2014 LTI	28 April 2015	84,639	£269,998 based on share price (319.00p)	12.5%	28 April 2018
David Rimmington	2014 LTI	28 April 2017	61,996	£237,600 based on share price (383.25p)	12.5%	28 April 2020
	2014 LTI	28 April 2016	71,259	£222,328 based on share price (312.00p)	12.5%	28 April 2019
	2014 LTI	28 April 2015	47,727	£152,249 based on share price (319.00p)	12.5%	28 April 2018

Basis of awards and summary of performance measures and targets

2014 LTI:
Share options awarded are based on the share price at close of business on date of award and a percentage of basic salary as follows: John Deane; 75% in 2015, 100% in 2016 and 2017. David Rimmington; 75% in 2014 and 2015, 90% in 2016 and 2017. Options have a nil exercise price.

Total Shareholder Return (TSR)
50% of the award will vest subject to the TSR target being in a certain range, with the range being the ranking of the TSR of Chesnara against the TSR of the individual companies in the FTSE 350 Higher Yield Index. The award will be made on a sliding scale from nil if the Chesnara TSR is below the median to full if the Chesnara TSR is in the upper quartile.

EEV/EcV growth target
The LTI Scheme has transitioned to Economic Value (EcV) as an equivalent post Solvency II replacement for Embedded Value (EEV). For performance years starting before 1/1/2016 the measure will be EEV. For performance years starting on or after 1/1/2016 the measure is EcV. 50% of the award will vest subject to the EEV/EcV outcome being within a certain range of its target. The award will be made on a sliding scale with nil being paid out if the outcome is less than or equal to 89% of target, up to a maximum pay-out if the outcome is greater than or equal to 114% of target.

Note 1 – No awards are made if performance is below the minimum criteria.
Note 2 – The face value is reported as an estimate of the maximum potential value on vesting.

Payments for loss of office (audited information)
No payments were made during the year for loss of office.

Statement of directors' shareholding and share interests (audited information)
The remuneration policy, effective from the 2017 AGM, requires executive directors to build up a shareholding through the retention of shares to the value of their basic salary. As at the reporting date this criteria had not yet been met. When the minimum holding level has not been achieved, directors may only dispose of shares where funds are required to discharge any income tax and National Insurance liabilities arising from awards received from a Chesnara incentive plan. The Chairman and non-executive directors are encouraged to hold shares in the company but are not subject to a formal shareholding guideline.

ANNUAL REMUNERATION REPORT (CONTINUED)

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 2017 or the date of resignation.

No changes took place in the interests of the directors between 31 December 2017 and 28 March 2018.

Name of director	Shares held: 1 January 2017	Shares held: 31 December 2017	Options: With performance measures	Options: Without performance measures[1]	Options: Vested but unexercised	Options: Exercised during the year	Options: Percentage of shareholding target held[2]
John Deane	19,677	29,677	329,437	70,569	–	–	85.4%
David Rimmington	8,848	20,781	180,982	56,111	14,856[3]	26,944	104.1%
Peter Mason	25,743	25,743	–	–	–	–	–
Veronica Oak	3,000	3,000	–	–	–	–	–
David Brand	5,500	5,500	–	–	–	–	–
Mike Evans	7,956	7,956	–	–	–	–	–
Jane Dale	3,333	3,333	–	–	–	–	–
Total	**74,057**	**95,990**	**510,419**	**126,680**	**–**	**–**	**–**

Notes

1. The 'options without performance measures' column in the table does not include the share options that will be awarded as part of the mandatory deferral rules under the 2014 STI in respect of awards made in relation to the 2017 financial year, which equate to 35% of the cash award under this scheme. The timetable for the administration of the scheme means that these will be reported in the 2018 Annual Report and Accounts.
2. Calculated using the share price of 389.25p at 31 December 2017.
3. Awarded under the 2014 LTI Scheme and vested on 20 May 2017.

Outstanding share options and share awards

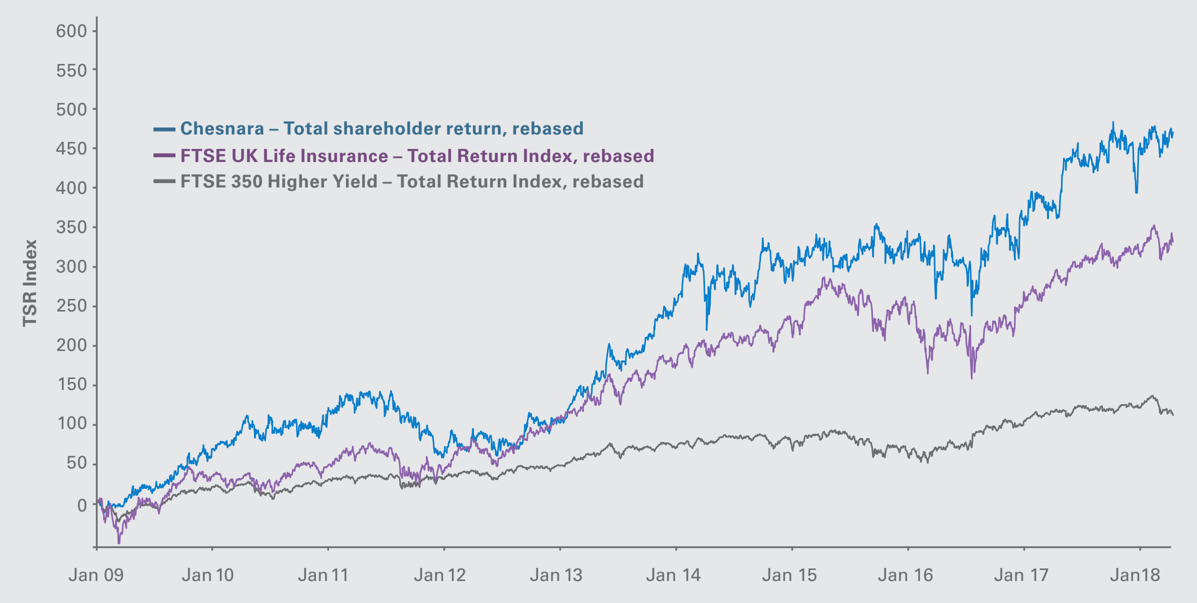
Below are details of outstanding share options and awards for current and previous executive directors.

Name of executive director	Scheme	Grant date	Exercise price (p)	Number of shares under option at 1 January 2017	Number granted during year	Number exercised during the year	Number lapsed during the year	Number waived during the year	Number of shares under option and unexercised at 31 December 2017	End of performance period	Vesting date	Performance period	Date of expiry of option
JOHN DEANE	2014 LTI (2017 award)	28/04/17	Nil	–	111,781	–	–	–	111,781	31/12/19	28/04/20	3 Years	28/04/27
	2014 LTI (2016 award)	28/04/16	Nil	133,017	–	–	–	–	133,017	31/12/18	28/04/19	3 Years	28/04/26
	2014 LTI (2015 award)	28/04/15	Nil	84,639	–	–	–	–	84,639	31/12/17	28/04/18	3 Years	28/04/25
	2014 STI (2016 award)	28/04/17	Nil	–	37,696	–	–	–	37,696	n/a	28/04/20	n/a	28/04/26
	2014 STI (2015 award)	28/04/16	Nil	26,575	–	–	–	–	26,575	n/a	28/04/19	n/a	28/04/25
	Share save	29/09/15	285.08	6,298	–	–	–	–	6,298	n/a	01/11/18	n/a	n/a
				250,529	**149,477**	**–**	**–**	**–**	**400,006**				
DAVID RIMMINGTON	2014 LTI (2017 award)	28/04/17	Nil	–	61,996	–	–	–	61,996	31/12/19	28/04/20	3 Years	28/04/27
	2014 LTI (2016 award)	28/04/16	Nil	71,259	–	–	–	–	71,259	31/12/18	28/04/19	3 Years	28/04/26
	2014 LTI (2015 award)	28/04/15	Nil	47,727	–	–	–	–	47,727	31/12/17	28/04/18	3 Years	28/04/25
	2014 LTI (2014 award)	20/05/14	Nil	41,800	–	(26,944)	(14,856)	–	–	31/12/16	20/05/17	3 Years	20/05/24
	2014 STI (2016 award)	28/04/17	Nil	–	20,293	–	–	–	20,293	n/a	28/04/19	n/a	28/04/25
	2014 STI (2015 award)	28/04/16	Nil	15,434	–	–	–	–	15,434	n/a	28/04/19	n/a	28/04/25
	2014 STI (2014 award)	27/03/15	Nil	14,086	–	–	–	–	14,086	n/a	27/03/18	n/a	20/05/24
	Share save	29/09/15	285.08	6,298	–	–	–	–	6,298	n/a	01/11/18	n/a	n/a
				196,604	**82,289**	**(26,944)**	**(14,856)**	**–**	**237,093**				
FRANK HUGHES*	2014 LTI (2016 award)	28/04/16	Nil	50,364	–	–	–	(33,576)	16,788	31/12/18	28/04/19	3 Years	28/04/26
	2014 LTI (2015 award)	28/04/15	Nil	48,399	–	–	–	(16,133)	32,266	31/12/17	28/04/18	3 Years	28/04/25
	2014 LTI (2014 award)	20/05/14	Nil	48,443	–	(31,227)	(17,216)	–	–	31/12/16	20/05/17	3 Years	20/05/24
	2014 STI (2015 award)	28/04/16	Nil	14,027	–	–	–	–	14,027	n/a	28/04/19	n/a	28/04/25
	2014 STI (2014 award)	27/03/15	Nil	15,237	–	–	–	–	15,237	n/a	27/03/18	n/a	20/05/24
	Share save	29/09/15	285.08	6,298	–	(3,324)	(2,974)	–	–	n/a	01/11/18	n/a	n/a
				182,768	**–**	**(34,551)**	**(20,190)**	**(49,709)**	**78,318**				

***Note:** Frank Hughes stepped down from the board effective 31 December 2016.

Performance graph and CEO remuneration table

The following graph shows the company's performance compared with the performance of the FTSE 350 Higher Yield Index and the FTSE UK Life Insurance Index. The FTSE 350 Higher Yield Index has been selected since 2014 as a comparison because it is the index used by the company for the performance criterion for its LTI, 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 group chief executive:

Year	Individual performing CEO role	CEO single figure of total remuneration £000	Annual bonus pay-out against maximum	Long term incentive vesting rates against maximum opportunity	Note
2017	John Deane	1,135	86.96%	80.95%	1
2016	John Deane	902	98.33%	–	1
2015	John Deane	596	81.96%	–	1
2014	Graham Kettleborough	712	91.30%	34.52%	2
2013	Graham Kettleborough	702	100.00%	n/a	3
2012	Graham Kettleborough	612	65.48%	100.00%	4
2011	Graham Kettleborough	384	17.39%	n/a	5
2010	Graham Kettleborough	631	100.00%	n/a	5
2009	Graham Kettleborough	502	94.27%	n/a	5

Note 1 – John Deane was appointed CEO on 1 January 2015.

Note 2 – During 2014 an LTIP that was granted to the CEO in 2012 vested. The LTIP included a condition such that the sum of the LTIPs and annual bonuses awarded in that year could not exceed 100% of the CEO's salary. The annual bonus in 2012 amounted to 65.48% of salary. When the performance measurements for the 2012 LTIP were assessed, the award was required to be restricted due to the operation of the 100% cap combined cap, such that the 2012 LTIP paid out 34.52% of the salary at the time of award.

During 2014 the annual bonus that was awarded represented 68.5% of the CEO's salary. The maximum payable was up to 75% of the CEO's salary, resulting in a 91.3% pay-out with reference to the maximum potential award.

Note 3 – During 2013 no LTIP value was earned because the annual bonus in isolation accounted for the full 100% combined bonus cap.

Note 4 – 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 5 – 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.

Percentage change in remuneration for the executive directors

The table below shows the percentage change in remuneration for the executive directors and the company's employees as a whole between the years 2017 and 2016.

Percentage change in remuneration in 2017 compared with 2016	Group chief executive %	Group finance director %	Group employees %
Salary and fees[1]	2.00	5.60	7.18
All taxable benefits	0.81	0.19	3.94
Annual bonuses	(16.33)	(13.90)	37.18

ANNUAL REMUNERATION REPORT (CONTINUED)

Comparison of total remuneration for the group CEO and UK employees

Following review of the Government's response to the Department of Business, Energy and Industrial Strategy Green Paper on Corporate Governance Reform, and mindful of likely guidance and regulatory requirements to be presented in 2018, a comparison of total remuneration for the group chief executive and an average of total remuneration for UK employees has been prepared for 2017.

Comparison of total remuneration in 2017	Group chief executive £	UK employees (average total remuneration) £	Ratio of group chief executive remuneration to UK employees (average total remuneration)
Total remuneration[1]	1,135,000	100,255	11.32

Note 1: This represents a single figure for total executive director remuneration in the year, compared to the average total remuneration of the UK workforce.

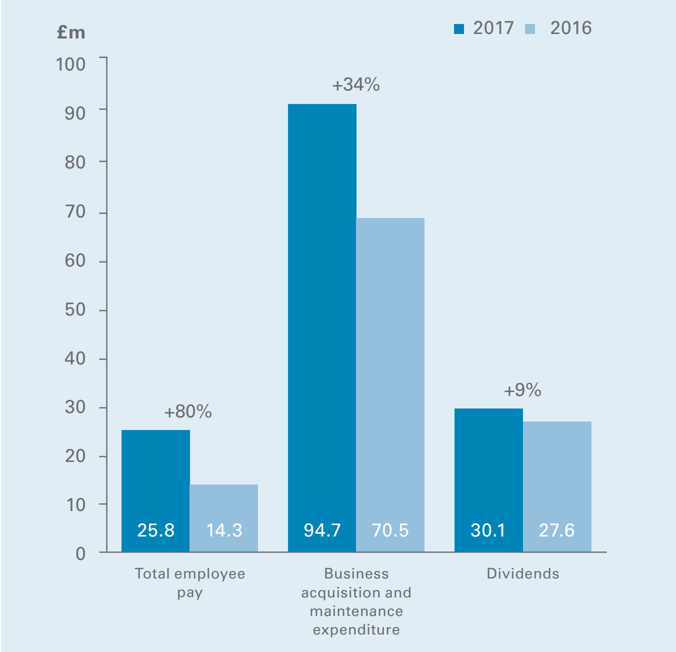
Relative importance of spend on pay

The graph to the right shows the actual expenditure of the group and change between the current and previous years:

The increases in employee pay and acquisition and maintenance expenditure, reflect the incremental costs in relation to Scildon, which was acquired in 2017.

The percentage increase in dividends is higher than the underlying increase in dividends per share, as it incorporates the impact of having an increased number of shares in issue, following the equity raising exercise in late 2016, to support the Scildon acquisition.

Due to Chesnara adopting 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. This has been chosen as a comparator to give an indication of the employee pay relative to the overall cost base. As can be seen, the total employee pay is a relatively small component.



Statement of Implementation of remuneration policy in the following financial year
The remuneration policy took effect following approval at the 2017 AGM. This section sets out how the policy will be implemented during 2018.

Salaries and fees

Executive directors
The salary of John Deane (GCEO) has been increased from £428.4k to £439.1k in line with the 2.5% average pay increase awarded to UK staff. David Rimmington, (GFD) has continued to develop in his role and has been awarded an increase of 2.4% above the average (total 4.9%) which the committee considers to be a merited increase resulting in a salary which is neither excessive relative to pay internally or the market generally. This translates to an increase in salary from £264k to £277k.

Non-executive directors
In line with the average salary increase to staff, the board has increased the base fee and committee chairmanship fees for non-executive directors by 2.5%. The Chairman's role has expanded following the acquisition of Scildon in the Netherlands and, in recognition of this extra time commitment, the Chairman's fees have increased by £9,500 to £120,000, which includes an inflationary increase of 2.5%.

The table below sets out the anticipated payments to non executive directors for 2018:

	Fees £000	Benefits* £000	Total £000
Peter Mason	120.00	1	121.00
Veronica Oak	59.45	1	60.45
David Brand	59.45	1	60.45
Mike Evans	59.45	1	60.45
Jane Dale	64.58	1	65.58
Total	**362.93**	**5**	**367.93**

* Benefits shown here relate to expenses grossed up for income tax which is settled by the company for travel to Chesnara's head office in Preston, which, for tax purposes, is deemed to be the NEDs normal place of work.

2018 award under the 2014 Short-Term Incentive Scheme
The Remuneration Committee proposes to grant awards to the executive directors under the 2014 Short-Term Incentive 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 deemed to be commercially sensitive and whilst they are not disclosed at this stage, they will be disclosed in 2018 together with the performance outcome relative to these targets.

Individual	Measures	Weighting	Ranges and targets			Potential outcomes in terms of % of basic salary		
			Minimum achievement (as % of target)	Target achievement (as % of target)	Max achievement (as % of target)	Minimum achievement	Target achievement	Max achievement
John Deane	IFRS pre-tax profit	40.0%	75.0%	100.0%	200.0%	nil	12.0%	40.0%
	EcV operating profit	40.0%	90.0%	100.0%	150.0%	nil	16.0%	40.0%
	Group strategic objectives	20.0%	75.0%	100.0%	125.0%	nil	10.0%	20.0%
David Rimmington	IFRS pre-tax profit	40.0%	75.0%	100.0%	200.0%	nil	10.8%	36.0%
	EcV operating profit	40.0%	90.0%	100.0%	150.0%	nil	14.4%	36.0%
	Group strategic objectives	20.0%	75.0%	100.0%	125.0%	nil	9.0%	18.0%

The STI will be implemented and operated by the Remuneration Committee as set out within the remuneration policy.

Measures
The three measures selected by the Remuneration Committee continue to ensure there is 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 EcV 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 objectives assigned to each executive director are relevant to their roles and include major regulatory or business development initiatives that the Committee considers key to delivery of the company's business plan. 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 Remuneration Committee has set the weightings. The financial measures that align most directly to shareholder benefit are generally assigned a higher weighting.

Targets
The IFRS pre-tax profit and EcV operating profit targets are initially based on the latest budget which is produced annually as part of the 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, in accordance with the scheme rules.

Malus and Clawback
This scheme includes malus and clawback provisions covering material misstatement, assessment error and misconduct if this arises within two years of an award vesting.

2018 award made under the 2014 LTI

In 2018 the Remuneration Committee proposes to grant awards to the executive directors under the Chesnara 2014 Long-Term Incentive 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 EcV target is commercially sensitive and will not be disclosed until 2021 together with the actual performance against those targets.

Individual	Measures	Weighting	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
John Deane	TSR	50%	=Median	Median	Upper quartile	nil	12.5%	50.0%
	EcV	50%				nil		50.0%
David Rimmington	TSR	50%	=Median	Median	Upper quartile	nil	11.3%	45.0%
	EcV	50%				nil		45.0%

The 2018 award under the 2014 LTI will be implemented and operated by the Remuneration Committee as set out within the remuneration policy.

Measures

The two performance measures for the 2018 LTI award use performance against the constituents of an index and an internal target. The external measure compares the 3-year TSR of Chesnara plc with the TSR of the companies comprising the FTSE 350 Higher Yield Index with averaging over the first and last calendar months. The internal measure assesses Economic Value growth which are set with due regard to the Board approved business plan. Both measures seek to 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 2020.

Weightings

For the 2018 award the two measures have been assigned equal weighting.

Targets

TSR: The Remuneration Committee proposes that the constituents of the FTSE 350 Higher Yield Index represents the most appropriate peer group for assessing the relative TSR performance. The award equates to 12.5% and 11.3% of salary for achieving median performance for John Deane and David Rimmington respectively, increasing on a straight-line basis to 50.0% and 45.0% of salary respectively for upper quartile performance.

EcV: The Economic 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 expectations for new business value from Movestic and Scildon. 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, in accordance with the scheme rules.

Malus and Clawback

This scheme includes malus and clawback provisions covering material misstatement, assessment error and misconduct if this arises within two years of an award vesting.

Approval

This report was approved by the board of directors on 28 March 2018 and signed on its behalf by:

Veronica Oak
Chairman of the Remuneration Committee

REMUNERATION POLICY

The current Remuneration Policy was approved by our shareholders at the Annual General Meeting held on 17 May 2017. The Policy as approved by shareholders can be found on our website: www.chesnara.co.uk/corporate-responsibility/governance-reports

Introduction
Remuneration policy
The policy has been developed by the committee to provide a clear framework for reward linked to the strategy of the company, aligned to the interests of executives and shareholders.

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, objectives and KPIs for the business, and developments in the external marketplace. The company has not consulted with employees.

Alignment of incentives with strategy
Chesnara plc is a holding company engaged in the management of life and pension books of business in the UK, Sweden and the Netherlands with oversight and governance being provided by a central governance team based in the UK.

The company has three core strategic objectives:

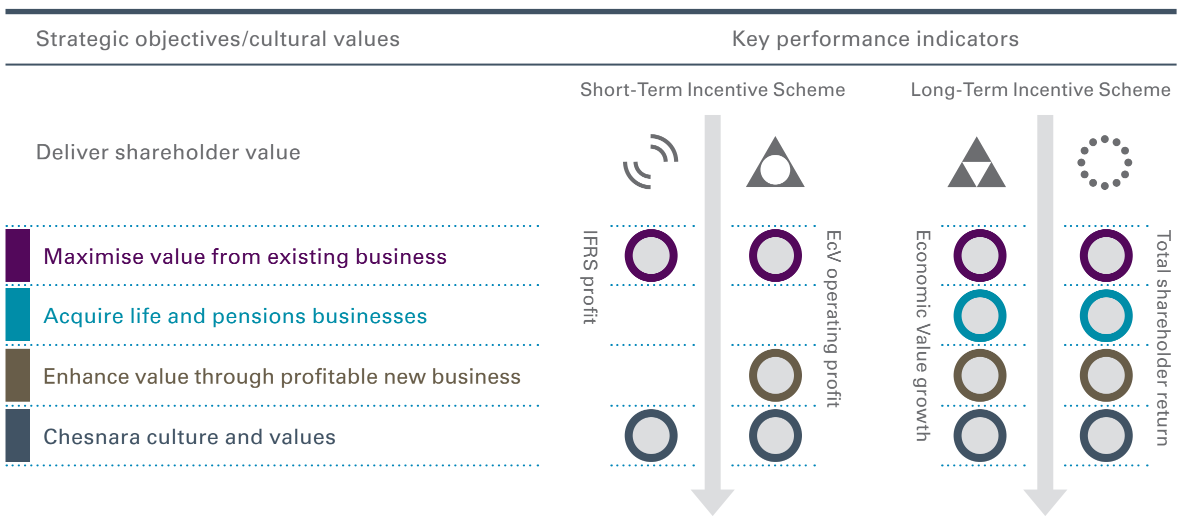
1. Maximise value from existing business;
2. Acquire life and pension business; and
3. Enhance value through profitable new business.

The achievement of these objectives are considered against the culture and risk environment of the company to ensure that rewards do not encourage excessive risk taking or an inappropriate culture to develop.

The schematic below illustrates how the company's KPIs align to its core strategic objectives and, in turn, how those KPIs flow through into the performance measures of the executive's short and long-term incentives schemes. Reading across the chart shows how the KPIs align to Chesnara's core strategic objectives. For example, 'Maximise value from existing business', 'Enhance value through profitable new business' and; 'Acquire life and pensions businesses' will directly impact the Economic Value growth of the group. Likewise progress against all three objectives should have an impact on the Total Shareholder Return to varying degrees.

The diagram demonstrates that the remuneration policy aligns well to all aspects of the group's objectives. For illustration purposes the diagram below shows the KPIs that the committee has most recently considered appropriate for the incentive schemes but as will be seen on pages 73 to 79 the committee may change the KPIs and / or their weighting for future awards. In addition to the KPIs shown, the Short-Term Incentive Scheme includes objectives for the executives covering key deliverables for the year ahead.

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.



REMUNERATION POLICY (CONTINUED)

The implementation of this policy involves:

- paying salaries that reflect individual roles, an individuals' development in that role 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 and clawback provisions, in the STI Scheme (including the deferred share award) and the LTI 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.

The Remuneration Policy table

Executive directors' remuneration

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

Purpose and link to strategy	Operation	Performance measures and maximum
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 – the experience and skills of the jobholder on commencement of the role and their development at the review point – the group'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 or significant changes in the jobholder's responsibilities).	Changes to responsibilities, increased complexity of the organisation, personal and group performance is taken into consideration when deciding whether a salary increase should be awarded.
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 and fuel benefit. 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.

The Remuneration Future Policy table (continued)

Purpose and link to strategy	Operation	Performance measures and maximum
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 can participate in a defined contribution pension scheme with employer contributions being 9.5% of basic salary. If pension limits are reached, the executive may elect to receive the balance of the contribution as cash.	No performance measures attached.
Short-Term Incentive Scheme (STI)		
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 targets and objectives in support of the group's business plan which are 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 three-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 remuneration report. The STI Scheme includes malus and clawback provisions.	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, but are not limited to, costs, IFRS pre-tax profit, EcV operating profit, cash generation, group strategic 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. The committee may substitute, vary or waive the performance measures in accordance with the scheme rules. The maximum award is 100% of basic salary with each participant being assigned a personal maximum to be disclosed in the remuneration report with each award made.
Long-Term Incentive Scheme (LTI)		
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 remuneration report. The LTI Scheme includes malus and clawback provisions.	Vesting is dependent on two weighted performance measures which the committee for 2017 weights equally but may vary the weighting and the Index as it considers appropriate in future years: 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 Higher Yield Index. No payout of this element 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 Economic Value:** this target is commercially sensitive and therefore, not disclosed upfront. 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 up to 100% of basic salary, with each participant being assigned a personal maximum to be disclosed in the remuneration report with each award made.

REMUNERATION POLICY (CONTINUED)

Non-executive directors' remuneration

Purpose and link to strategy	Operation	Performance measures and maximum
Fees & expenses		
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.	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.

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 business plan and 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, but are not limited to, costs, IFRS pre-tax profit, EcV operating profit, cash generation, group 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 EcV) and a comparative measure (TSR). The measures and targets are set by the committee. The maximum potential award for the group EcV measure requires significant outperformance of budgeted targets. The TSR measure uses the FTSE 350 Higher 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 to 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 remuneration report.

The remuneration 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 upfront.

Short-Term Incentive Scheme (STI)

(i) based on a broad range of measures – including group objectives;

(ii) performance measures and their weighting are determined by the committee each year 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) maximum potential award up to 100% of salary with each participant having a personal maximum which is to be disclosed in the remuneration report for each award made;

(iv) award is part cash and part share award deferred for a further 3 years. Currently the intention is to structure the award 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;

(v) unvested awards may be withheld under the terms of the malus provision. Cash awards are subject to a 2 year clawback provision; and

(vi) it is the intention of the committee to make a new award each year.

Long-Term Incentive Scheme (LTI)

(i) a performance share plan;

(ii) uses 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 is at least 3 years;

(v) maximum potential award is up to 100% of salary with each participant having a personal maximum which is to be disclosed in the remuneration report for each award made;

(vi) includes a malus provision and a 2 year clawback provision; and

(vii) it is the intention of the committee to make a new award each year.

Minimum shareholding requirement

In order to align the executive directors' interests with those of shareholders, a minimum shareholding requirement applies 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.

Expenses

In line with the company's Expenses Policy, all directors may receive reimbursement of reasonable expenses incurred in connection with company business and including settling any tax incurred in relation to these.

2. 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 personal performance 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. In line with local regulations the remuneration to employees within the Netherlands does not include any bonus element.
- **Long-term plans:** Only executive directors are currently 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. This may be reviewed as appropriate in the light of growth in the company.
- **Pension:** The level of contribution made by the company to executive directors is the same as that offered to other UK employees.

3. Other

The company currently operates an SAYE in the UK which expires in 2018. 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 policy table 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.

REMUNERATION POLICY (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. Regardless of whether a departing executive is deemed to be a 'good leaver' or 'bad leaver', the committee has discretion to pay a departing executive's legal fees subject to any such payment being made in accordance with the terms of a compromise agreement which waives all claims against the company.

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 (and where deemed to be a bad leaver).	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 (bad leaver).	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.
Under special circumstances: Good Leaver Status whether 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 for the 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. If leaving by reason of redundancy the payment may include statutory redundancy pay.	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. The 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, by exception 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. The 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 or immediately if termination is as a result of not being elected at the AGM.
- There are no compensation terms regardless of the circumstances that may lead to a contract being terminated.

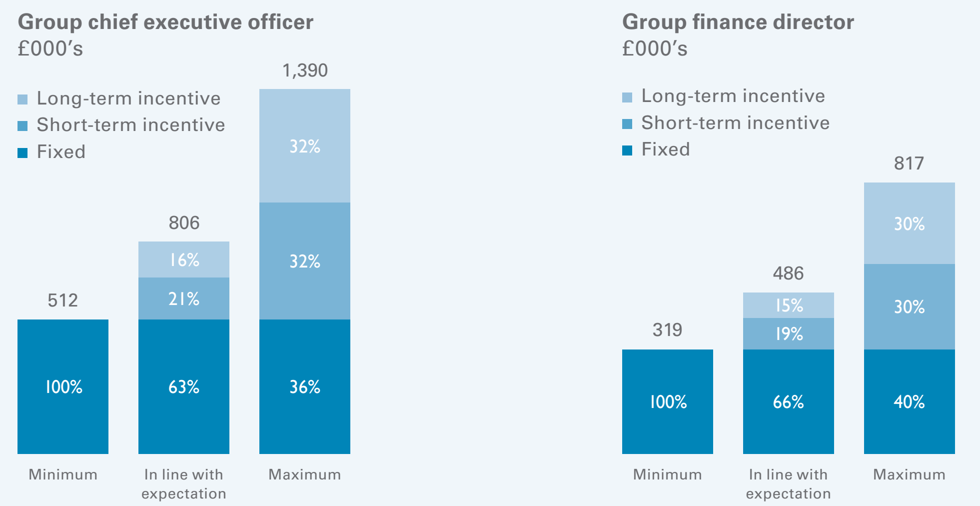
Other directorships

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, variable pay should be no more than 200% of salary. 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 2017 policy applies throughout the period.



In line with expectation performance assumes that the STI and LTI payments are at 37.8% and 29.2% of their maximum respectively for the group chief executive and 34.0% and 26.3% of their maximum for the group finance director. The targets are based on the measures outlined above but are not declared prior to the publication of the accounts for the relevant year as they may be commercially sensitive.

Minimum

The table below analyses the constitution of the minimum remuneration projection for 2018:

Director	Salary and fees £000	Benefits £000	Total fixed pay £000	Total fixed pay £000
Group chief executive	439.1	31.6	41.7	512.4
Group finance director	277.0	16.2	26.3	319.5

The pension figure above is based on 9.5% of gross basic salary.

Statement of shareholder views

Given there is very little change in policy between this and our last remuneration policy the committee has not considered it necessary to consult with shareholders.

AUDIT & RISK COMMITTEE REPORT

2017 has been a busy year, with special attention provided to the completion and integration of the Scildon acquisition and the external audit tender.

Chairman's introduction

I am very pleased to introduce the report on the activities of the Audit and Risk Committee during 2017, which was my first full year as Chairman. There were no changes to the membership of the committee in the year. In addition to the regular activities of the committee we had a number of significant new matters to consider, including a tender process for our external auditors, overseeing the acquisition of Scildon and the inaugural external reporting under Solvency II. Together with the final publication of the new insurance accounting standard, IFRS17, we have been kept very busy.

Full details of the external audit tender are set out on page 82. The process was thorough and considered a number of criteria, including the requirements of the expanded group following the acquisition of Scildon. The committee members were unanimous in the decision to reappoint Deloitte (and to replace EY at Scildon).

The committee wished to ensure that the acquisition of Scildon was properly consolidated in the group accounts and that there are strong controls in place for financial reporting and risk management. We received a number of reports from management supporting this during the year which received appropriate scrutiny and challenge.

The committee oversaw the production of the first public report under Solvency II requirements, the Solvency & Financial Condition Report (published in June 2017); this is an annual report which will fall under the ongoing remit of the committee.

Following the publication of IFRS17 standards, the committee received training on the new standard to ensure common understanding. Project planning commenced at the end of the year and this is expected to be a significant area of focus for the group and the committee during 2018 and 2019.

Risk management is an important part of the Committee's work and we received high quality information regarding the group's risk exposures and the actions taken to manage these risks. Our group risk management system was rolled out to Scildon following acquisition and good progress has been made with embedding our requirements.

The company secretary undertook a questionnaire-based performance evaluation of the committee at the end of the year and I was pleased to note that we are comfortable that we have a good mix of skills and experience, we challenge in an open and constructive manner and have focused on the right areas. We are not complacent however and have identified a number of areas to progress during 2018.

The rest of this report sets out our activities in more detail.

Jane E Dale

Jane Dale
Chairman of the Audit & Risk Committee

28 March 2018

NUMBER OF MEETINGS DURING YEAR: 9

MEMBERS:

Jane Dale	-	Chairman
Mike Evans	-	Member
David Brand	-	Member
Veronica Oak	-	Member

The requirements for the composition of the Audit & Risk Committee are detailed within its terms of reference. The composition of the committee in accordance with the requirements of the UK Corporate Governance Code and with DTR 7.1.1AR and committee member biographies are detailed on pages 50 and 51.

Role of the Audit & Risk Committee

The role of the audit and 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 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 and risk committee are available on our website **www.chesnara.co.uk**

Introduction
The responsibilities of the Chesnara Audit and Risk Committee cover a combination of risk and audit matters relevant to Chesnara. The following report has been structured to reflect this.

Audit responsibilities
This section of the report includes the following:

1. **Activities during 2017:** A summary of the work performed by the Audit and Risk Committee during the year.
2. **External audit:** Further detail of how the committee has overseen various aspects of the external audit during the year, including overseeing a tender process.
3. **Internal audit:** The work performed by the committee in overseeing the internal audit of Chesnara.
4. **Significant issues:** Provides some insight into the significant issues that the committee has considered during the year in relation to the financial statements and how these were addressed.

1. Activities during 2017

As part of its annual planning cycle the committee set its objectives for 2017 at the start of the year, focusing on the larger and more important aspects that were expected to be delivered. This included overseeing the external audit tender, the review and approval of the inaugural Solvency II narrative reports and various tasks associated with the acquisition of Scildon. The committee actively monitored the progress of these objectives throughout the year. A summary of the activities performed is included in the table below.

Financial reporting	– **Solvency II narrative reporting:** Supported the development of, and review of, the inaugural Chesnara group Solvency and Financial Condition Report and Regular Supervisory Report. – **Financial performance:** Monitored and scrutinised the financial performance of the group during the year, covering IFRS, Solvency, EcV and Cash Generation. – **Actuarial assumptions:** Reviewed and challenged the actuarial assumptions underpinning the quarterly financial reporting process. See 'Significant issues' section on page 84 for further detail. – **Annual Report and Accounts:** Reviewed all aspects of the annual report and accounts, including; compliance with accounting standards, accounting policy appropriateness, consideration of financial reporting changes and emerging practice, whether they are fair, balanced and understandable, disclosures surrounding going concern and longer-term viability (including any associated management supporting papers). See 'Significant issues' section on page 84 for further details on certain aspects of the 2017 Annual Report and Accounts. – **Scildon acquisition:** Oversaw the acquisition accounting for Scildon and the post acquisition financial reporting capability and controls. See 'Significant issues' section on page 84 for further detail. – **Interim report:** Reviewed and challenged the Chesnara interim financial report for the half year ended 30 June 2017. – **FRC updates:** Actively monitored key publications issued by the Financial Reporting Council regarding financial reporting matters.
External audit	– **External audit tender:** Oversaw the external audit tender that took place during the year and made a recommendation to the board regarding its outcome. See page 82 for further detail. – **External audit plans:** Reviewed the group-wide plans of the external auditor, including consideration of the key audit risks. See page 84 for further detail. – **External audit quality:** Assessed the quality of the external auditor during the year, including consideration of feedback from management and reports issued by the Financial Reporting Council. – **External audit reporting and feedback:** Reviewed key findings reported by the external auditor on the annual report and accounts, half year report and the Solvency and Financial Condition Report, including financial reporting judgments and control matters. As part of its interactions with the external auditor the committee met with the external auditor without the presence of executive directors. – **External audit independence:** Reviewed the assessment regarding the independence of the external auditor, with specific consideration given to audit fees and also the nature / volume of the services delivered by the external auditor during the year.
Internal audit	– **Review of plans:** Reviewed and approved the plans of the internal audit functions across the group, via interactions with local Audit & Risk Committees. See page 83 for more information. – **Review of internal audit findings:** Received regular updates from local Audit & Risk Committees regarding key findings from divisional internal audits that have been performed during the year. Reviewed the internal audit findings, management responses and tracking of required follow up actions for Chesnara entity internal audits. See page 83 for more information.
Other	– **Feedback from divisional Audit and Risk Committees:** Reviewed and challenged regular feedback provided by the group's divisional Audit and Risk Committees. – **Committee terms of reference:** The committee reviewed its terms of reference during the year and also completed its annual assessment of compliance with its terms of reference. – **Performance evaluation:** The committee conducted a performance evaluation, completed by members and regular attendees regarding various aspects of the committee's performance.

AUDIT & RISK COMMITTEE REPORT (CONTINUED)

2. External audit

External audit tender

Background

During the year the group held a tender for its external audit arrangements for the year ending 31 December 2018. The intention to tender was noted in the 2017 interim financial statements with no shareholder concerns identified or communicated. Deloitte was the incumbent auditor at the point of the tender, having been the auditor of Chesnara since the year ended 31 December 2009. The audit partner, Stephen Williams, had been Chesnara's external audit partner for one year at the point of the tender. In line with regulations, a mandatory tender would have been required ten years from appointment (i.e. for the year ending 31 December 2019). As part of the implementation of a strong and robust governance framework for the group, and in line with a mandatory rotation in Sweden due shortly, coupled with the fact that Scildon's incumbent external auditor was EY, it was deemed appropriate to complete the tender earlier in the cycle.

Process and decision

The audit tender process took place during September to November and was the responsibility of the ARC. This was led throughout by the Chairman, Jane Dale. Through Jane, the ARC had responsibility for initiating and supervising the audit tender process, making the recommendation to the board as to its first and second choice candidates for appointment and providing feedback to the audit firms throughout the process.

The ARC led the design of the tender process and the detailed documentation requested. Jane was the ARC representative meeting the audit firms, with the full committee reviewing the tender documents and attending the tender presentations.

The audit tender was designed to implement a selection process which was efficient, open, transparent, fair and effective. To achieve this, the tender was managed through the following process:

Audit firm selection	Three firms were invited to participate in the process; Deloitte, KPMG and EY. No firms were precluded from consideration, including those firms outside of the 'Big 4'. Due to the complexity of the group, both in terms of geographical spread and the industry specialism, the selected participants were deemed the most suitable to ensure audit quality.
Request for information (RFI) issued	To ensure each firm was able to complete the external audit, each firm was asked to initially provide a response on the following key areas: – Details of challenges of appointment including conflicts, operational challenges and barriers to completing the work; – Detail the proposed audit team, the rationale for those individuals and succession plans for all key service lines; and – The latest relevant Audit Quality Report from the FRC and, if possible, the latest dealings with the Audit Quality Review Team specific to the proposed audit team. An assessment of the responses to the RFI was performed and it was concluded that there were no issues that restricted any of the firms from completing the audit.
Request for proposal (RFP) issued	Following the RFI process, each firm was formally asked to submit a proposal document. The RFP specified that each proposal document needed to include information covering: the team selection; the proposed group audit approach; the approach to transition; thoughts on IFRS 17; how quality is ensured; independence and governance; and fees.
Management meetings and data room access	A data room was created that provided access to key corporate documents relevant to the audit service delivery. This covered organisational, financial, regulatory, risk and governance aspects of the group and its divisions. In addition, each audit firm was provided access to relevant group and divisional management through a structured schedule of meetings.
Proposal and presentation to ARC	Following access to the data room and the completion of management meetings, each audit firm delivered their audit services proposal document. These were subsequently presented to the Audit and Risk Committee.
ARC assessment	With the primary goal of audit quality, the ARC met after the round of tender presentations to conduct a robust debate over the relative strengths and weaknesses of the three teams. The decision drew from the experience of the committee through the presentation process, the quality of the tender documentation and from each feedback provided by key group and divisional management. The overall assessment focused on audit quality, specifically: understanding of the business; people; audit approach; and general Audit firm quality, independence and fees.
ARC recommendation	A recommendation to reappoint Deloitte was made to the board and accepted in November 2017. Throughout the process, Deloitte demonstrated their strength in ensuring continued audit quality across the group and the strength of the team to deliver the audit and support the business through coming changes. Whilst for the group audit mandatory rotation of audit firms is every twenty years, the reappointment means that: – Mandatory rotation is required every ten years in Sweden and so there will be a transition to a new local auditor for Movestic for the year ending 31 December 2019. This appointment will be subject to a separate process that will be determined in due course by the Movestic Audit and Risk Committee. – Mandatory rotation is required every ten years in the Netherlands and so there will be a transition to a new local auditor for Waard for the year ending 31 December 2022. This appointment will be subject to a separate process that will be determined in due course by the Waard Audit and Risk Committee. It was concluded that these matters did not have an impact on the quality of the audit or on its operational effectiveness.

Effectiveness of the audit process
The effectiveness of the external audit process was captured within the external audit tender process that took place in the year. It 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, Stephen Williams, was appointed during 2016 and this will be his second year leading the Chesnara audit;
- 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;
- The report produced by the Financial Reporting Council dated June 2017 entitled 'Deloitte LLP Audit Quality Inspection'. The report was discussed with the auditor although 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. The company is committed to putting its audit out to tender at least every ten years, resulting in the next audit tendering process taking place at the latest during 2027, following the 2026 audit.

Provision of non-audit services and independence
The committee has in place a policy on the engagement of the audit firm for non-audit services. Approval is granted where the service is clearly related to the process of audit services, including regulatory returns. In other cases the approval of the committee is required and documented governance processes are followed.

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 Deloitte, and its associates, for both audit and non-audit services during the year have been provided below, with associated commentary for significant non-audit services.

Audit fees	**2017 £000**	**% proportion**	**2016 £000**	**% proportion**
Audit services	647	61	587	32
Assurance services	413	39	719	39
Non-audit services	-	-	532	29
Total	**1,060**	**100**	**1,838**	**100**

Non-audit services
There were no other non-audit services in 2017 aside from the assurance services as detailed above. Non-audit services in 2016 related to fees associated with the proposed acquisition of Scildon. We do not believe that the level of non-audit service fees compromised the objectivity or independence of the auditors.

In addition €255,500 was paid to Ernst & Young in respect of the audit of Scildon.

3. Internal audit
Chesnara has chosen to adopt a devolved, federal, model for Internal Audit. This means that each subsidiary company is responsible for the oversight of its own Internal Audit work, supervised by each local Audit & Risk Committee. As a result, the group utilises a mix of outsourced and in-house capabilities, adapted to meet the specific needs of each local market. Chesnara believes this model is suitable for a group operating across different territories, in different languages. The Chesnara Audit & Risk Committee maintains oversight of each subsidiary via regular updates from each local Audit & Risk Committee.

Chesnara believes that this model remains appropriate even as the group continues to grow but seeks opportunities to enhance its effectiveness where appropriate; for example we are currently reviewing the Waard and Scildon models to seek operational synergies. The Chesnara Audit & Risk Committee will also be seeking to evaluate the effectiveness of the model during 2018, including ensuring that overall consistency of approach and reporting is achieved.

AUDIT & RISK COMMITTEE REPORT (CONTINUED)

4. Significant issues:

The table below provides information regarding the significant issues that the committee has considered in relation to the preparation of these financial statements:

Area of focus	Reporting issue	Role of the committee	Conclusion/ action taken
Scildon acquisition	The financial statements need to appropriately reflect the acquisition of Scildon. In particular the financial statements need to include: – **Acquisition accounting and associated disclosure:** The acquisition has resulted in the recognition of an intangible asset, representing the value of the in-force insurance policies at the point of acquisition. This asset is being amortised over the expected profit emergence profile of the acquired policies. See note 7 of the IFRS financial statements. – **Risk disclosures:** The risk disclosures in the report and accounts need to be updated to capture any incremental principal risks arising from the Scildon acquisition. See pages 42 to 45. – **Scildon defined benefit scheme:** Scildon introduces a defined benefit pension scheme to the group, which requires accounting treatment and disclosures in compliance with IAS19. Special attention has been required to ensure that the associated reporting disclosures are appropriate. See note 35 of the financial statements.	The committee reviewed and challenged various accounting papers provided by management supporting the accounting for the Scildon acquisition. Regarding risk disclosures, the Audit and Risk Committee was provided with papers highlighting the impact of Scildon on the group's principal risks. For the Scildon pension scheme, the committee has received a number of papers on both the scheme itself and associated accounting disclosure.	The committee concluded that: – the judgments underpinning the acquisition account of Scildon are acceptable; – the risk disclosures appropriately reflect the risks of Scildon; and – the disclosures regarding the Scildon DB scheme are appropriate and articulate the nature of the scheme.
Segmental reporting	The acquisition of Scildon prompted the group to re-consider the operating segments in the IFRS financial statements. This concluded that Scildon will be reported as a separate segment and the previously reported two UK segments of CA and S&P will be condensed into one segment. This reflects the way in which the Chesnara board reviews the results.	The committee reviewed and challenged the paper prepared by management regarding the updated segmentation.	The committee concluded that the updated segment classification is appropriate and complies with the requirements of IFRS 8 'Operating Segments'.
Reporting of alternative performance measures (APMs)	During November 2017 the Financial Reporting Council (FRC) issued the results of its thematic review over the reporting of Alternative Performance Measures. The report emphasised where companies still have work to do. Chesnara has always sought to be clear and transparent regarding the use of alternative performance measures (such as Solvency II), but has considered the findings and has sought to improve disclosures in this regard (see pages 10 to 11).	The committee has read the FRC's thematic review and noted that improved APM disclosures have been provided in this year's report.	The Report and Accounts have a new section (see pages 10 to 11) which defines our KPIs and APMs. This more clearly sign-post to other sections of the report and accounts to provide linkage between the measures and the outcomes. Where appropriate, reconciliations back to the reported IFRS metrics have been introduced.
Business model – key relationships	Draft amendments to 'Guidance on the strategic report' were issued during 2017, which were subject to a consultation period that closed in October. Whilst the new guidelines have not yet been issued in final form, they included a useful reminder of the need for the annual report to include information relating to sources of value that are not recognised in the financial statements.	The committee has reviewed management's summary and response to the key points from the updated guidance. The committee has reviewed the updated disclosures in the annual report.	The Annual Report now includes further information regarding the sense of purpose of the group and provides further information throughout regarding its key stakeholders. In particular, the Chairman's statement on page 15 contains a section dedicated to this matter.
Viability and prospects	The FRC is advising companies to consider developing their reporting on longer term prospects and viability in two stages, encouraging companies to separate prospects from viability and differentiate the time horizons used for those assessments. The FRC also calls for companies to revisit their assessment of the risks and ongoing uncertainties regarding the effects of the EU referendum, making appropriate disclosures to reflect their latest analysis and how this has developed over the year.	The committee has reviewed the disclosures in the financial statements and management's' paper supporting the disclosures that have been made. It was concluded that the disclosures were appropriate.	The group's longer-term viability statement has been refreshed and is included on page 41. We have also provided an update on our current thinking regarding the impact of Brexit on our business (page 15).
Actuarial assumptions	The valuation of insurance liabilities in the financial statements are underpinned by key actuarial assumptions. These are inherently judgmental in nature and as a result require the committee's approval. In particular, the assumptions include the group's approach to valuing liabilities for products with guarantees, which sit within the UK business.	The committee reviewed and approved the actuarial basis of assumptions report underpinning the valuation of insurance liabilities.	The committee concluded that the actuarial assumptions were appropriate. Disclosures over key judgments are included in on pages note 3 and note 31 of the IFRS financial statements. In addition, the external audit report makes reference to certain actuarial judgements (see pages 92 to 97).

Risk responsibilities

This section of the report provides information regarding the risk oversight responsibilities of the Audit and Risk Committee. Overall the committee is responsible for:

- the group's risk management and internal control systems and their effectiveness;
- overseeing the group's risk profile in the context of its current and future strategy;
- discussing and recommending to the board for approval, the group's risk appetite statement, reverse stress testing and scenario stress testing;
- advising the board on proposed changes to the group's risk appetite statement where this is deemed appropriate;
- monitoring risk exposures across the group and advising the board where such exposures do not appear to accord with the group's risk appetite statement;
- reviewing the group's capability to identify and manage emerging and new risk types;
- challenging the regular stress and scenario testing of the group's business;
- determining whether there is a sufficient level of risk mitigation in place;
- overseeing due diligence of a major strategic transaction, including any proposed acquisition or disposal, prior to the board taking a decision to proceed with a view to ensuring that the board is aware of all material risks associated with the transaction;
- considering the adequacy and effectiveness of the technology infrastructure and supporting documentation in the risk management system and framework;
- considering and approving the remit of the risk function and ensuring it has adequate resources and appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards;
- providing qualitative and quantitative advice to the Remuneration Committee on risk weightings to be applied to any performance objectives; and
- considering and recommending to the board for approval, the group's risk related regulatory submissions, including the ORSA.

The table below provides some further information regarding the specific activities that the committee has performed during the year in discharging its risk oversight responsibilities:

Principal risk definition: Reviewed and challenged the group's definition of principal risks for the purpose of reporting and monitoring against these risks, including how they are mitigated through the group's internal control framework. This resulted in an increase in materiality levels to reflect the enlarged group including Scildon.
Risk plan review and sign off: The committee reviewed and approved the group and divisional risk plans and associated resourcing needs. One of the key focus areas of the 2018 plan is to ensure that Scildon is fully integrated into the group's risk management framework.
Quarterly risk reporting: During the year, the committee reviewed the quarterly group and divisional risk reports on the identification, evaluation and management of principal risks across the group, including any emerging risks. As part of this process, it flagged any items of concern or clarification requiring follow up. The quarterly risk reporting included 'in focus' sections as required, including for example the impact of the Scildon acquisition on the group's risk profile as well as various changes in the regulatory and political environment with potential to change the risk profile.
Internal control report: The committee reviewed and approved the annual internal controls assessment report.
Systems of governance review: A review of the effectiveness of the systems of governance review was facilitated by the risk function. This considered a number of areas of the overall system of governance including its completeness, effectiveness, its use and the overall culture. This concluded there were no major areas of concern. Any areas for improvement have been built into the 2018 plans, with suitable priorities attached.
ORSA review: The committee reviewed the 2017 ORSA during the year, and made a formal recommendation to the board to approve it. The ORSA includes the outcome of the group's stress and scenario testing. The stresses that are modelled are reviewed and approved as part of the ORSA planning process, and the results are included in the final ORSA report
Risk appetite: Reviewed and approved developments to the group's risk appetite framework, as the group continues to seek the optimal way to articulate its preferences towards taking, or not taking risks.
Review divisional Audit & Risk Committee progress: Received and challenged updates provided by divisional Audit & Risk Committees.
Continuous solvency monitoring: Reviewed the output from the group's continuous solvency monitoring activities. There were no issues arising from this process during the year.
ORSA Policy: Reviewed and approved the ORSA Policy. The main change arising from the policy was to provide additional clarity over the division of responsibility/activities between the Audit and Risk Committee and board over the ORSA process.
Standard formula assessment: As part its annual cycle, the actuarial function performs an assessment of the appropriateness of the standard formula for the purposes of calculating the group's capital requirements under Solvency II. The work and associated findings was reviewed and challenged by the Audit and Risk Committee.

Jane E Dale

Jane Dale
Chairman of the Audit & Risk Committee

28 March 2018

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 2017. The Corporate Governance Report on pages 53 to 57 forms part of the Directors' Report.

The following information, that has been included by way of a cross reference to other areas of the Annual Report and 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 41 and the 'Risk management' section on pages 42 to 45.

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 24 to 29.

Greenhouse gas reporting
The 'Corporate and social responsibility' section on pages 46 to 47.

Environmental, employee and social community matters
The 'Corporate and social responsibility' section on page 46.

Directors
Full information of the directors who served in 2017 is detailed in the Corporate Governance Report on pages 53 to 57. Detail of the non-executive directors who served as chairmen and members of the board committees of the board are set out in the Corporate Governance Report on pages 53 to 57. 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 62 to 79, which also includes details of directors' interests in shares and share options. The Chairman and 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 are retained at the company's office, and 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 2016 and 31 December 2017 and the period to 28 March 2018.

Director evaluations
During the year, the Chairman evaluated the performance of the directors in one-to-one meetings and the senior independent director evaluated the performance of the Chairman. It was confirmed that each director continued to make effective contributions to their role and the board as a whole.

Director appointments
With regard to the appointment and replacement of directors, the company follows the UK Corporate Governance Code 2016 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. There were no new appointments made in the year.

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 41 to the IFRS Financial Statements 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 2017, the company had 149,885,761 ordinary shares in issue, of which 86,040 were held as treasury shares with a nominal value of £4,302. During the year, the maximum number of treasury shares held was 147,535 with a nominal value £7,377. The number of treasury shares disposed of during the year was 61,495, with a nominal value of £3,075.

In order to retain maximum flexibility, the company proposes to renew the authority granted by ordinary shareholders at the Annual General Meeting in 2018, 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 2017, shareholders approved resolutions to allot shares up to an aggregate nominal value of £4,213,496 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.

Articles of Association
The Company's Articles of Association may only be amended by special resolution of the company at a general meeting of its shareholders.

Conflicts of interest
Procedures are in place to ensure compliance with the directors' conflict of interest duties as set out in the Companies Act 2006. The company has complied with these procedures during the year and the board considers that the procedures operated effectively. During the year, details of any new conflicts or potential conflicts were advised and submitted to the board for consideration, and where appropriate, approved.

Results and dividends
The consolidated statement of comprehensive income for the year ended 31 December 2017, prepared in accordance with International Financial Reporting Standards adopted by the EU and set out on page 98 shows:

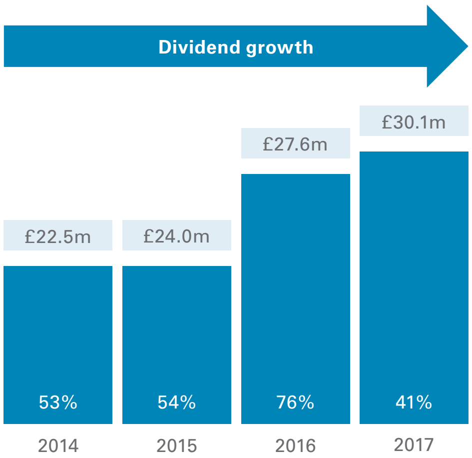
	2017 £000	2016 £000
Profit for year attributable to shareholders	78,434	35,280

An interim dividend of 7.00p per ordinary share was paid by Chesnara on 11 October 2017. The board recommends payment of a final dividend of 13.07p per ordinary share on 23 May 2018 to shareholders on the register at the close of business on 13 April 2018.

The Chesnara dividend policy is directly influenced by two key factors. We recognise that our shares are predominantly held as a source of predictable and sustainable income. Our primary aim is therefore to provide an attractive yield with steady growth where possible.

Our aim to satisfy investor expectations cannot and will not be delivered at the expense of financial security and solvency. As such, dividend capacity is assessed giving full regard to our Group Capital Management policy which currently prohibits dividends to be declared that would result in Chesnara having a solvency ratio below 110%.

Total dividend as a ratio of cash generated



Over the past 4 years, £104m of dividends have been paid at an average annual yield of 6% (based on average annual share prices) representing 53% of the cash generated over the period.

Considerations

Cash generation – Historical and projected cash generation levels need to support any dividend payment although there is no explicit requirement for the current year's cash generation to cover the dividend.

Solvency – Dividends will not be paid if they were to result in a breach in our Capital Management policy which currently sets a minimum dividend paying solvency constraint of 110%.

Acquisition strategy – The Chesnara business model is based upon making future acquisitions and any dividend payments consider the financial requirements to continue to deliver our acquisition strategy.

Investor expectations – In addition to a stable and attractive dividend yield, our investors value predictability and sustainability of earnings. As such, under normal circumstances, 'special dividends' are unlikely.

The board makes dividend decisions with reference to a range of management information, reports and policies including the group ORSA, group business plan, solvency analysis including sensitivities, analysis of historical financial results and the Group Capital Management policy.

DIRECTORS' REPORT (CONTINUED)

Substantial shareholdings

Information provided to the company by major shareholders pursuant to the FCA's Disclosure and Transparency Rules (DTR), is published via a regulatory information service and is available on the company's website. The company had been notified under Rule 5 of the DTR of the following interests in voting rights in its shares as at 31 December 2017 and 21 March 2018:

Name of substantial shareholder	Total number of ordinary shares held	Percentage of the issued share capital as at 31 December 2017
HSBC Global Custody Nominees (UK) Ltd	19,814,044	13.23%
Standard Life Aberdeen plc	18,058,396	12.05%
Invesco Ltd	7,601,155	5.07%
Prudential plc group of companies	6,547,370	4.37%

Subsequent to 31 December 2017 there have been changes to this position and the holdings as at 21 March 2018 are 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 21 March 2018
Standard Life Aberdeen plc	21,365,374	14.26%
HSBC Global Custody Nominees (UK) Ltd	19,814,044	13.23%
Invesco Ltd	7,601,155	5.07%
Prudential plc group of companies	6,547,370	4.37%

Related party transactions and significant contracts

During the year ended 31 December 2017, the company did not have any material transactions or transactions of an unusual nature with, and did not make loans to, related parties in which any director has or had a material interest. There were no significant contracts with substantial shareholders during the year.

Post balance sheet events

There have been no post balance sheet events that either require adjustment to the financial statements or are important in the understanding of the company's current position, financial performance or results.

Charitable donations

Charitable donations made by group companies during the year ended 31 December 2017 were £nil (2016: £nil). No political contributions were made during the year ended 31 December 2017 (2016: £nil).

Employees

The average number of employees during the year was 329 (2016: 201), the material increase reflecting the acquisition of Scildon.

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.

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 to the IFRS Financial Statements. Detailed analysis of relevant risks and other factors is included within the Risk Management section on page 42 to 45, within the Financial Management section on pages 40 to 41 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 or she ought to have taken as a director to make himself or herself 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

The Audit and Risk Committee, in the year, undertook an external audit tender process. The conclusion and recommendation to the board was for the re-appointment of Deloitte LLP as auditor of the company. Full details and results of the audit tender undertaken are in the Audit and Risk Committee Report, on pages 82 to 83. 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 28 March 2018 and signed on its behalf by:

David Rimmington
Group 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.

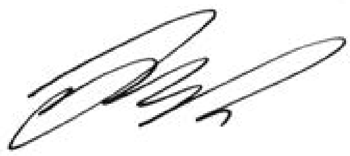
The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies 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.

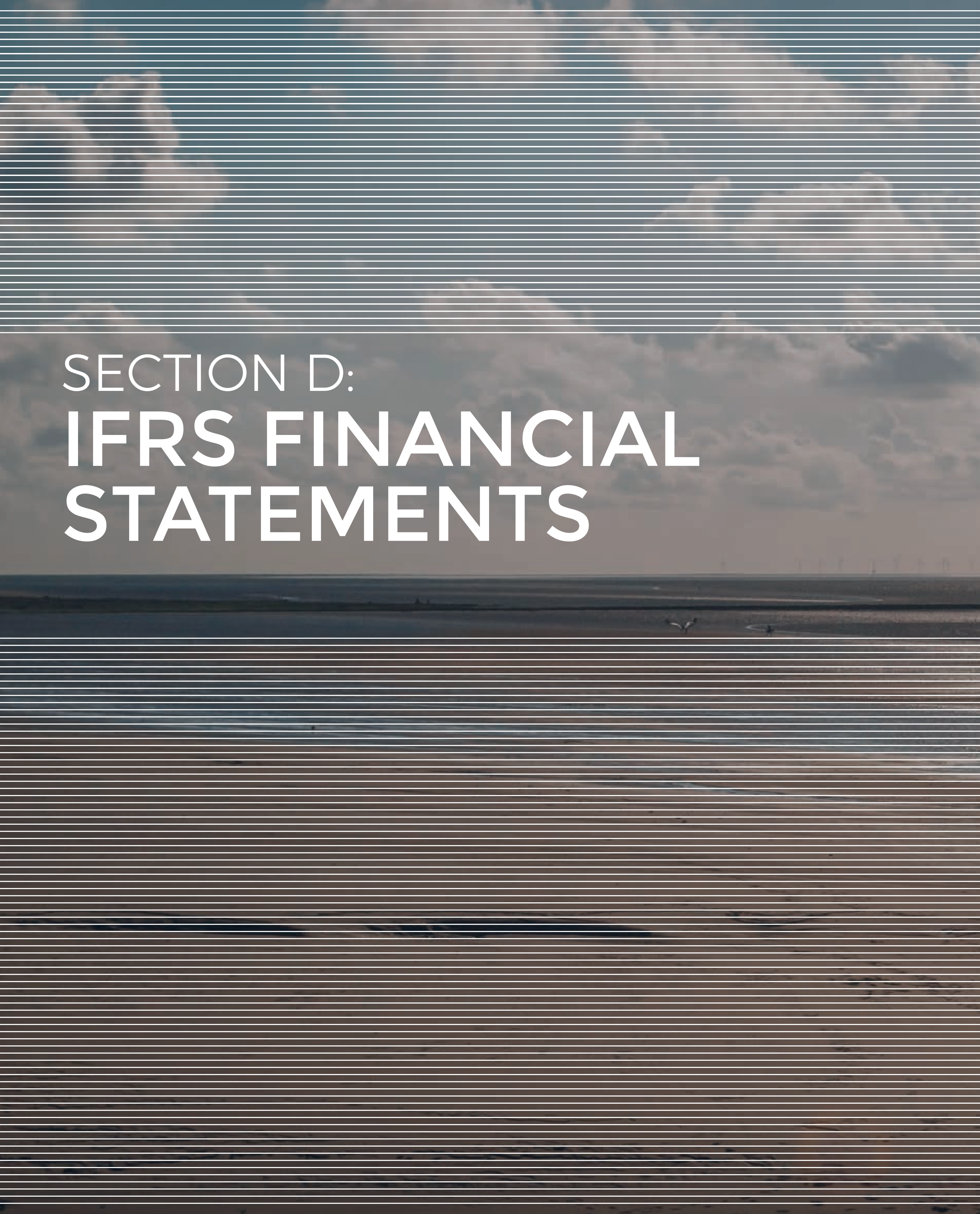


Peter Mason
Chairman

28 March 2018

John Deane
Group Chief Executive Officer

28 March 2018



SECTION D:
IFRS FINANCIAL STATEMENTS

SECTION D • IFRS FINANCIAL STATEMENTS

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The Lancashire coast, England, UK

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CHESNARA PLC

Report on the audit of the financial statements

Opinion

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 2017 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.**

We have audited the financial statements of Chesnara plc (the 'parent company') and its subsidiaries (the 'group') which comprise:

- the consolidated statement of comprehensive income;
- the consolidated and parent company balance sheets;
- the consolidated and parent company statements of changes in equity;
- the consolidated and parent company cash flow statements;
- the statement of accounting policies; and
- the related notes 1 to 52.

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.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: – Accuracy of the Save & Prosper cost of guarantees; – Scildon Liability Adequacy Test; and – Valuation of the Scildon AVIF intangible asset.
Materiality	The materiality that we used in the current year was £11.6m (2016: £8.9m) which was determined on the basis of 3% of adjusted net assets.
Scoping	We focused our group audit scope on the audit work at three UK geographic locations where the group's policies are administered, three overseas geographic locations where the group's policies are also administered, and in Luxemburg where the group undertake certain fund management activities.
Significant changes in our approach	In the prior year, our audit report included two key audit matters which are not included in our report this year: credit risk adjustment and Protection Life AVIF. In relation to the credit risk adjustment , this is no longer identified as a key audit matter, as we have monitored the adjustment since the previous year-end date, and have noted that there had been minimal movement in the key assumptions and in the credit spreads. Furthermore, there have been no significant changes to the key assumptions on the Protection Life AVIF and we noted sufficient headroom on the intangible asset at the year-end date. These matters were therefore no longer considered key audit matters. We have also included two new key audit matters which were not included in the prior year audit report: the Scildon Liability Adequacy Test and the Valuation of the Scildon AVIF intangible asset. These have been included as a result of the acquisition of the Scildon business during the year, and the key audit risks that have been identified in this respect as outlined below.

Conclusions relating to principal risks, going concern and viability statement

Going concern

We have reviewed the directors' statement in note 2c to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the group's and company's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements.

We are required to state whether we have anything material to add or draw attention to in relation to that statement required by Listing Rule 9.8.6R(3) and report if the statement is materially inconsistent with our knowledge obtained in the audit.

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

Principal risks and viability statement

Based solely on reading the directors' statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the directors' assessment of the group's and the company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to:

- the disclosures on pages 43-45 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation on page 56 that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity; or
- the directors' explanation on page 41 as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We are also required to report whether the directors' statement relating to the prospects of the group required by Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Accuracy of Save and Prosper cost of guarantees

Key audit matter description	The assessment of the cost of guarantee reserves for 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. Historically, the residual cost to shareholders arising from the cost of guarantees has fluctuated as a result of movements in bond yields and equity markets with a value of £19.3m at 31 December 2017 (31 December 2016: £35.7m). This movement is mainly due to high asset returns over 2017, which increased policyholder asset shares, and reduce the residual cost to shareholders. The value is determined by a third party actuarial consultant, and the directors compare this valuation against an in-house derived estimate using an approximation model to validate its reasonableness. Due to the highly judgemental nature of this balance, we identified manipulation of this estimate as an area of potential fraud. See note 3e for management's consideration of critical accounting judgment and key sources of estimation and uncertainty, note 31c for disclosure of the calculation methodology and the charge to income for the current and prior year and the Audit & Risk Committee report on page 84.
How the scope of our audit responded to the key audit matter	We assessed the design and implementation of the internal controls in place to monitor and manage the risks associated with the cost of guarantee reserve. We assessed the competence of the actuarial consultant. Such an assessment includes a direct challenge of the actuarial consultant's working papers and a challenge of the historical accuracy of modelling when compared with actual experience. We used actuarial specialists within our audit team to challenge the appropriateness of assumptions input into the model and benchmark against external actuarial data. Sensitivity analysis was also performed to assess potential management bias. We developed an independent expectation of how the assumptions impact the model and challenged management's explanation and analysis to support any variations.
Key observations	Based on the audit procedures performed, we consider that the S&P residual cost of guarantees is not materially misstated.

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

Valuation of the Scildon acquired value in-force ('Scildon AVIF') business intangible

Key audit matter description	Following the acquisition of Scildon in 2017, the group have recorded an AVIF intangible asset on the group balance sheet, reflecting the capitalised future profit in the Scildon life insurance business. There is significant judgement involved in the initial valuation of the AVIF, as well as in the discount rate used in the calculation. Management is required to assess the impairment of the Scildon AVIF intangible balance at least annually, which also involves significant judgement. See note 3a for management's consideration of significant accounting judgements. The accounting policy adopted by the Group is documented within note 2(o) to the financial statements and the acquired in-force business intangible is disclosed in note 20.
How the scope of our audit responded to the key audit matter	We assessed the design and implementation of the internal controls in place to monitor and manage the risks associated with the capitalisation of the AVIF intangible. We constructed an independent discount rate and compared this to the discount rate used by management. We interrogated the policy cash flows which form the basis of the AVIF calculation through a combination of data analytics and tests of controls, to gain assurance over their completeness and accuracy. We have also assessed the reasonableness of the valuation adjustments made to the base VIF. We have challenged the amortisation profile produced by management for the future run off of the Scildon book.
Key observations	Based on the audit procedures performed, we consider the assumptions in the base VIF, and the calculation and magnitude of the adjustments thereof, and the resultant AVIF to be reasonable. We conclude that the discount rate used and amortisation profile are appropriate.

Scildon reserving adjustment

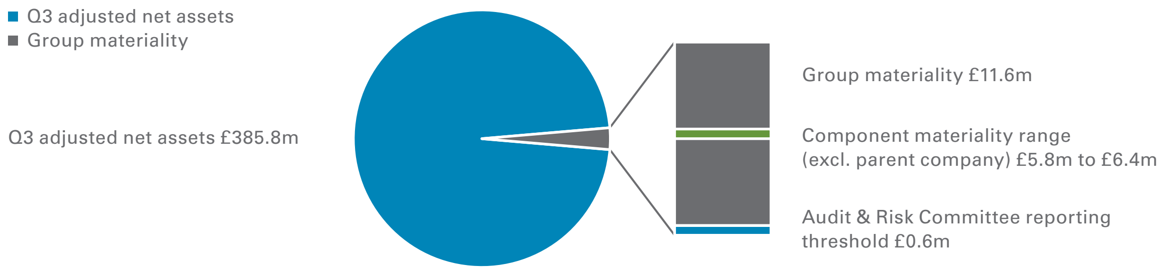
Key audit matter description	Scildon measures the majority of its life insurance contract liabilities using historical market rates of interest, along with a number of other parameters and assumptions. IFRS 4 requires an insurer, at the end of each reporting period, to assess whether its recognised insurance liabilities are adequate, using current estimates of future cash flows (the 'Liability adequacy test' or 'LAT'). Given Scildon's accounting policy makes use of historical market interest rates, there is a heightened risk that its insurance liabilities are not adequate. We therefore considered the liability adequacy test to be a key audit matter, specifically in relation to the mortality, lapse and expense assumptions which feed into this test, given that the insurance liabilities are most sensitive to these factors. The accounting policy adopted by the group is documented within Note 2h iv to the financial statements.
How the scope of our audit responded to the key audit matter	The following specific procedures have been performed: – Evaluation of the design and implementation of the key controls over the setting of the assumptions feeding in to the LAT; – Performing analytical checks on policy cash flows to identify outliers and movements compared to the prior period, which were then investigated; – For a sample of policies, ran the policy cash flows through a model to test that the calculations within management's model are accurate; and – Assessed the results of the experience investigations carried out by management to determine whether they provide support for the assumptions.
Key observations	Based on the audit procedures performed, we found that the Liability Adequacy Test performed by management was reasonable, supporting the adequacy of Scildon's insurance contract liabilities.

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.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
Materiality	£11.6m (2016: £8.6m)	£9.7m (2016: £7.7m)
Basis for determining materiality	3% of adjusted Q3 net assets We use 90% of the benchmark to determine materiality due to the level of inherent volatility in equity prices in the net asset amount so that materiality does not exceed 3% of the year end net asset figure.	
Rationale for the benchmark applied	In our judgement we believe that a net assets measure is more closely aligned to the objectives of capital solvency and efficiency, dividend payments and ultimately cash generation that is relevant for this business model. This represents a stable long-term measure of value in a business which has a significant closed insurance book.	



Excluding the parent company, the component materiality levels set by the group auditor range from £5.8m to £6.4m (2016: £4.3m to £5.6m). The movement in range in the year arises due to foreign exchange movements impacting the re-translated group balance sheet.

We agreed with the Audit & Risk Committee that we would report to the committee all audit differences in excess of £578,000 (2016: £427,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. The change in the reporting threshold has been made following our reassessment of what matters require communicating. 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 was scoped by obtaining an understanding of the group and its environment, including group-wide controls, and assessing the risks of material misstatement at the group level.

Based on this assessment, we focused our group audit scope primarily on the audit work at seven (2016: five) geographic locations where the group's policies are administered. Three (2016: three) relate to Countrywide Assured plc and are in the United Kingdom, and the remaining four (2016: two) locations are in the Netherlands and Sweden and relate to Waard Leven, Hollands Welvaren Leven, Waard Schade, Movestic Livförsäkring AB, Movestic Fund Management S.A., and Scildon. All components were subject to a full scope audit.

The group audit team performed the audit work directly at three of the seven locations. The remaining four locations involved the use of component audit teams, and included a programme of planned visits that has been designed so that the senior statutory auditor and a senior member of the group audit team visited each of the locations at least once in the financial year, except for Luxemburg which was not considered to be material for group reporting purposes.

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

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report & accounts, other than the financial statements and our auditor's report thereon.

We have nothing to report in respect of these matters.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

- Fair, balanced and understandable – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's position and performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- Audit & Risk Committee reporting – the section describing the work of the Audit & Risk Committee does not appropriately address matters communicated by us to the Audit & Risk Committee; or
- Directors' statement of compliance with the UK Corporate Governance Code – the parts of the directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Responsibilities of directors

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, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

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

Use of our report

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.

Report on other legal and regulatory requirements

Opinions 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.

In our opinion, based on the work undertaken in the course of the audit:
– 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; and
– the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the group and the parent company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

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.

We have nothing to report arising from these matters.

Other matters

Auditor tenure
Following the recommendation of the Audit & Risk Committee, we were appointed by group's board with effect from 1 October 2009 to audit the financial statements for the year ending 31 December 2009 and subsequent financial periods. Following a competitive tender process, we were reappointed as auditor of the company for the period ending 31 December 2018 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is 9 years, covering the years ending 2009 to 2017.

Consistency of the audit report with the additional report to the audit committee
Our audit opinion is consistent with the additional report to the Audit & Risk Committee we are required to provide in accordance with ISAs (UK).

Stephen Williams FCA (Senior statutory auditor)
for and on behalf of Deloitte LLP
Statutory Auditor
Manchester, United Kingdom
28 March 2018

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December	Note	2017 £000	2016 £000
Insurance premium revenue		231,515	109,450
Insurance premium ceded to reinsurers		(54,191)	(44,900)
Net insurance premium revenue		**177,324**	**64,550**
Fee and commission income	**9**	113,848	72,932
Net investment return	**10**	531,817	515,681
Total revenue net of reinsurance payable		**822,989**	**653,163**
Other operating income	**11**	17,242	17,614
Total income net of investment return		**840,231**	**670,777**
Insurance contract claims and benefits incurred			
Claims and benefits paid to insurance contract holders	**12**	(465,729)	(346,117)
Net decrease in insurance contract provisions	**12**	51,033	11,392
Reinsurers' share of claims and benefits	**12**	49,449	62,364
Net insurance contract claims and benefits		(365,247)	(272,361)
Change in investment contract liabilities	**13**	(293,603)	(274,724)
Reinsurers' share of investment contract liabilities	**13**	3,681	5,617
Net change in investment contract liabilities		(289,922)	(269,107)
Fees, commission and other acquisition costs	**14**	(24,405)	(23,838)
Administrative expenses	**15**	(70,269)	(46,615)
Other operating expenses			
Charge for amortisation of acquired value of in-force business	**16**	(13,271)	(10,419)
Charge for amortisation of acquired value of customer relationships	**16**	(101)	(236)
Other	**16**	(4,239)	(4,394)
Total expenses net of change in insurance contract provisions and investment contract liabilities		**(767,454)**	**(626,970)**
Total income less expenses		**72,777**	**43,807**
Share of profit of associate	**24**	949	150
Profit recognised on business combination	**7**	20,319	–
Financing costs	**17**	(4,443)	(3,272)
Profit before income taxes	**8**	**89,602**	**40,685**
Income tax expense	**18**	(11,168)	(5,405)
Profit for the year	**8**	**78,434**	**35,280**
Items that will not be reclassified to profit and loss:			
Foreign exchange translation differences arising on the revaluation of foreign operations	**4**	8,274	(20,114)
Revaluation of pension obligations	**35**	124	–
Revaluation of investment property		90	–
Total comprehensive income for the year		**86,922**	**55,394**
Basic earnings per share (based on profit for the year)	**47**	52.38p	27.67p
Diluted earnings per share (based on profit for the year)	**47**	52.13p	27.56p

The notes and information on pages 104 to 173 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

31 December	Note	2017 £000	2016 £000
Assets			
Intangible assets			
Deferred acquisition costs	19	61,858	48,318
Acquired value of in-force business	20	119,039	62,943
Acquired value of customer relationships		641	736
Goodwill	21	806	–
Software assets	22	6,358	6,560
Property and equipment	23	4,327	519
Investment in associates	24	6,407	5,433
Investment properties		1,199	245
Reinsurers' share of insurance contract provisions	31	233,154	254,859
Amounts deposited with reinsurers	32	38,776	37,437
Financial assets			
Equity securities at fair value through income	25	512,724	485,165
Holdings in collective investment schemes at fair value through income	25	5,202,772	4,104,602
Debt securities at fair value through income	25	1,628,817	474,091
Policyholders' funds held by the group	25	265,729	229,397
Mortgage loan portfolio	25/26	48,106	54,756
Insurance and other receivables	25/27	59,448	39,646
Prepayments	25	7,325	5,271
Derivative financial instruments	25/28	1,682	2,773
Total financial assets		7,726,603	5,395,701
Reinsurers' share of accrued policyholder claims	38	25,888	19,307
Income taxes		7,681	3,352
Cash and cash equivalents	29	210,647	260,353
Total assets		**8,443,384**	**6,095,763**
Liabilities			
Insurance contract provisions	31	3,962,279	2,242,446
Other provisions		1,098	823
Financial liabilities			
Investment contracts at fair value through income	32	3,420,273	3,028,269
Liabilities relating to policyholders' funds held by the group	33	265,729	229,397
Borrowings	34	129,202	86,843
Derivative financial instruments	28	22,494	1,348
Total financial liabilities		3,837,698	3,345,857
Deferred tax liabilities	36	22,794	5,420
Reinsurance payables	37	11,406	6,899
Payables related to direct insurance and investment contracts	38	97,163	61,416
Deferred income	39	4,701	5,438
Income taxes		8,514	8,624
Other payables	40	44,984	23,657
Bank overdrafts	29	1,091	1,622
Total liabilities		**7,991,728**	**5,702,202**
Net assets	8	**451,656**	**393,561**
Shareholders' equity			
Share capital	41	43,766	43,766
Share premium	41	141,983	142,058
Treasury shares	42	(98)	(161)
Other reserves	43	27,664	19,300
Retained earnings	44	238,341	188,598
Total shareholders' equity		**451,656**	**393,561**

The notes and information on pages 104 to 173 form part of these financial statements.

Approved by the board of directors and authorised for issue on 28 March 2018 and signed on its behalf by:

Peter Mason
Chairman

John Deane
Chief executive officer

Company Number: 04947166

COMPANY BALANCE SHEET

31 December	Note	2017 £000	2016 £000
Assets			
Non-current assets			
Financial assets			
Investments in subsidiaries	**25**	354,720	249,234
Deferred tax asset		338	202
Total non-current assets		**355,058**	**249,436**
Current assets			
Financial assets			
Holdings in collective investment schemes at fair value through income	**25**	29,091	72,939
Receivables and prepayments		3,060	3,007
Income taxes		3,032	2,279
Cash and cash equivalents	**29**	11,867	44,183
Total current assets		**47,050**	**122,408**
Total assets		**402,108**	**371,844**
Current liabilities			
Borrowings	**34**	22,029	52,697
Other payables	**40**	4,651	4,785
Total current liabilities		**26,680**	**57,482**
Non-current liabilities			
Borrowings	**34**	67,428	–
Total non-current liabilities		**67,428**	**–**
Total liabilities		**94,108**	**57,482**
Net assets		**308,000**	**314,362**
Shareholders' equity			
Share capital	**41**	7,494	7,494
Share premium	**41**	141,983	142,058
Treasury shares	**42**	(98)	(161)
Other reserves	**43**	50	50
Retained earnings	**44**	158,571	164,921
Total shareholders' equity		**308,000**	**314,362**

The notes and information on pages 104 to 173 form part of these financial statements.

The profit for the financial year of the parent company was £22.5m (2016: £22.3m).

The financial statements of Chesnara plc (registered number 4947166) were approved by the board of directors and authorised for issue on 28 March 2018 and signed on its behalf by:

Peter Mason
Chairman

John Deane
Chief executive officer

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December	Note	2017 £000	2016 £000
Profit for the year		**78,434**	**35,280**
Adjustments for:			
Depreciation of property and equipment	**23**	698	173
Amortisation of deferred acquisition costs	**19**	14,506	12,162
Amortisation of acquired value of in-force business	**20**	13,271	10,408
Amortisation of acquired value of customer relationships		101	172
Amortisation of software assets	**22**	2,218	794
Share based payment		(159)	623
Tax paid		11,209	5,405
Interest receivable		4,785	(20,882)
Dividends receivable		(4,619)	(30,209)
Interest expense	**17**	4,443	3,272
Fair value gains on financial assets		(210,706)	(205,870)
Profit arising on business combination	**7**	(20,319)	–
Share of profit of associate	**24**	(949)	(150)
Increase in intangible assets related to insurance and investment contracts		(28,634)	(16,448)
Interest received		4,560	20,281
Dividends received		4,336	29,446
Changes in operating assets and liabilities (excluding the effect of acquisitions)	**35**	124	–
Changes in operating assets and liabilities:			
Increase in financial assets		(145,613)	(283,944)
Decrease in reinsurers' share of insurance contract provisions		17,074	34,177
Increase in amounts deposited with reinsurers		(1,339)	(3,496)
Decrease in insurance and other receivables		11,317	10,294
Decrease in prepayments		12,722	1,795
Decrease in insurance contract provisions		(91,110)	(16,530)
Decrease/(increase) in investment contract liabilities		414,014	362,641
(Increase)/decrease in provisions		272	(1,306)
Increase/(decrease) in reinsurance payables		4,424	(3,660)
Increase/(decrease) in payables related to direct insurance and investment contracts		2,432	(2,114)
(Decrease)/increase in other payables		(935)	2,808
Net cash generated from/(utilised by) operations		**86,987**	**(54,878)**
Income tax paid		(27,480)	(4,709)
Net cash generated from/(utilised by) operating activities		**59,507**	**(59,587)**
Cash flows from investing activities			
Business combinations	**7**	(117,993)	–
Development of software		(928)	(3,502)
Disposal/(purchases) of property and equipment		(314)	948
Net cash utilised by investing activities		**(119,235)**	**(2,554)**
Cash flows from financing activities			
(Loss)/Proceeds from issue of share capital		(75)	66,708
Net proceeds from borrowings		42,022	4,268
Sale of treasury shares		63	–
Dividends paid		(29,484)	(24,181)
Interest paid		(4,266)	(3,095)
Net cash generated from financing activities		**8,260**	**43,700**
Net decrease in net cash and cash equivalents		**(51,468)**	**(18,441)**
Net cash and cash equivalents at beginning of year		258,731	259,911
Effect of exchange rate changes on net cash and cash equivalents		2,293	17,261
Net cash and cash equivalents at end of the year	**29**	**209,556**	**258,731**

Note: Net cash and cash equivalents includes overdrafts.

The notes and information on pages 104 to 173 form part of these financial statements.

COMPANY STATEMENT OF CASH FLOWS

Year ended 31 December	Note	2017 £000	2016 £000
Profit for the year		**22,465**	**22,311**
Adjustments for:			
Tax recovery		(1,860)	(1,498)
Interest receivable		1,683	1,641
Share based payment		669	478
Dividends receivable		(32,701)	(30,500)
Increase in financial assets		43,848	(67,927)
Changes in operating assets and liabilities:			
(Increase)/decrease in loans and receivables		(213)	621
(Increase)/decrease in prepayments		24	(55)
Increase in other payables		(23)	3,351
Net cash generated from/(utilised by) operating activities		**33,892**	**(71,578)**
Income tax received		996	900
Net cash generated from/(utilised by) operating activities		**34,888**	**(70,678)**
Cash flows from investing activities			
Business combinations		(105,486)	–
Dividends received from subsidiary company		32,701	30,500
Net cash (utilised by)/generated from investing activities		**(72,785)**	**30,500**
Cash flows from financing activities			
Net proceeds from the issue of share capital		–	66,708
Redemption of redeemable preference share		(75)	–
Sale of treasury shares		63	–
Net proceeds from borrowings		36,760	–
Dividends paid		(29,484)	(24,181)
Interest paid		(1,683)	(1,464)
Net cash generated from financing activities		**5,581**	**41,063**
Net (decreases)/increase in net cash and cash equivalents		**(32,316)**	**885**
Net cash and cash equivalents at beginning of year		44,183	43,298
Net cash and cash equivalents at end of the year	**29**	**11,867**	**44,183**

Note: Net cash and cash equivalents includes overdrafts.

The notes and information on pages 104 to 173 form part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2017

	Note	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2017		**43,766**	**142,058**	**19,300**	**(161)**	**188,598**	**393,561**
Profit for the year		–	–	–	–	78,434	78,434
Dividends paid		–	–	–	–	(29,484)	(29,484)
Foreign exchange translation differences	4	–	–	8,274	–	–	8,274
Revaluation of pension obligations		–	–	–	–	124	124
Revaluation of investment property		–	–	90	–	–	90
Share based payment		–	–	–	–	669	669
Sale of treasury shares		–	(75)	–	63	–	(12)
Equity shareholders' funds at 31 December 2017		**43,766**	**141,983**	**27,664**	**(98)**	**238,341**	**451,656**

Year ended 31 December 2016

	Note	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2016		**42,600**	**76,516**	**(814)**	**(161)**	**177,021**	**295,162**
Profit for the year		–	–	–	–	35,280	35,280
Dividends paid		–	–	–	–	(24,181)	(24,181)
Foreign exchange translation differences	4	–	–	20,114	–	–	20,114
Share based payment		–	–	–	–	478	478
Issue of new shares		1,166	65,542	–	–	–	66,708
Equity shareholders' funds at 31 December 2016		**43,766**	**142,058**	**19,300**	**(161)**	**188,598**	**393,561**

The notes and information on pages 104 to 173 form part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2017

	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2017	**7,494**	**142,058**	**50**	**(161)**	**164,921**	**314,362**
Profit for the year	–	–	–	–	22,465	22,465
Dividends paid	–	–	–	–	(29,484)	(29,484)
Share based payment	–	–	–	–	669	669
Sale of treasury shares	–	(75)	–	63	–	(12)
Equity shareholders' funds at 31 December 2017	**7,494**	**141,983**	**50**	**(98)**	**158,571**	**308,000**

Year ended 31 December 2016

	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2016	**6,328**	**76,516**	**50**	**(161)**	**166,313**	**249,046**
Profit for the year	–	–	–	–	22,311	22,311
Dividends paid	–	–	–	–	(24,181)	(24,181)
Share based payment	–	–	–	–	478	478
Issue of new shares	1,166	65,542	–	–	–	66,708
Equity shareholders' funds at 31 December 2016	**7,494**	**142,058**	**50**	**(161)**	**164,921**	**314,362**

The notes and information on pages 104 to 173 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 in the United Kingdom and registered in England and Wales. The company is limited by shares and has a primary listing on the London Stock Exchange. The address of the registered office is 2nd Floor, Building 4, West Strand Business Park, West Strand Road, Preston, England, PR1 8UY, UK.

The company and its subsidiaries, together forming the group, comprise UK, Swedish and Dutch life and pensions businesses.

The UK business is represented by the CA segment, as described in note 8. Its activities are performed entirely in the UK, where it underwrites 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. It is 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 8, 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.

The Dutch business, which comprises the Waard Group and Scildon segments, is described in note 8. These represent the group's Dutch life and general insurance businesses. The Waard Group consists of three insurance companies Waard Leven N.V., Hollands Welvaren Leven N.V. and Waard Schade N.V., and a servicing company, Tadas Verzekering. During the year, the book of policies held within Hollands Welvaren Leven N.V. was successfully integrated into Waard Leven via a Part VII transfer. The Waard Group's policy base is predominantly made up of term life policies, although also includes unit-linked policies and some non-life policies, covering risks such as occupational disability and unemployment. The Scildon segment represents the Group's latest Dutch life insurance business, which was acquired on 5 April 2017. Scildon's policy base is predominantly made up of individual protection and savings contracts. It is open to new business and sells protection, individual savings and group pension contracts via a broker-led distribution model.

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 28 March 2018.

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 business, the Swedish business, which comprises the Movestic segment and the Dutch business which comprises the Waard Group and Scildon.

(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.

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
IFRIC 22	Foreign currency transactions and advance consideration
Amendments to IFRS 10, IFRS 12 and IAS 28 (Dec 2014)	Investment entities: applying the consolidation exception
Amendments to IFRS 10 and IAS 28 (Sept 2014)	Sale or contribution of assets between an investor and its associate or joint venture
IFRS 16	Leases
IFRS 9	Financial instruments
IFRS 17	Insurance contracts

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. An exemption has been granted to life insurers to delay the implementation of IFRS 9 until the earlier of the introduction of IFRS 17 (insurance contracts) and 2021.
- IFRS 16 is effective for annual periods beginning on or after 1 January 2019 and the impact on the financial statements of the group will be assessed in due course.
- IFRS 17 (insurance contracts) was issued in May 2017 and will be effective from 2021. The company has commenced its IFRS 17 implementation programme, but has yet to quantify the financial impact of its adoption.

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 44.

(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 company balance sheet is also presented in this manner.

The preparation of financial statements in conformity with IFRSs requires management to make judgments, 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 judgments 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. Judgments 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.

In accordance with IFRS 4, Insurance Contracts, on adoption of IFRS the group applied existing accounting practices for insurance and participating investment contracts, modified as appropriate to comply with the IFRS framework and applicable standards, introducing changes only where they provide more reliable and relevant information.

(d) Business combinations

The group uses the purchase method of accounting 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 year 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 year, 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 year 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 business, 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 the S&P component of the CA segment, 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 the original CA book, all such contracts are wholly reinsured with ReAssure Limited (ReAssure - previously Guardian Assurance plc), 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; or

(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.

(h) Insurance contracts

There are fundamental differences between the nature of the insurance contracts subsisting in the UK, Swedish and Dutch businesses, including inter alia contract longevity: the related product characteristics are set out for the separate UK, Swedish and Dutch 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:

(i) Premiums

Across all four businesses, 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.

In Sweden 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) Claims and benefits

Claims are accounted for in the accounting year in which they are due or notified. Surrenders are accounted for in the accounting year 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.

Swedish non-life 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.

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 31.

(iii) Acquisition costs

In the UK, Swedish and Scildon segments, 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

In the UK and Dutch businesses, 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 basis in order to comply with the reporting requirements of the Prudential Sourcebook for Insurers and the Dutch Central Bank respectively. 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 or mortality improvement has been made.

In respect of CA (S&P book), 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 (original book) for those classes of non-linked and unit-linked business where policyholders participate in profits the liability is wholly reassured to ReAssure. 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.

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.

In Sweden, 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(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 business, 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.

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 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.

(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 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. The 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(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 to 5 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 12 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 four different categories of financial assets are used: 'financial assets at fair value through income', 'mortgage loan portfolio', 'prepayments' 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 the Waard mortgage loan portfolio and 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 at 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 insurance and other 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.

The mortgage loan portfolio held by the Waard Group is stated at amortised cost less impairment losses and incorporates the effective interest rate calculation method.

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.

(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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2 Significant accounting policies (continued)

(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.

Dutch business (Waard)

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.

Dutch business (Scildon)

Scildon has a defined benefit plan. The pension scheme is administered by Stichting Pensionfonds Legal & General Nederland. The company has agreed to contribute to the premium for the unconditional part of the pension. Part of the plan consists of a defined contribution scheme. The company pays a contribution to the scheme and subsequently has no further financial obligations with respect to this part of the scheme. Further disclosure can be found in note 35. Net liability for defined benefit obligations on page 156.

(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-based payments

The value of employee share options and other equity settled share based payments is calculated at fair value at the grant date using appropriate and recognised option pricing models. Vesting conditions, which comprise service conditions and performance conditions, other than those based upon market conditions, are not taken into account when estimating the fair value of such awards but are taken into account by adjusting the number of equity instruments included in the ultimate measurement of the transaction amount. The value of the awards is recognised as an expense on a systematic basis over the period during which the employment services are provided. Where an award of options is cancelled by an employee, the full value of the award (less any value previously recognised) is recognised at the cancellation date.

(dd) 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.

(ee) 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.

(ff) 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 judgments 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 judgments in applying the group's accounting policies. Such estimates and judgments 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 judgments are made, are set out below. Each item identifies the business segments, as described in note 8, to which it is relevant.

Critical accounting judgments

(a) Classification of long-term contracts (CA, Movestic, Waard Group and Scildon)

The group has exercised judgment 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 judgment 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. Refer to note 2(g) – Product Classification on page 106.

(b) 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. Refer to note 2(bb) – Employee Benefits on page 112.

(c) Accounting for pension plans (Scildon)

Scildon has a defined benefit plan. The pension scheme is an indexed average pay scheme with a pension of 1.7% per year of service. Indexation is conditional since 1 January 2013. The pension scheme is administered by Stichting Pensionfonds Legal & General Nederland. The company has agreed to contribute to the premium for the unconditional part of the pension. Apart from the obligations which may arise from the collective agreement provisions, the company is not obliged to make additional contributions to the claims brought under the pension fund. The company is not entitled to refunds or discounts. Part of the plan consists a defined contribution scheme. The company pays a contribution to the scheme and subsequently has no further financial obligations with respect to this part of the scheme. This contribution is recognised as an expense when paid. Refer to note 2(bb) – Employee Benefits on page 112.

Key sources of estimation and uncertainty

(a) Acquired value of in-force business (CA, Movestic, Waard Group and Scildon)

The group applies accounting estimates and judgments 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. Refer to accounting policy note 2(o) on page 109 and note 20 on page 138.

The acquired value of in-force business is 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 judgment. In particular the value is sensitive to the rate at which future cash flows are discounted and to the rates of return on invested assets, based on applying a range of discount rates, which have been determined with reference to our review of the current market assessment of the true value of money and the risks specific to the asset for which the cash flows have not been adjusted. The rates used for the purpose of the impairment testing were 4%, 6%, 8%, 10% and 12%.

From the results of the most recent impairment tests, we can conclude that we have sufficient headroom between the AVIF carrying values and the underlying value of in-force business, to make the sensitivity with regard to discount rate movements irrelevant for the foreseeable future.

As at 31 December 2017, the carrying value of acquired in-force business, net of amortisation, was £11.2m in respect of CA (as at 31 December 2016: £16.9m), £4.0m in respect of S&P (31 December 2016: £4.5m), £32.8m in respect of Movestic (as at 31 December 2016: £36.0m), £5.0m in respect of Waard Group (31 December 2016: £5.5m) and £66.1m in respect of Scildon.

(b) Deferred acquisition costs and deferred income – investment contracts (CA, Movestic and Scildon)

The group applies judgment 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. Judgment 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. Refer to accounting policy 2(k) on page 108 and note 19 on page 137.

As at 31 December 2017, the carrying values of deferred acquisition costs, net of amortisation, and of deferred income, in respect of CA, were £2.5m and £4.7m respectively (as at 31 December 2016: £2.9m and £5.4m 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 2017, the carrying values of deferred acquisition costs, net of amortisation, in respect of Movestic, was £55.2m (as at 31 December 2016: £45.4m). An increase in the length of the amortisation period by one year would have increased profit before tax for the year ended 31 December 2017 by £2.9m and shareholders' equity as at 31 December 2017 by £2.3m.

As at 31 December 2017, the carrying values of deferred acquisition costs, net of amortisation, in respect of Scildon, was £12.3m. An increase in the length of the amortisation period by one year would have increased profit before tax for the year ended 31 December 2017 by £0.4m and shareholders' equity as at 31 December 2017 by £0.3m.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

3 Key sources of estimation and uncertainty (continued)

(c) Estimates of future benefits payments arising from long-term insurance contracts (CA and Scildon)

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.

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 31 on page 148.

(d) 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 CA means that future expenses are relatively predictable and hence assumptions made for actuarial reserving purposes are not subject to material levels of judgment. 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 sensitivity in respect of a 10% increase maintenance expenses is quantified in note 31 on page 153.

(e) 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 2017, the carrying value of insurance contract liabilities which contain S&P discretionary participation features was £229.4m (31 December 2016: £297.5m).

(f) 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 2017, the carrying value of the insurance claim reserves, gross of reinsurance, was £81.5m (as at 31 December 2016: £81.6m). The key sensitivities in respect of insurance claim reserves are considered in note 31 on page 153.

(g) 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 2017, such claims ceded to reinsurers and reflected on the balance sheet were £54.1m (31 December 2016: £54.9m). The application of a 10% bad debt provision on the reinsurance balance would reduce 2017 profit before tax by £5.4m and shareholders' equity by £4.2m.

4 Exchange rates

The group's principal overseas operations during the year were located within Sweden and the Netherlands.

The results and cash flows of these operations have been translated into Sterling at an average rate for the year of £1 = SEK 11.00 (2016: £1 = SEK 11.57) for the Swedish business and £1 = EUR 1.14 (2016: £1 = EUR 1.22) for the Dutch business.

The average rate used for the post acquisition of Scildon for the period to 31 December 2017 was £1 = EUR 1.13.

Assets and liabilities have been translated at the year end rate of £1 = SEK 11.07 (31 December 2016: £1 = SEK 11.14) for the Swedish business and £1 = EUR 1.13 (31 December 2016: £1 = EUR 1.17) for the Dutch business.

Total foreign currency exchange rate movements for the year ended 31 December 2017 resulted in a profit recognised in the Consolidated Statement of Comprehensive Income of £8.3m (year ended 31 December 2016: profit of £20.1m).

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, Swedish and Dutch businesses are such that insurance risk is managed separately for the separate businesses. Accordingly, the information which follows differentiates these businesses. The UK and Waard businesses which are substantially closed to new business, are differentiated in the information provided below, where necessary. The Swedish and Dutch businesses, which are open to new business, comprises the Movestic and Scildon segments respectively.

(a) UK business

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

	2017		2016	
	Gross £000	Net £000	Gross £000	Net £000
Long-term unit-linked without DPF (sums assured)	2,414,486	2,147,432	2,643,702	2,320,059
Long-term non-linked without DPF (sums assured)	10,276,621	1,371,461	11,086,146	1,511,001
Immediate annuities (benefits per annum)	5,683	5,647	5,800	5,764
Deferred annuities with DPF (benefits per annum)	2,035	2,035	1,755	1,755
Long-term with DPF (sums assured)	325,162	315,422	336,745	326,812

Long-term unit-linked and non-linked insurance contracts – without discretionary participation features

Product features

The UK business has 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 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 business, 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 73% 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5 Management of insurance risk (continued)

(a) UK business (continued)

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 95.3% 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 ReAssure 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.

Long-term insurance contracts – with discretionary participation features – CA (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 a fixed charge for expenses, and certain direct 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 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 98.5% 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 business, as follows:

Expense risk

The strategy of the UK business is to outsource the majority of 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 business monitors the financial soundness of third party administrators and has 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.

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 business 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 business are set out in note 31 Insurance Contract Provisions.

(b) 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

	2017		2016	
	Gross £000	Net £000	Gross £000	Net £000
Group				
Sweden	22,343	6,630	21,005	6,011
Norway	19	4	24	5
Individual				
Death	3,534	1,529	3,200	1,448
Waiver of premium	3,373	986	3,288	961
Income protection	7,656	6,520	7,715	6,644
	36,925	**15,669**	**35,232**	**15,069**

Claims outstanding
As at 31 December

	2017		2016	
	Gross £000	Net £000	Gross £000	Net £000
Group				
Sweden	44,995	13,057	41,927	11,337
Norway	1,103	238	2,975	535
Individual				
Death	721	293	821	327
Waiver of premium	10,359	3,444	9,812	3,217
Income protection	24,895	12,991	26,052	13,536
	82,073	**32,023**	**81,587**	**28,952**

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 Sweden and have been sold in Norway in the past via intermediaries. 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 typically provides a maximum coverage of insured benefits up to 40 times a base amount (31 December 2017: SEK 44,800, being approximately £4,044) 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 (31 December 2017 NOK: 93,634, being approximately £8,453) although most policies are between 5 to 10 times the base amount.

All contracts are for an annual period.

5 Management of insurance risk (continued)

(b) Swedish business (continued)

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 and size 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 claim portfolio arising from the acquisition of the business of Aspis Liv, a small Swedish Life and Health insurer in 2010, is 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 120m (approximately £10.8m).

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 99.7% 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 forecasts that its maximum loss would be approximately SEK 150m (approximately £13.5m) gross of reinsurance and SEK 5m (approximately £0.5m) 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 31 Insurance Contract Provisions.

(c) Waard Group

Sums assured/benefits per annum – gross and net of reinsurance
31 December

	2017		2016	
	Gross £000	Net £000	Gross £000	Net £000
Long-term unit-linked without DPF (sums assured)	22,198	22,198	28,997	28,997
Long-term non-linked without DPF (sums assured)	2,221,481	2,107,479	2,499,291	2,260,004

Protection

Product feature

The division mainly wrote term life, sold as a single premium policy in combination with a loan or mortgage. Policy conditions allow for a surrender value at lapse. In addition, similar types of policies covering the risk of disability, unemployment and accident were written. The most significant factors that could increase risk are epidemics and changes in lifestyle and the social security environment.

Management of risks

The portfolio is in run-off and no significant underwriting occurs. For the existing portfolio, the division entered into an excess of loss and catastrophe (Life) and quota share (Health) reinsurance agreement to mitigate the risk in excess of risk appetite for mortality, disability and unemployment.

Concentration of insurance risk

Waard did not write group life and health contracts and an excess of loss limit of €100,000 is applied for life risk, hence concentration risk is limited.

Unit-linked

Product features

The division wrote unit-linked business, with policies paying out 90% of the unit-value at death of the policyholder and 100% at expiry. Early surrender triggers smaller charges for policyholders.

Persistency and expense risk

The portfolio is small and very mature. To mitigate the expense risk, management may also consider the possibility of merging the portfolio into a larger scale one, keeping cost levels appropriate. Persistency levels are moderate and largely depend on investment performance.

Assumptions and sensitivities

The assumptions and sensitivities relating to insurance contract provisions for Waard are set out in note 31 Insurance Contract Provisions.

(d) Scildon

Sums assured/benefits per annum – gross and net of reinsurance
31 December

	2017		2016	
	Gross £000	Net £000	Gross £000	Net £000
Long-term unit-linked without DPF (sums assured)	2,885,027	2,281,513	–	–
Long-term non-linked without DPF (sums assured)	22,925,387	13,484,481	–	–
Immediate annuities (benefits per annum)	91,639	8,188	–	–

Protection

Product feature

The division mainly wrote term life, sold as a regular premium policy. Older policy profit sharing conditions (before 2011) allow for a surrender value at lapse or profit sharing at maturity. The current Mass market product has no surrender value or profit sharing. The most significant factors that could increase risk are epidemics and changes in lifestyle leading to higher mortality.

Management of risks

The product is the main new business product, significant underwriting occurs. Reinsurance agreements, quota share with a maximum retention per policy, to mitigate the risk in excess of risk appetite for mortality at the moment of underwriting are in place. The national NHT cover in case of terrorism is in place but no additional catastrophe or stop loss reinsurance is in place.

Concentration of insurance risk

Scildon does write group pensions contracts (SME segment) with an excess of loss limit of €200,000 per life, hence concentration risk is limited.

Unit-linked

Product features

Scildon writes unit-linked and index linked business, with most policies paying out 0%, 90% or 110% of the unit-value at death of the policyholder and 100% at expiry. Early surrender triggers smaller charges for policyholders. Index linked policies contains either explicit of or implicit guarantees triggers smaller charges for policyholders. Group pension is also unit-linked based.

Persistency and expense risk.

The portfolio is large, but slowly decreasing. To mitigate the expense risk, management may also consider the possibility of merging the portfolio into a larger scale one, keeping cost levels appropriate. Persistency levels are moderate, due to the guarantees given for some policies the risk is high persistency.

Assumptions and sensitivities

The assumptions and sensitivities relating to insurance contract provisions for Scildon are set out in note 31 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 the euro against sterling, arising from its ownership of Movestic, Scildon and the Waard Group.

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 two types of investment contract: unit-linked savings and unit-linked pensions predominantly written in the UK and Sweden.

(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 charges 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) No investment contracts exist within the Dutch business.

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 CA (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.

The notes below explain how market risks are managed using the categories utilised in the businesses' (Asset Liability Matching) ALM 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 2017	Unit-linked contracts £000	*Insurance contracts with DPF £000	Annuities in payment £000	Other non-linked contracts £000	Total £000
Assets					
Property and equipment	–	–	–	4,327	4,327
Investment in associates	–	–	–	6,407	6,407
Investment properties	245	–	–	1,760	2,005
Reinsurers' share of insurance contract provisions	40,410	39,897	–	152,847	233,154
Amounts deposited with reinsurers	38,776	–	–	–	38,776
Financial assets					
Equity securities at fair value through income	512,710	6	–	8	512,724
Holdings in collective investment schemes at fair value through income	4,860,152	216,980	–	125,640	5,202,772
Debt securities at fair value through income	691,412	155,341	192,713	589,351	1,628,817
Mortgage loan portfolio	–	–	–	48,106	48,106
Insurance and other receivables	14,431	1,555	731	42,731	59,448
Prepayments	188	32	–	7,105	7,325
Derivative financial instruments	76	559	–	1,047	1,682
Total financial assets	6,078,969	374,473	193,444	813,988	7,460,874
Reinsurers' share of accrued policyholder claims	8,933	–	–	16,955	25,888
Income taxes	–	–	–	7,681	7,681
Cash and cash equivalents	89,765	1,922	4,667	114,293	210,647
Total assets	**6,257,098**	**416,292**	**198,111**	**1,118,258**	**7,989,759**
Liabilities					
Insurance contract provisions	2,774,427	349,541	111,547	726,764	3,962,279
Other provisions	–	–	–	3,098	3,098
Financial liabilities					
Investment contracts at fair value through Income	3,415,666	–	–	4,607	3,420,273
Borrowings	–	–	–	129,202	129,202
Derivative financial instruments	22,421	73	–	–	22,494
Total financial liabilities	3,438,087	73	–	133,809	3,571,969
Deferred tax liabilities	–	–	–	22,794	22,794
Reinsurance payables	372	8	–	11,026	11,406
Payables related to direct insurance and investment contracts	32,122	5,061	1,050	58,930	97,163
Income taxes	–	–	–	8,514	8,514
Other payables	7,099	516	–	35,369	42,984
Bank overdrafts	259	5	–	827	1,091
Total liabilities	**6,252,366**	**355,204**	**112,597**	**1,001,131**	**7,721,298**

*Insurance contract with DPF include shareholder funds within the CA (S&P) with-profits funds.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

31 December 2016

	Unit-linked contracts £000	*Insurance contracts with DPF £000	Annuities in payment £000	Other non-linked contracts £000	Total £000
Assets					
Property and equipment	–	–	–	519	519
Investment in associates	–	–	–	5,433	5,433
Investment properties	245	–	–	–	245
Reinsurers' share of insurance contract provisions	63,649	40,474	–	150,736	254,859
Amounts deposited with reinsurers	37,437	–	–	–	37,437
Financial assets					
Equity securities at fair value through income	485,153	5	–	7	485,165
Holdings in collective investment schemes at fair value through income	3,702,355	252,194	–	150,053	4,104,602
Debt securities at fair value through income	157,600	120,193	112,479	83,819	474,091
Mortgage loan portfolio	–	–	–	54,756	54,756
Insurance and other receivables	10,331	3,024	–	26,291	39,646
Prepayments	560	229	–	4,482	5,271
Derivative financial instruments	315	33	–	2,425	2,773
Total financial assets	4,356,314	375,678	112,479	321,833	5,166,304
Reinsurers' share of accrued policyholder claims	12,789	46	–	6,472	19,307
Income taxes	–	–	–	3,352	3,352
Cash and cash equivalents	89,766	1,849	4,566	164,172	260,353
Total assets	**4,560,200**	**418,047**	**117,045**	**652,517**	**5,747,809**
Liabilities					
Insurance contract provisions	1,445,438	360,493	115,502	321,013	2,242,446
Other provisions	2	36	–	785	823
Financial liabilities					
Investment contracts at fair value through income	3,023,340	–	–	4,929	3,028,269
Borrowings	–	–	–	86,843	86,843
Derivative financial instruments	97	1,251	–	–	1,348
Total financial liabilities	3,023,437	1,251	–	91,772	3,116,460
Deferred tax liabilities	–	–	–	5,420	5,420
Reinsurance payables	500	8	–	6,391	6,899
Payables related to direct insurance and investment contracts	27,978	5,605	875	26,958	61,416
Income taxes	–	–	–	8,624	8,624
Other payables	9,954	390	–	13,313	23,657
Bank overdrafts	148	97	–	1,377	1,622
Total liabilities	**4,507,457**	**367,880**	**116,377**	**475,653**	**5,467,367**

*Insurance contract with DPF include shareholder funds within the CA (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 ReAssure 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 CA (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. 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.

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.

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

(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 serve 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 2017

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	2,772,893	2,772,893	–	–	–	–	2,772,893
With DPF	349,541	197,293	80,819	58,936	27,688	8,145	372,881
Annuities in payment	111,548	26,534	22,456	18,146	13,841	18,506	99,483
Other non-linked	713,877	411,658	282,146	163,817	81,912	44,249	983,782
Investment contract liabilities							
Unit-linked	3,415,407	3,415,407	–	–	–	–	3,415,407
Other	4,867	4,867	–	–	–	–	4,867
Derivatives	22,794	324	22,470	–	–	–	22,794
Other liabilities	330,371	330,371	–	–	–	–	330,371
Total	**7,721,298**	**7,159,347**	**407,891**	**240,899**	**123,441**	**70,900**	**8,002,478**

31 December 2016

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	1,445,438	1,445,438	–	–	–	–	1,445,438
With DPF	360,493	196,328	82,172	67,846	35,706	11,160	393,212
Annuities in payment	115,502	27,206	23,290	19,085	14,790	20,369	104,740
Other non-linked	321,013	171,288	71,767	41,985	17,732	8,262	311,034
Investment contract liabilities							
Unit-linked	3,023,340	3,023,340	–	–	–	–	3,023,340
Other	4,929	4,929	–	–	–	–	4,929
Derivatives	1,348	1,348	–	–	–	–	1,348
Other liabilities	195,305	195,305	–	–	–	–	195,305
Total	**5,467,368**	**5,065,182**	**177,229**	**128,916**	**68,228**	**39,791**	**5,479,346**

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 ReAssure 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' on page 126. The maturity analysis in respect of the CA (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; and

(ii) its investment in Waard and Scildon, the assets and liabilities of which are principally denominated in euros.

The group's currency risk through its ownership of Movestic, Scildon and Waard Group is reflected in:

(i) foreign exchange translation differences arising on the translation into sterling and consolidation of Movestic, Scildon and Waard Group's financial statements; and

(ii) the impact of adverse exchange rate movements on cash flows between Chesnara plc and its foreign subsidiaries: in the short-term these relate to cash flows from Movestic, Scildon and Waard to Chesnara by way of dividend payments and the acquisition of LGN, the purchase consideration of which is denominated in euros. The risk on cash flows is managed by closely monitoring exchange rate movements and buying forward foreign exchange contracts, where deemed appropriate.

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	2017 £000	2016 £000
Swedish krona		
Assets	3,127,868	2,700,944
Liabilities	(3,057,590)	(2,638,100)
Net assets	**70,278**	**62,844**
Euro		
Assets	2,312,577	207,940
Liabilities	(1,976,235)	(122,655)
Net assets	**336,432**	**85,285**
Norwegian krone		
Assets	968	2,473
Liabilities	(1,312)	(2,427)
Net assets	**(344)**	**46**
US dollar		
Assets	528	128
Liabilities	(106)	–
Net assets/(liabilities)	**422**	**128**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

(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 equity and property values;

(ii) a 100 basis point increase and decrease in per annum market rates of interest; and

(iii) 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 below.

Variation in/arising from	2017		2016	
	Profit before tax £m	Shareholders' equity £m	Profit before tax £m	Shareholders' equity £m
100 bp increase in market rates of interest	(46.8)	(35.2)	(3.4)	(2.7)
100 bp decrease in market rates of interest	45.8	34.3	0.3	0.3
10% increase in equity and property prices	11.9	9.5	12.7	10.1
10% decrease in equity and property prices	(12.8)	(10.2)	(13.1)	(10.5)
10% favourable movement in SEK: sterling exchange rate	1.1	7.8	1.0	7.0
10% adverse movement in SEK: sterling exchange rate	(0.9)	(6.4)	(0.8)	(5.7)
10% favourable movement in EUR: sterling exchange rate*	2.5	37.4	0.6	9.4
10% adverse movement in EUR: sterling exchange rate*	(2.1)	(30.6)	(0.5)	(7.7)

*The 10% favourable and adverse movement for euros includes the Scildon post acquisition values.

(v) 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	2017			2016		
	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	5,155,886	46,886	5,202,772	4,015,093	89,509	4,104,602
Debt securities	751,393	877,424	1,628,817	142,875	331,216	474,091
Cash and cash equivalents	82,322	128,325	210,647	75,264	185,089	260,353
Derivative financial instruments	1,123	559	1,682	2,740	33	2,773
Reinsurers' share of insurance contract liabilities	–	233,154	233,154	–	254,859	254,859
Amounts deposited with reinsurers	–	38,776	38,776	–	37,437	37,437
Mortgage loan portfolio	–	48,106	48,106	–	54,756	54,756
Insurance and other receivables	38,941	20,507	59,448	22,975	16,671	39,646
Reinsurers' share of accrued policyholder claims	10,267	15,621	25,888	–	19,307	19,307
Income taxes	–	7,681	7,681	–	3,352	3,352
Total	**6,039,932**	**1,417,039**	**7,456,971**	**4,258,947**	**992,229**	**5,251,176**

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.

The group's exposure to credit risk is summarised as:

Credit rating As at 31 December 2017	AAA £000	AA £000	A £000	Below A £000	Unrated £000	Total £000
Reinsurers share of insurance contract liabilities	–	139,258	–	4,991	88,905	233,154
Holdings in collective investment schemes	–	–	42,961	–	3,925	46,886
Amounts deposited with reinsurers	–	–	–	–	38,776	38,776
Debt securities at fair value through income	92,796	258,910	188,279	301,201	36,238	877,424
Mortgage loan portfolio	–	–	–	–	48,106	48,106
Insurance and other receivables	1,139	9,600	1,242	3,333	5,193	20,507
Reinsurers share of accrued policyholder claims	–	5,906	48	732	8,935	15,621
Derivative financial instruments	–	–	559	–	–	559
Income taxes	–	7,198	–	–	483	7,681
Cash and cash equivalents	–	54,906	69,459	1,428	2,532	128,325
Total	**93,935**	**475,778**	**302,548**	**311,685**	**184,987**	**1,417,039**
As at 31 December 2016						
Reinsurers share of insurance contract liabilities	–	133,154	2,171	5,155	114,380	254,860
Holdings in collective investment schemes	–	–	82,789	–	6,720	89,509
Amounts deposited with reinsurers	–	–	–	–	37,437	37,437
Debt securities at fair value through income	127,786	175,745	12,190	14,469	1,026	331,216
Mortgage loan portfolio	–	–	–	–	54,756	54,756
Insurance and other receivables	1,261	9,312	76	951	5,071	16,671
Reinsurers share of accrued policyholder claims	–	5,107	967	374	12,858	19,306
Derivative financial instruments	–	–	32	–	1	33
Income taxes	2,956	–	–	–	396	3,352
Cash and cash equivalents	–	40,952	94,827	49,310	–	185,089
Total	**132,003**	**364,270**	**193,052**	**70,259**	**232,645**	**992,229**

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 £98.0m as at 31 December 2017 (31 December 2016: £124.0m) to ReAssure, which does not have a published credit rating. Of this amount £71.0m (31 December 2016: £96.0m) is in respect of currently guaranteed benefits. This counterparty exposure has been mitigated by ReAssure granting to CA a floating charge over related investment assets, which ranks that company equally with ReAssure policyholders. In order to monitor the ongoing creditworthiness of ReAssure, CA reviews the financial statements and regulatory returns submitted by ReAssure to the PRA on an annual basis. No credit limits were exceeded during the year ended 31 December 2017 and 31 December 2016.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6 Management of financial risk (continued)

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 2017, further interim distributions totalling £13,590 (2016: £19,072) 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.

7 Business combinations

On 5 April 2017, Chesnara plc acquired the entire issued share capital (100%) of Legal & General Nederland Levensverzekering Maatschappij N.V. (Legal & General Nederland) an open book life assurance company based in the Netherlands, from Legal & General Group plc, a UK based financial services group for a total consideration of €161.2m (approximately £137.5m), comprising €160.0m base consideration plus interest for the period to completion of €1.2m. On 11 April 2017, it was announced that the newly acquired company was to be re-branded as Scildon. Scildon's policy base is predominantly made up of individual protection and savings contracts. It is open to new business and sells protection, individual savings and group pension contracts via a broker-led distribution model. The acquisition creates scale and presence in the Dutch market and leaves us well positioned to take advantage of any further value adding opportunities that may arise.

The acquisition of this shareholding has given rise to a profit on acquisition of £20.3m calculated as follows:

	Book value £000	Provisional fair value adjustments £000	Fair value £000
Assets			
Intangible assets			
Deferred acquisition costs	11,763	(11,763)	–
Acquired value of in-force business	–	66,296	66,296
Software assets	1,002	–	1,002
Property and equipment	4,022	–	4,022
Investment properties	981	–	981
Reinsurers' share of insurance contract provisions	1,314	–	1,314
Financial assets:			
Holdings in collective investment schemes at fair value through income	811,715	–	811,715
Debt securities at fair value through income	1,058,393	–	1,058,393
Insurance and other receivables	15,567	–	15,567
Prepayments	12,647	–	12,647
Total financial assets	1,898,322	–	1,898,322
Deferred tax asset	8,168	–	8,168
Defined benefit pension scheme surplus	1,056	–	1,056
Income taxes	127	–	127
Cash and cash equivalents	19,533	–	19,533
Total assets	**1,946,288**	**54,533**	**2,000,821**
Liabilities			
Insurance contract provisions	1,736,953	–	1,736,953
Derivatives	23,725	–	23,725
Deferred tax liabilities	10,919	13,634	24,553
Payables related to direct insurance contracts	31,967	–	31,967
Income taxes	10,183	–	10,183
Other payables	15,595	–	15,595
Total liabilities	**1,829,342**	**13,634**	**1,842,976**
Net assets	**116,946**	**40,899**	**157,845**
Net assets acquired			**157,845**
Total consideration, paid in cash			**(137,526)**
Profit arising on business combination			**20,319**

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. We stated in our interim financial statements that we planned to consider the alignment of the IFRS reserving methodology within Scildon with that of the wider Chesnara group. After considering this further in the context of the introduction of the new insurance contract liability standard, IFRS 17, we have decided to defer this proposed alignment until the new standard becomes effective in 2021.

Acquired receivables: Within the net assets acquired are reinsurance related and other receivable balances totalling £16.9m, 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 £1.3m is discounted as a result of the long-term nature of this asset.

Acquired value of in-force business: The acquisition has resulted in the recognition of net of tax intangible asset amounting to £49.8m, 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.

Gain on acquisition: As shown on the previous page, a gain of £20.3m has been recognised on acquisition. Under IFRS 3, a gain on acquisition is defined as being a 'bargain purchase'. At the point of price negotiation and subsequent deal completion, Legal & General was following a strategic plan to dispose of non-core businesses, which included its Dutch operation. In the opinion of the Directors, this resulted in a disposal pricing strategy for Legal & General Nederland that sought to offer an attractive investment opportunity for potential buyers.

Acquisition-related costs: The costs in respect of the transaction amounted to £8.1m. £4.1m of these costs have been included in Administration Expenses, of which £3.8m was recognised within the Consolidated Statement of Comprehensive Income in 2016, with the remainder recognised in the current period. Transaction costs of £3.3m were incurred in respect of the equity fund-raising and were deducted from equity in 2016. Debt fund-raising costs amounted to £0.8m and will be amortised over the life of the loan using the effective interest rate method of amortisation.

Results of Scildon: The results of Scildon have been included in the consolidated financial statements of the Group with effect from 5 April 2017. Net insurance premium revenue for the period was £119.8m, with contribution to overall consolidated profit before tax of £18.4m, before the amortisation of the AVIF and deferred acquisition cost intangible assets. Had Scildon been consolidated from 1 January 2017, the Consolidated Statement of Comprehensive Income would have included net insurance premium revenue of £178.0m, and would have contributed £16.6m to the overall consolidated profit before tax.

8 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 2017 comprise:

CA: This segment represents 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. This segment also contains Save & Prosper Insurance Limited which was acquired on 20 December 2010 and its then subsidiary Save & Prosper Pensions Limited. The S&P business was transferred to CA during 2011. This segment also contains the business of Protection Life, which was purchased on 28 November 2013 and the business of which was transferred to CA effective from 1 January 2015. CA is responsible for conducting 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'.

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 pensions and savings business and providing some life and health product offerings.

Waard Group: This segment represents the group's Dutch life and general insurance business, which was acquired on 19 May 2015 and comprises the three insurance companies Waard Leven N.V., Hollands Welvaren Leven N.V. and Waard Schade N.V., and a servicing company, Tadas Verzekering. During the year, the book of policies held within Hollands Welvaren Leven N.V. was successfully integrated into Waard Leven via a Part VII transfer. The Waard Group's policy base is predominantly made up of term life policies, although also includes unit-linked policies and some non-life policies, covering risks such as occupational disability and unemployment

Scildon: This segment represents the Group's latest Dutch life insurance business, which was acquired on 5 April 2017. Scildon's policy base is predominantly made up of individual protection and savings contracts. It is open to new business and sells protection, individual savings and group pension contracts via a broker-led distribution model.

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.

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 2017.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

8 Operating segments (continued)

(i) Segmental income statement for the year ended 31 December 2017

	CA £000	Movestic £000	Waard Group £000	Scildon £000	Other group activities £000	Total £000
Net insurance premium revenue	39,036	15,438	2,227	120,623	–	177,324
Fee and commission income	29,009	49,155	20	35,664	–	113,848
Net investment return	251,041	223,310	7,349	50,016	101	531,817
Total revenue (net of reinsurance payable)	**319,086**	**287,903**	**9,596**	**206,303**	**101**	**822,989**
Other operating income	13,985	3,215	42	–	–	17,242
Segmental income	**333,071**	**291,118**	**9,638**	**206,303**	**101**	**840,231**
Net insurance contract claims and benefits incurred	(191,524)	(5,447)	(1,051)	(167,225)	–	(365,247)
Net change in investment contract liabilities	(66,969)	(222,953)	–	–	–	(289,922)
Fees, commission and other acquisition costs	(1,368)	(31,959)	(331)	(1,494)	–	(35,152)
Administrative expenses:						
Amortisation charge on software assets	–	(2,052)	–	(124)	–	(2,176)
Depreciation charge on property and equipment	–	(292)	(52)	(229)	–	(573)
Other	(21,678)	(13,485)	(3,015)	(18,813)	(10,528)	(67,520)
Operating expenses	(952)	(3,302)	–	1	14	(4,239)
Financing costs	(4)	(2,756)	–	–	(1,683)	(4,443)
Share of profit from associates	–	949	–	–	–	949
Profit before tax and consolidation adjustments	**50,576**	**9,821**	**5,189**	**18,419**	**(12,096)**	**71,908**
Other operating expenses:						
Charge for amortisation of acquired value of in-force business	(6,224)	(3,527)	(662)	(2,858)	–	(13,271)
Charge for amortisation of acquired value of customer relationships	–	(101)	–	–	–	(101)
Fees, commission and other acquisition costs	–	6,601	–	4,146	–	10,747
Segmental income less expenses	**44,352**	**12,794**	**4,527**	**19,707**	**(12,096)**	**69,283**
Profit arising on business combination	–	–	–	–	20,319	20,319
Profit before tax	**44,352**	**12,794**	**4,527**	**19,707**	**8,223**	**89,602**
Income tax (expense)/credit	(7,085)	71	(1,068)	(4,946)	1,860	(11,168)
Profit after tax	**37,267**	**12,865**	**3,459**	**14,761**	**10,083**	**78,434**

Further analysis of the segmental profit before tax and consolidation adjustments can be found on page 36 of the Financial Review section.

(ii) Segmental balance sheet as at 31 December 2017

	CA £000	Movestic £000	Waard Group £000	Scildon £000	Other group activities £000	Total £000
Total assets	3,020,489	3,148,135	166,803	2,060,569	47,388	8,443,384
Total liabilities	(2,849,557)	(3,057,934)	(109,421)	(1,881,301)	(93,515)	(7,991,728)
Net assets	**170,932**	**90,201**	**57,382**	**179,268**	**(46,127)**	**451,656**
Investment in associates	–	6,407	–	–	–	6,407
Additions to non-current assets	–	23,836	313	3,719	–	27,868

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(iii) Segmental income statement for the year ended 31 December 2016

	CA £000	Movestic £000	Waard Group £000	Other group activities £000	Total £000
Net insurance premium revenue	46,989	14,903	2,658	–	64,550
Fee and commission income	31,610	41,296	26	–	72,932
Net investment return	337,903	169,130	8,464	184	515,681
Total revenue (net of reinsurance payable)	**416,502**	**225,329**	**11,148**	**184**	**653,163**
Other operating income	13,360	3,751	503	–	17,614
Segmental income	**429,862**	**229,080**	**11,651**	**184**	**670,777**
Net insurance contract claims and benefits incurred	(263,202)	(7,695)	(1,464)	–	(272,361)
Net change in investment contract liabilities	(100,599)	(168,508)	–	–	(269,107)
Fees, commission and other acquisition costs	(1,664)	(25,089)	(330)	–	(27,083)
Administrative expenses:					
Amortisation charge on software assets	–	(1,243)	–	–	(1,243)
Depreciation charge on property and equipment	–	(197)	–	–	(197)
Other	(20,460)	(12,800)	(3,664)	(8,251)	(45,175)
Operating expenses	(1,204)	(3,209)	–	19	(4,394)
Financing costs	(2)	(1,629)	–	(1,641)	(3,272)
Share of profit from associates	–	150	–	–	150
Profit before tax and consolidation adjustments	**42,731**	**8,860**	**6,193**	**(9,689)**	**48,095**
Other operating expenses:					
Charge for amortisation of acquired value of in-force business	(6,247)	(3,554)	(618)	–	(10,419)
Charge for amortisation of acquired value of customer relationships	–	(236)	–	–	(236)
Fees, commission and other acquisition costs	–	3,245	–	–	3,245
Segmental income less expenses	**36,484**	**8,315**	**5,575**	**(9,689)**	**40,685**
Profit before tax	**36,484**	**8,315**	**5,575**	**(9,689)**	**40,685**
Income tax (expense)/credit	(6,663)	(7)	(1,721)	2,986	(5,405)
Profit after tax	**29,821**	**8,308**	**3,854**	**(6,703)**	**35,280**

(iv) Segmental balance sheet as at 31 December 2016

	CA £000	Movestic £000	Waard Group £000	Other group activities £000	Total £000
Total assets	3,047,490	2,718,156	207,160	122,957	6,095,763
Total liabilities	(2,883,575)	(2,638,490)	(122,655)	(57,482)	(5,702,202)
Net assets	**163,915**	**79,666**	**84,505**	**65,475**	**393,561**
Investment in associates	–	5,433	–	–	5,433
Additions to non-current assets	–	11,894	–	–	11,894

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

9 Fees and commission income

Year ended 31 December		
	2017	2016
Fee income	**£000**	**£000**
Policy-based fees	43,519	13,696
Fund management-based fees	48,386	36,391
Benefit-based fees	14,585	16,226
Change in deferred income – gross	737	774
Change in deferred income – reinsurers' share	(64)	(59)
Total fee income	107,163	67,028
Commission income	6,685	5,904
Total fee and commission income	**113,848**	**72,932**

10 Net investment return

Year ended 31 December		
	2017 £000	**2016 £000**
Dividend income	39,855	30,444
Interest income	34,189	21,047
Rental income from investment properties	15	893
Net fair value gains and losses		
Equity securities designated as at fair value through income on initial recognition	442,445	392,726
Debt securities designated as at fair value through income on initial recognition	6,306	72,021
Derivative financial instruments	9,007	(1,450)
Net investment return	**531,817**	**515,681**

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 2016: £nil).

11 Other operating income

Year ended 31 December		
	2017 £000	**2016 £000**
Investment management fee rebate	13,991	13,749
Charges to policyholder funds for yield tax	2,963	3,194
Other	288	671
Total other operating income	**17,242**	**17,614**

All of the income streams set out in notes 9,10 and 11 equate to revenue as defined by IAS 18.

12 Insurance contract claims and benefits

Year ended 31 December	2017 £000	2016 £000
Claims and benefits paid to insurance contract holders	465,729	346,117
Decrease in insurance contract provisions	(51,033)	(11,392)
Total insurance contract claims and benefits	**414,696**	**334,725**
Reinsurer's share of claims and benefits	(49,449)	(62,364)
Net insurance contract claims and benefits incurred	**365,247**	**272,361**

13 Change in investment contract liabilities

Year ended 31 December	2017 £000	2016 £000
Changes in the fair value of investment contracts designated on initial recognition as fair value through income	266,344	261,180
Changes in the fair value of policyholders' funds held by the group designated on initial recognition as fair value through income	27,259	13,544
Total increase in investment contract liabilities	**293,603**	**274,724**
Reinsurers' share of investment contract liabilities	(3,681)	(5,617)
Net increase in investment contract liabilities	**289,922**	**269,107**

Investment contract benefits comprise benefits accruing to holders of investment contracts issued by the group.

14 Fees, commission and other acquisition costs

Year ended 31 December	2017 £000	2016 £000
Directly expensed costs:		
Insurance contracts		
Commission, new business and renewal costs	12,904	11,009
Deferred amount	(12,167)	(7,048)
	737	**3,961**
Investment contracts		
Commission, new business and renewal costs	24,836	20,810
Deferred amount	(15,644)	(13,064)
	9,192	**7,746**
Amortisation of deferred acquisition costs:		
Insurance contracts	8,177	7,326
Investment contracts	6,329	4,837
Investment contracts-reinsurance	(30)	(32)
Total	**24,405**	**23,838**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

15 Administrative expenses

Year ended 31 December	Note	2017 £000	2016 £000
Personnel-related costs	45	30,919	17,998
Investment management fees		7,580	6,213
Amortisation charge on software assets		2,218	794
Depreciation charge on property and equipment		698	197
Costs paid to third-party administrators		13,295	11,518
Other goods and services		15,559	9,895
Total		**70,269**	**46,615**

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	2017 £000	2016 £000
Fees payable to the company's auditor for the audit of the company's financial statements	50	50
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*	743	537
Audit-related assurance services**	462	719
Corporate finance services***	–	532
Total	**1,255**	**1,838**

*Includes Ernst & Young audit fees in respect of the Scildon audit.
**Includes the audit of regulatory returns submitted to the UK regulator in both years.
***2016 relates to the fees associated with the proposed acquisition of LGN.

16 Other operating expenses

Year ended 31 December	2017 £000	2016 £000
Charge for amortisation of acquired value of in-force business	**13,271**	**10,419**
Charge for amortisation of acquired value of customer relationships (AVCR)	**101**	**236**
Other		
Direct operating expenses of investment properties		
Revenue-generating properties	–	1
Non revenue-generating properties	2	56
Recovery of cash deposit	(14)	(19)
Payment of yield tax relating to policyholder funds	3,286	3,194
Other	965	1,162
Total	**4,239**	**4,394**

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.

17 Financing costs

Year ended 31 December	2017 £000	2016 £000
Interest expense on bank borrowings	1,687	1,644
Interest expense on financial reinsurance	2,674	1,516
Other interest	82	112
Total financing costs	**4,443**	**3,272**

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.

18 Income tax

Total income tax comprises: Year ended 31 December	2017 £000	2016 £000
CA and other group activities – net expense	(5,225)	(3,862)
Movestic – net credit	71	37
Waard Group – net expense	(1,068)	(1,580)
Scildon – net expense	(4,946)	–
Total net expense	**(11,168)**	**(5,405)**

UK Business

CA and other group activities Year ended 31 December	2017 £000	2016 £000
Current tax		
Current year	(6,220)	(5,155)
Overseas tax	(480)	(524)
Adjustment to prior years	–	167
Net expense	(6,700)	(5,512)
Deferred tax		
Origination and reversal of temporary differences	1,475	1,650
Total income tax expense	**(5,225)**	**(3,862)**

Reconciliation of effective tax rate on profit before tax Year ended 31 December	2017 £000	2016 £000
Profit before tax	**32,256**	**26,795**
Income tax using the domestic corporation tax rate of 19.25% (2016: 20.0%)	(6,209)	(5,359)
Other permanent differences	(468)	(441)
Effect of UK tax bases on insurance profits		
Offset of franked investment income	1,753	2,008
Variation in rate of tax on amortisation of acquired in-force value	(6)	80
Foreign tax	(390)	(426)
Effect of change in tax rate	48	75
Other	47	35
Over provided in previous years	–	166
Total income tax expense	**(5,255)**	**(3,862)**

There has been a change in tax rate during the year, due to a reduction in the corporation tax rate from 20% to 19%.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

18 Income tax (continued)

Movestic

Movestic
Year ended 31December

	2017 £000	2016 £000
Current tax		
Current year expense*	(6)	(7)
Adjustments for prior years	(9)	–
Net credits	(15)	(7)
Deferred tax		
Origination and reversal of temporary differences	86	44
Total income tax credit	**71**	**37**

*Tax in Sweden is levied as against the value of policyholder unit-linked funds and is borne by the policyholder. This results in a small residual direct corporation tax charge.

Reconciliation of effective tax rate on profit before tax
Year ended 31 December

	2017 £000	2016 £000
Profit before tax	**12,794**	**8,315**
Income tax using the domestic corporation tax rate of 22%	(2,815)	(1,829)
Non-taxable income in relation to unit-linked business	2,242	2,053
Impact of different tax rate for subsidiaries	(578)	–
Non-taxable fair value adjustment	698	(44)
Temporary differences	41	–
Permanent differences	461	(93)
Unrecognised tax recoverable	72	(8)
Non-deductible expenses	(41)	(42)
Under provided in prior years	(9)	–
Total income tax credit	**71**	**37**

Waard Group

Waard Group
Year ended 31 December

	2017 £000	2016 £000
Current tax		
Current year expense	(1,243)	(2,575)
Adjustment to prior years	55	(31)
Net credits	(1,188)	(2,606)
Deferred tax		
Origination and reversal of temporary differences	(120)	1,026
Total income tax expense	**(1,068)**	**(1,580)**

Waard Group (continued)

Reconciliation of effective tax rate on profit before tax
Year ended 31 December

	2017 £000	2016 £000
Profit before tax	**4,527**	**5,574**
Income tax using the domestic corporation tax rate of 25%	(1,132)	(1,393)
Impact of different tax rate for subsidiaries	9	–
Permanent differences	–	(156)
Over/(Under) provided in prior years	55	(31)
Total income tax expense	**(1,068)**	**(1,580)**

Scildon

Scildon
Year ended 31 December

	2017 £000	2016 £000
Current tax	**(3,014)**	**–**
Current year expense	–	–
Net credits	(3,014)	–
Deferred tax		
Origination and reversal of temporary differences	(1,932)	–
Total income tax expense	**(4,946)**	**–**

Reconciliation of effective tax rate on profit before tax
Year ended 31 December

	2017 £000	2016 £000
Profit before tax	**19,707**	**–**
Income tax using the domestic corporation tax rate of 25%	(4,927)	–
Non-deductible expenses	(28)	–
Over provided in prior years	9	–
Total income tax expense	**(4,946)**	**–**

19 Deferred acquisition costs

Year ended 31 December

	2017 £000	2016 £000
Balance at 1 January	**48,318**	**36,061**
Additions arising from new business	27,685	20,132
Amortisation charged to income	(14,506)	(12,163)
Foreign exchange translation difference	361	4,288
Balance at 31 December	**61,858**	**48,318**
Current	6,191	5,362
Non-current	55,667	42,956
Total	**61,858**	**48,318**

The amortisation charged to income is recognised in fees, commission and other acquisition costs (see note 14).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

20 Acquired value of in-force business (AVIF)

31 December	2017 £000	2016 £000
Cost:		
Balance at 1 January	**151,617**	**143,409**
Additions – acquisition of subsidiary	66,296	–
Foreign exchange translation difference	3,288	8,208
Balance at 31 December	**221,201**	**151,617**
Amortisation and impairment losses:		
Balance at 1 January	**88,674**	**75,068**
Amortisation for the year	13,271	10,408
Foreign exchange translation difference	217	3,198
Balance at 31 December	**102,162**	**88,674**
Carrying amounts at 1 January	**62,943**	**68,341**
At 31 December	**119,039**	**62,943**
Current	13,428	9,498
Non-current	105,611	53,445
Total	**119,039**	**62,943**

The amortisation charged to the Consolidated Statement of Comprehensive Income is recognised in Other Operating Expenses (see note 16).

21 Goodwill

The goodwill is arising from the purchase of Sparplatsen by the Movestic business.

22 Software assets

31 December	2017 £000	2016 £000
Cost:		
Balance at 1 January	**21,061**	**15,962**
Additions – acquisition of subsidiary	1,069	–
Additions	928	3,525
Disposals	–	(441)
Foreign exchange translation difference	160	2,015
Balance at 31 December	**23,218**	**21,061**
Amortisation and impairment losses:		
Balance at 1 January	**14,501**	**11,242**
Additions – acquisition of subsidiary	67	–
Amortisation charge for the year	2,218	794
Impairment write-down	–	1,039
Foreign exchange translation difference	74	1,426
Balance at 31 December	**16,860**	**14,501**
Carrying amounts at 31 December	**6,358**	**6,560**
Current	2,260	1,991
Non-current	4,098	4,569
Total	**6,358**	**6,560**

23 Property and equipment

31 December	2017 £000	2016 £000
Cost:		
Balance at 1 January	**2,303**	**2,235**
Additions – acquisitions of subsidiary	8,825	–
Additions	211	91
Disposals	(36)	(307)
Foreign exchange translation difference	500	284
Balance at 31 December	**11,803**	**2,303**
Amortisation and impairment losses:		
Balance at 1 January	**1,784**	**1,677**
Additions – acquisitions of subsidiary	4,803	–
Depreciation charge for the year	698	197
Disposals	(19)	(306)
Foreign exchange translation difference	210	216
Balance at 31 December	**7,476**	**1,784**
Carrying amounts at 31 December	**4,327**	**519**
Current	723	176
Non-current	3,604	343
Total	**4,327**	**519**

24 Investment in associate

31 December	2017 £000	2016 £000
Balance at 1 January	**5,433**	**4,707**
Share of profit	949	150
Foreign exchange translation difference	25	576
Balance at 31 December	**6,407**	**5,433**

Associates at 100%	Assets £000	Liabilities £000	Revenues £000	Profit £000
Modernac S.A.	43,862	30,786	9,454	1,923
Total at 31 December 2017	**43,862**	**30,786**	**9,454**	**1,923**

Associates at 49%	Equity at 100% £000	Equity at 49% £000	49% share of profit £000
Modernac S.A	13,076	6,407	949
Total at 31 December 2017	**13,076**	**6,407**	**949**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

25 Financial instruments

Group

Financial assets by measurement category at 31 December

	2017 £000	2016 £000
Fair value through income		
Designated at fair-value through income on initial recognition	7,610,042	5,293,255
Derivative financial instruments	1,682	2,773
Mortgage loan portfolio	48,106	54,756
Insurance and other receivables	59,448	39,646
Prepayments	7,325	5,271
Total	**7,726,603**	**5,395,701**

Fair value is the amount for which an asset or liability 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 2017

Financial assets	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Equities – listed	512,724	–	–	512,724
Holdings in collective investment schemes	5,202,772	–	–	5,202,772
Debt securities – fixed rate:				
– Government bonds	961,194	30,202	–	991,396
– Listed	631,416	–	–	631,416
Debt securities – floating rate listed	6,005	–	–	6,005
Total debt securities	1,598,615	30,202	–	1,628,817
Policyholders' funds held by the group	265,729	–	–	265,729
Derivative financial instruments	–	1,682	–	1,682
Total	**7,598,840**	**31,884**	**–**	**7,611,724**
Current				5,048,130
Non-current				2,563,594
Total				**7,611,724**
Financial liabilities				
Investment contracts at fair value through income	–	3,420,272	–	3,420,272
Liabilities related to policyholders' funds held by the group	265,729	–	–	265,729
Derivative financial instruments	22,170	324	–	22,494
Total	**287,899**	**3,420,596**	**–**	**3,708,495**

Fair value measurement at 31 December 2016

Financial assets	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Equities – listed	485,165	–	–	485,165
Holdings in collective investment schemes	4,104,602	–	–	4,104,602
Debt securities – fixed rate:				
– Government bonds	322,870	29,357	–	352,227
– Listed	120,302	–	–	120,302
Debt securities – floating rate listed	1,562	–	–	1,562
Total debt securities	444,734	29,357	–	474,091
Policyholders' funds held by the group	229,397	–	–	229,397
Derivative financial instruments	–	2,773	–	2,773
Total	**5,263,898**	**32,130**	**–**	**5,296,028**
Current				2,749,699
Non-current				2,546,329
Total				**5,296,028**
Financial liabilities				
Investment contracts at fair value through income	–	3,028,269	–	3,028,269
Liabilities related to policyholders' funds held by the group	229,397	–	–	229,397
Derivative financial instruments	–	1,348	–	1,348
Total	**229,397**	**3,029,617**	**–**	**3,259,014**

The debt securities classified as Level 2 at 2016 and 2017 are traded in active markets with less depth or wider-bid ask spreads. This does not meet the classification as Level 1 inputs. The fair values of debt securities not traded in active markets are determined using broker quotes or valuation techniques with observable market inputs. Financial instruments valued using broker quotes are classified at Level 2, only where there is a sufficient range of available quotes.

These assets were valued using counterparty or broker quotes and were periodically validated against third-party models.

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 linked and non-linked 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 2017 £000	Carrying amount 2016 £000	Fair value 2017 £000	Fair value 2016 £000
Financial liabilities				
Borrowings	129,202	86,843	132,204	87,196

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. The group holds no Level 3 liabilities as at the balance sheet date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

25 Financial instruments (continued)

Company

Fair value measurement at 31 December	2017 £000	2016 £000
Holdings in collective investment schemes	29,091	72,939
Total	**29,091**	**72,939**
Current	29,091	72,939
Non-current	–	–
Total	**29,091**	**72,939**

There were no Level 2 and Level 3 assets.

Investment in subsidiaries
Company

Year ended 31 December	2017 £000	2016 £000
Balance at 1 January	**249,234**	**249,234**
Capital contribution to Chesnara Holdings B.V.*	105,486	–
Balance at 31 December	**354,720**	**249,234**
Current	–	–
Non-current	354,720	249,234
Total	**354,720**	**249,234**

*During the year Chesnara plc provided a capital contribution to Chesnara Holding B.V of £105.5m to part fund the acquisition of Scildon. The remainder of the acquisition cost of £137.5m was funded by a dividend from Chesnara Holdings B.V. of £32.0m.

A list of investments in subsidiaries held by the group is disclosed in note 52.

26 Mortgage loan portfolio

Year ended 31 December	2017 £000	2016 £000
Loans and receivables at amortised cost	**48,106**	**54,756**
Current	18,476	9,827
Non-current	29,630	44,929
Total	**48,106**	**54,756**

The mortgage loan portfolio was acquired in 2016 by the Waard Group and is stated at amortised cost.

27 Insurance and other receivables

Group

Insurance and other receivables
31 December

	2017 £000	2016 £000
Receivables arising from insurance contracts		
Brokers	711	–
Policyholders	4,260	2,479
Receivables arising from investment contracts		
Other	10,042	10,084
Other receivables		
Loan to associated companies	697	673
Accrued interest income	15,898	7,942
Receivables from fund management companies	7,711	5,637
Initial margin payments on derivatives	3,621	6,545
Other	16,508	6,286
Total	**59,448**	**39,646**
Current	57,941	38,186
Non-current	1,507	1,460
Total	**59,448**	**39,646**

The carrying amount is a reasonable approximation of fair value.

28 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 and interest rate swaps within the Scildon business.

31 December

	2017		2016	
	Asset £000	Liability £000	Asset £000	Liability £000
Interest rate swaps	–	(22,170)	–	–
Exchange-traded futures	635	(324)	349	(1,348)
Financial reinsurance embedded derivative	1,047	–	2,424	–
Total	**1,682**	**(22,494)**	**2,773**	**(1,348)**
Current	898	(22,494)	957	(1,348)
Non-current	784	–	1,816	–
Total	**1,682**	**(22,494)**	**2,773**	**(1,348)**

28 Derivative financial instruments (continued)

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 25.

Exchange-traded futures (by geographical investment market)
31 December

	2017		2016	
	Asset £000	Liability £000	Asset £000	Liability £000
Australia	2	(23)	16	–
Canada	6	–	–	–
Switzerland	–	(3)	3	(25)
Europe	5	(73)	28	(171)
UK	62	(197)	277	–
Hong Kong	28	–	–	(64)
Japan	154	(16)	10	(51)
USA	378	(11)	15	(1,034)
Denmark	–	(1)	–	(3)
Total	**635**	**(324)**	**349**	**(1,348)**

Financial reinsurance embedded derivative

In respect of Movestic, the group has 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 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 25.

Derivatives within the CA (S&P with-profits funds)

As part of its investment management strategy, CA enters into a limited range of derivative instruments to manage its exposure to various risks.

CA 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. CA 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.

CA 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 25.

Derivatives within the Scildon

Scildon uses various interest rate derivatives to hedge some of the risk of changes in value of its obligations under insurance contracts in non-linked funds.

29 Cash and cash equivalents

Group

31 December	2017 £000	2016 £000
Bank and cash balances	86,545	134,055
Call deposits due within 1 month	40,011	38,851
Call deposits due after 1 month	84,091	87,447
Total cash and cash equivalents	**210,647**	**260,353**
Bank overdrafts	(1,091)	(1,622)
Cash and cash equivalents in the statement of cash flows	**209,556**	**258,731**

The effective interest rate on short-term bank deposits was 0.20% (2016: 0.18%), with an average maturity of 31 days (2016: 35 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 £89.8m (2016: £89.8m) held in unit-linked policyholders' funds.

Company

31 December	2017 £000	2016 £000
Bank and cash balances	1,259	6,009
Cash deposits due within 1 month	546	23,049
Cash deposits maturing between greater than 1 month and less than 1 year	10,062	15,125
Total	**11,867**	**44,183**

30 Capital management

(a) Regulatory context:

Solvency II

The Chesnara group is required to comply with the Solvency II capital regime. Solvency II came into force on 1 January 2016 and is a EU insurance legislation that aims to unify the EU insurance market and enhance consumer protection. The Solvency II regime includes rules over the quantity and quality of capital (known as 'own funds') that insurance companies and groups need in order to meet the regime's required level of capital (known as the 'Solvency Capital Requirement'). The Chesnara group operates exclusively within the EU and as a result the Solvency II regime applies to the group and all regulated insurance companies within the group. The regulators responsible for the supervision of the group and its subsidiaries have been shown in section (c)(i).

The Solvency II regime has specific rules regarding how own funds are recognised and valued. In a number of cases, the IFRS and Solvency II value of an asset and liability are the same, but in some cases there are differences. In particular, liabilities for insurance and investment contracts are valued differently, with IFRS remaining largely based on the previous Solvency I regime. In addition, Solvency II has differing treatments for certain intangible assets. A high level reconciliation between the IFRS net assets and Solvency II own funds of the group and its subsidiaries has been provided in part (c)(ii) of this note.

Regarding the Solvency Capital Requirement (SCR) of the Chesnara group and its subsidiaries, the group has elected to use the 'standard formula' approach for its calculation, which means we are applying the formulae as included in the Solvency II framework. The calculations within the standard formula have been designed such that, on the basis that an insurance company holds own funds that are at least equal to its SCR, it will be able to withstand a 1 in 200 year event. An alternative would have been to use an 'internal model' but this was not deemed appropriate for the size and complexity of the Chesnara group.

Company law

As well as complying with the Solvency II regime, each company within the group is required to comply with relevant company law capital and distribution rules.

(b) Objectives, policies and processes for managing capital

(i) Objectives

To manage compliance with the externally imposed capital requirements the group and its subsidiaries have established capital management policies in place. The objectives of these policies are:

- to ensure that capital is managed in a way that is consistent with the business strategy of the group and its subsidiaries, in that they:
  - promote fair customer outcomes through protecting policyholders;
  - provide protection to shareholders through ensuring that the business is adequately protected against stress events; and
  - provide a framework to support the decision making process for returns to shareholders via dividends.
- to ensure that capital of the group and its subsidiaries is managed in accordance with the board's risk appetite, in particular each board's aversion for own funds to fall below the SCR.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

30 Capital management (continued)

(b) Objectives, policies and processes for managing capital (continued)

(ii) Policies

In light of the objectives for the group's and its subsidiaries' capital management policies, the following quantitative limits for managing own funds are applied across the group:

Region	CA	Movestic	Waard Group	Scildon	Group
Dividend paying limit: Own funds stated as % of SCR	120%	120%	200%	200%	110%
Management actions limit: Own funds stated as % of SCR	110%	110%	175%	175%	105%

Dividend paying limit: This is the point at which a dividend would cease to be paid, until at such time the solvency position was restored above this point. This limit is set by the relevant board in each division with reference to its respective risk appetite, as articulated in each divisions' capital management policy.

Management actions limit: This is the point at which, should own funds fall below this level, additional management actions would be taken to restore own funds back above this level. In essence this represents an internal 'ladder of intervention limit' that is set by the group and divisional boards.

To put the above table and definitions in context, and taking group as an example, this means that the group will not pay a dividend should the payment of the dividend take the group own funds to below 110% of its SCR. Should own funds fall below 105% of SCR additional management actions will be taken.

(iii) Process for management of capital

The following key processes and procedures are in place across the group to manage adherence to the capital management policies in place:

- *Internal solvency reporting:* A number of internal reports are produced that focus on the solvency position of the group/company. These include the Own Risk & Solvency Assessment (ORSA) report, a quarterly actuarial report and a quarterly finance report. All of these are presented to and approved by the board.
- *Production of projections:* On at least an annual basis, solvency projections are produced for the group and its subsidiaries. These projections are included in both the business plans and the ORSA report, and show how management anticipates the solvency position to develop over time. The projections process includes assessing the impact of a number of different stress scenarios to ensure that the sensitivities of the business are understood. Both the ORSA and the business plans are presented to and approved by the board.
- *Regular review of internal limits in place:* On at least an annual basis, the limits described in (b)(ii) of this note are reviewed and assessed, having regard to the developments of the business and any other changes that may have affected the group's/divisions' risk appetite.
- *Recovery management protocol:* A protocol for management actions has been designed which, in effect, represents an internally set 'ladder of intervention'. The protocol includes items such as solvency monitoring frequency, what level of escalations are required and what management actions need to be considered.
- *Trigger monitoring:* On at least a monthly basis specific key risk indicators are monitored against pre-defined trigger points. The trigger points are set having regard for the sensitivity of the group to certain scenarios. Trigger points and the list of risk indicators being monitored are assessed at least annually.

(iv) Compliance during year

The group, and all insurance companies within the group, have held own funds above their respective Solvency Capital Requirements at all times during the year.

(c) Quantitative analysis

(i) Group solvency position

The solvency position of the group and its divisions at 31 December 2017 and at 31 December 2016, which is unaudited, has been shown in the tables below. They present a view of the solvency position which may differ to the position of the individual insurance company(ies) within that division.

31 December 2017 (unaudited)

Region	CA £m	Movestic £m	Waard Group £m	Scildon £m	Other group & consolidation adjustments £m	Group £m
Own funds (pre dividends)	198.7	230.7	61.2	210.0	(65.8)	634.8
Proposed dividend	(32.0)	(2.8)	(13.0)	(22.2)	50.5	(19.6)
Own funds (post dividends)	**166.7**	**227.8**	**48.2**	**187.8**	**(15.3)**	**615.2**
SCR	128.1	149.0	10.0	81.4	53.3	421.8
Solvency surplus	**38.6**	**78.8**	**38.2**	**106.4**	**n/a**	**193.4**
Solvency ratio	**130%**	**153%**	**483%**	**231%**	**n/a**	**146%**
Dividend paying limit (% of SCR)	120%	120%	200%	200%	n/a	110%
Dividend paying limit (£)	153.7	178.9	20.0	162.8	n/a	464.0
Surplus over dividend paying limit	13.0	49.0	28.2	25.0	n/a	151.2

31 December 2016

Region	CA £m	Movestic £m	Waard Group £m	Other group & consolidation adjustments £m	Group £m
Own funds (pre dividends)	196.3	192.3	86.6	49.2	524.4
Proposed dividend	(30.0)	(2.7)	–	13.7	(19.0)
Own funds (post dividends)	**166.3**	**189.6**	**86.6**	**62.9**	**505.4**
SCR	129.8	135.6	12.2	43.1	320.7
Solvency surplus	**36.5**	**54.0**	**74.4**	**n/a**	**184.7**
Solvency ratio	**128%**	**140%**	**712%**	**n/a**	**158%**
Dividend paying limit (% of SCR)	120%	120%	200%	n/a	110%
Dividend paying limit (£)	155.8	162.7	24.3	n/a	352.8
Surplus over dividend paying limit	10.5	26.9	62.3	n/a	152.6

(ii) Reconciliation between Solvency II own funds and IFRS net assets (unaudited)

The tables below show the key differences between the Solvency II own funds reported in part (c)(i) and the group's IFRS net assets.

31 December 2017 (unaudited)

Region	CA £m	Movestic £m	Waard Group £m	Scildon £m	Other group & consolidation adjustments £m	Group £m
Solvency II own funds (post dividends)	**166.7**	**227.8**	**48.2**	**187.8**	**(15.3)**	**615.2**
Add Back: Ring-fenced fund surplus restrictions	26.6	–	–	–	–	26.5
Add Back: Intangible assets	11.5	94.1	63.1	12.3	1.6	182.6
Add Back: Foreseeable dividends	32.0	2.8	13.0	22.2	(50.5)	19.6
Add Back: Difference in valuation of technical provisions	(78.5)	(233.6)	(10.7)	(111.2)	24.0	(410.0)
Add Back: Difference in deferred tax	12.4	–	(10.4)	24.7	(6.4)	20.3
Add Back: Other valuation differences	0.2	(0.9)	(2.1)	–	0.2	(2.5)
IFRS Net Assets	**170.9**	**90.2**	**101.1**	**135.8**	**(46.3)**	**451.7**

31 December 2016 (unaudited)

Region	CA £m	Movestic £m	Waard Group £m	Other group & consolidation adjustments £m	Group £m
Solvency II own funds (post dividends)	**166.3**	**189.6**	**86.6**	**62.9**	**505.4**
Add Back: Ring-fenced fund surplus restrictions	10.6	–	–	0.2	10.8
Add Back: Intangible assets	19.1	88.8	5.5	–	113.4
Add Back: Foreseeable dividends	30.0	2.7	–	(13.7)	19.0
Add Back: Difference in valuation of technical provisions	(71.3)	(199.2)	(8.6)	20.6	(258.5)
Add Back: Difference in deferred tax	8.9	(0.3)	3.3	(4.0)	7.9
Add Back: Other valuation differences	0.3	(1.9)	(2.3)	(0.5)	(4.4)
IFRS Net Assets	**163.9**	**79.7**	**84.5**	**65.5**	**393.6**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

31 Insurance contract provisions

(a) Analysis of insurance contract provisions by operating segment

31 December		2017			2016	
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
CA	1,992,705	173,718	1,818,987	2,041,761	194,765	1,846,996
Movestic	86,271	54,149	32,122	85,951	54,926	31,025
Waard Group	100,329	4,413	95,916	114,734	5,168	109,566
Scildon	1,782,974	874	1,782,100	–	–	–
Total insurance contract provisions	**3,962,279**	**233,154**	**3,729,125**	**2,242,446**	**254,859**	**1,987,587**
Current	243,326	39,087	204,239	286,720	86,518	200,202
Non-current	3,718,953	194,067	3,524,886	1,955,726	168,341	1,787,385
Total	**3,962,279**	**233,154**	**3,729,125**	**2,242,446**	**254,859**	**1,987,587**

(b) Analysis of movement in insurance contract provisions

Year ended 31 December		2017			2016	
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Balance at 1 January	**2,242,446**	**254,859**	**1,987,587**	**2,232,083**	**282,628**	**1,949,455**
Arising on business combination	1,736,389	1,314	1,735,075	–	–	–
Premiums received	186,260	15,053	171,207	75,126	24,523	50,603
Fees deducted	(59,961)	(1,555)	(58,406)	(24,226)	(1,773)	(22,453)
Reserves released in respect of benefits paid	(410,873)	(55,286)	(355,587)	(320,807)	(105,846)	(214,961)
Movements in provisions for contracts sold – Movestic						
– in current year	30,304	17,856	12,448	25,226	16,173	9,053
– in prior years	(26,070)	(17,128)	(8,942)	(18,870)	(12,127)	(6,743)
Investment return	170,646	3,273	167,373	197,054	9,412	187,642
Other movements	93,138	14,768	78,370	76,860	41,869	34,991
Balance at 31 December	**3,962,279**	**233,154**	**3,729,125**	**2,242,446**	**254,859**	**1,987,587**

(c) Basis and assumptions for calculating insurance contract provisions

UK

(i) Basis

The process used to determine the assumptions underlying the calculation of IFRS 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.

The technical provision for CA (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 ReAssure. When performing the gross liability adequacy test allowance is made for expected future bonuses paid by ReAssure. This is based on the realistic liabilities of the underlying policies reinsured, as provided to CA by ReAssure.

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 the PL component of CA, 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.

(ii) Principal assumptions:

Mortality
A base mortality table is selected which is most appropriate for each type of contract taking into account rates charged 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.

For CA (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	2017		2016	
	SPI	SPP	SPI	SPP
Assurances:				
Regular premium plans	2.625%	2.625%	2.625%	2.625%
Single premium contracts	3.000%	3.750%	3.000%	3.375%
Linked TIC*	–	4.000%	–	4.000%

*Trustee Investment Contract, a unit-linked contract ('TIC').

Discount rates
CA uses appropriate rates of interest, for different product types, in discounting projected liabilities. As at 31 December 2017 for the material product types, these lay between 0.20% and 2.05% (31 December 2016: between 0.40% and 1.70%).

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%	65%	75%	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 CA funds.

Taxation
It has been assumed that current tax legislation and tax rates will not change.

The sensitivities of technical provisions to changes in assumptions are set out overleaf.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

31 Insurance contract provisions (continued)

(c) Basis and assumptions for calculating insurance contract provisions (continued)

UK (continued)

(iii) Valuation of options and guarantees

Contracts with discretionary participation features

The principal financial options and guarantees in CA (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.

Provisions for CA (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 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.

The cost of guaranteeing a minimum investment return on participating contracts 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.

The following sets out the cumulative charge to shareholders for the cost of guarantees on these bases:

Year ended 31 December	2017 £000	2016 £000
At beginning of the year	**35,746**	**37,156**
Charge/(credit) to income	16,511	(1,410)
At the end of year	**19,235**	**35,746**

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 £696,000 as at 31 December 2017 (31 December 2016: £644,000).

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 3.6% 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 2017 was £4.2m (31 December 2016: £4.5m). 485 policies invested in the fund (31 December 2016: 498), of which 36 (31 December 2016: 37) were paying premiums (for a total of approximately £10,000 per annum (31 December 2016: £10,000)).

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:	2.94% pa
Rate of return on cash:	0.47% pa
Discount rate:	0.30% 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 2017 was £0.2m (31 December 2016: £0.3m).

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 2017 was £10.0m (31 December 2016: £9.1m).

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 2017 was £0.1m (31 December 2016: £0.1m).

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 2017 was £0.3m (31 December 2016: £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 2017 is £0.1m (31 December 2016: £0.2m).

Sweden

(i) Basis

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 following Finansinspektionen guidelines.

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.

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 claims 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

31 Insurance contract provisions (continued)

(c) Basis and assumptions for calculating insurance contract provisions (continued)

Sweden (continued)

(ii) Principal assumptions:

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.

(iii) Analysis of claims development – gross

	2012 £000	2013 £000	2014 £000	2015 £000	2016 £000	2017 £000
Estimate of ultimates						
End of accident year	27,889	29,240	28,798	28,926	34,712	32,303
One year later	18,710	23,494	21,971	22,047	25,341	
Two years later	17,861	20,775	18,670	19,617		
Three years later	16,997	18,936	15,656			
Four years later	15,369	17,090				
Five years later	14,813					
Current estimate of ultimate claims	14,813	17,090	15,656	19,617	25,341	32,303
Cumulative payments	(12,194)	(13,258)	(8,964)	(9,055)	(10,454)	(7,009)
In balance sheet	2,620	3,832	6,692	10,562	14,888	25,294
Provision for prior years						17,592
Liability in balance sheet						81,479

Analysis of claims development – net

	2012 £000	2013 £000	2014 £000	2015 £000	2016 £000	2017 £000
Estimate of ultimates						
End of accident year	10,367	11,644	13,895	11,078	11,127	11,406
One year later	5,389	7,686	7,419	5,993	6,961	
Two years later	4,860	6,873	4,722	5,181		
Three years later	4,918	4,070	3,628			
Four years later	2,813	3,414				
Five years later	2,759					
Current estimate of ultimate claims	2,759	3,414	3,628	5,181	6,961	11,406
Cumulative payments	(2,014)	(2,331)	(1,537)	(1,858)	(2,063)	(1,363)
In balance sheet	745	1,083	2,092	3,323	4,899	9,383
Provision for prior years						7,623
Liability in balance sheet						29,806

Netherlands (Waard Group)

(i) Basis

For protection policies insurance contract provisions comprise a technical reserve for future claims and a claim reserve for those not settled to completion at the reporting date.

For general insurance contracts an unearned premium reserve reflecting the non-expired term of contract is held plus a claims provision.

For insurance contracts where the policy value reflects the value of supporting assets (unit-linked contracts) the Insurance Contract Provision equals the value of assets held.

(ii) Principal assumptions

The technical reserve uses assumptions for mortality, expenses and discounting that were used in the contract pricing, reflecting a book reserve approach. The continued appropriateness of these assumptions are assessed by undertaking a liability adequacy test.

Claims reserves for general insurance business in Waard Schade contain assessment of those Incurred But Not Reported (IBNR) which are regularly updated reflecting analysis of recent reporting patterns.

Netherlands (Scildon)

(i) Basis

For insurance contracts where the policy value reflects the value of supporting assets (unit-linked contracts) the Insurance Contract Provision equals the value of assets held.

For other policies, a discounted value of claims/benefits is used.

(ii) Principal assumptions

The technical reserve uses assumptions for mortality, expenses and discounting that were used in the contract pricing, reflecting a book reserve approach.

For the annuity portfolio mark to market interest assumptions are used. Term policies written after 2015 are reserved on best estimate market value reserves.

(d) Sensitivity to changes in assumptions

Impact on reported profits and equity to changes in key variables:

	CA Change in net of tax profits and equity		Scildon Change in net of tax profits and equity		Movestic Change in net of tax profits and equity	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Change in variable						
100 basis point increase credit spreads	n/a	n/a	(19.2)	–	n/a	n/a
100 basis point increase in Investment return	(1.1)	(2.0)	(30.5)	–	n/a	n/a
100 basis point decrease in Investment return	(1.7)	(0.5)	33.1	–	n/a	n/a
10% increase in mortality/morbidity	1.5	1.0	(0.1)	–	n/a	n/a
10% increase in mortality alone	2.9	1.6	(0.1)	–	n/a	n/a
10% increase in morbidity alone	(0.6)	(0.7)	–	–	n/a	n/a
10% increase in policy maintenance expenses	(4.4)	(4.7)	–	–	n/a	n/a
5% increase in loss ratio						
Gross before reinsurance	n/a	n/a	–	–	(3.2)	(3.2)
Net after reinsurance	n/a	n/a	–	–	(1.2)	(1.1)
5% decrease in loss ratio						
Gross before reinsurance	n/a	n/a	–	–	3.2	3.2
Net after reinsurance	n/a	n/a	–	–	1.2	1.1
1% increase in discount rate						
Gross before reinsurance	n/a	n/a	–	–	–	–
Net after reinsurance	n/a	n/a	–	–	–	–
1% decrease in discount rate						
Gross before reinsurance	n/a	n/a	–	–	–	–
Net after reinsurance	n/a	n/a	–	–	–	–

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

31 Insurance contract provisions (continued)

UK businesses (CA)

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 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 31(d) table presented 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.

The 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 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 and subject to treating customers fairly.

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.

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.

Dutch business (Waard Group)

The most material sensitivity within Waard Group is interest rates. Due to the fact that Waard measures its insurance contract liabilities using historical rates of interest, a rise in interest rates results in a fall in the value of fixed-interest assets with no change in the value of liabilities. The impact on net of tax profits and equity at 2017 is negative £2.1m.

Dutch business (Scildon)

The key sensitivity within Scildon is interest rates. Similarly to Waard Group, Scildon measures the majority of its insurance contract liabilities using historical rates of interest. This means that a rise in interest rates results in a fall in the value of fixed-interest assets with only a small reduction in the value of liabilities. The impact on net of tax profits and equity at 2017 is negative £30.5m.

32 Investment contracts at fair value through income and amounts deposited with reinsurer

Analysis by operating segment

31 December		2017			2016	
	Investment contract liability £000	Amount deposited with reinsurer £000	Net £000	Investment contract liability £000	Amount deposited with reinsurer £000	Net £000
CA	776,551	38,776	737,775	758,559	37,437	721,122
Movestic	2,643,722	–	2,643,722	2,269,710	–	2,269,710
Total	**3,420,273**	**38,776**	**3,381,497**	**3,028,269**	**37,437**	**2,990,832**
Current	797,615	38,776	758,839	108,795	372	108,423
Non-current	2,662,658	–	2,622,658	2,919,474	37,065	2,882,409
Total	**3,420,273**	**38,776**	**3,381,497**	**3,028,269**	**37,437**	**2,990,832**

The fair values of the groups' investment contract liabilities have been disclosed according to a three-level valuation hierarchy in note 25.

33 Liabilities relating to policyholders' funds held by the group

Unit-linked
31 December

	2017 £000	2016 £000
Balance at 1 January	**229,397**	**189,919**
Deposits received	52,449	44,276
Fees deducted from account balances	(2,095)	(1,669)
Investment yield	10,453	13,544
Foreign exchange translation difference	1,093	23,621
Other movements	(25,568)	(40,294)
Balance at 31 December	**265,729**	**229,397**
Current	16,210	13,993
Non-current	249,519	215,404
Total	**265,729**	**229,397**

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 25.

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 25.

34 Borrowings

Group
31 December

	2017 £000	2016 £000
Bank loan	89,457	52,697
Amount due in relation to financial reinsurance	39,745	34,146
Total	**129,202**	**86,843**
Current	32,379	61,471
Non-current	96,823	25,372
Total	**129,202**	**86,843**

Company
31 December

	2017 £000	2016 £000
Bank loan	**89,457**	**52,697**
Current	22,029	52,697
Non-current	67,428	–
Total	**89,457**	**52,697**

The bank loan as at 31 December 2017 comprises the following:

- on 3 April 2017 tranche one of a new facility was drawn down, amounting to £40.0m. This facility is unsecured and is repayable in 10 six-monthly instalments on the anniversary of the draw down date. The outstanding principal on the loan bears interest at a rate of 2.00 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. The proceeds of this loan facility were utilised, together with existing group cash, to repay in full, the pre-existing loan facilities totalling £52.8m.
- on 3 April 2017 tranche two of the new loan facility was drawn down, amounting to €71.0m. As with tranche one, this facility is unsecured and is repayable in 10 six-monthly instalments on the anniversary of the draw down date. The outstanding principal on the loan bears interest at a rate of 2.00 percentage points above the European Inter-Bank Offer Rate and is repayable over a period which varies between one and six months at the option of the borrower.

The fair value of the sterling denominated bank loan at 31 December 2017 was £35.0m (31 December 2016: £52.8m).

The fair value of the euro denominated bank loan at 31 December 2017 was £55.0m (31 December 2016: nil).

The fair value of amounts due in relation to financial reinsurance was £42.2m (31 December 2016: £34.4m).

Bank loans are presented net of unamortised arrangement fees. Arrangement fees are recognised in profit or loss using the effective interest rate method.

35 Defined benefit obligations

Scildon operates a defined benefit pension scheme for the benefit of its present and past employees. A summary of the scheme assets and liabilities as at the balance sheet date and the movements in the post-acquisition period are provided below.

The amount included in the balance sheet arising from the obligations in respect of the scheme is as follows:

As at period ended	31 December 2017 £000	6 April 2017 £000
Present value of defined benefit obligations	47,459	44,864
Fair value of plan assets	(48,354)	(45,813)
Surplus	(895)	(949)
Effect of asset ceiling test	895	949
Net liability arising from defined benefit obligation	**–**	**–**

As at 31 December 2017, there was a surplus in the Pension Fund of £0.9m. The Scildon defined benefit scheme is accounted for under the provisions of IAS 19. As such, pension surplus assets are not recognisable on the face of the balance sheet and as a consequence are subject to an asset ceiling test, which effectively reduces the asset value to nil. The company is unable to recognise the surplus position in terms of potential refunds of past contributions made or through lower future contributions to the scheme.

Amounts recognised in income in respect of the scheme are as follows:

Post acquisition movement	2017 £000
Service cost:	
– Current service cost	1,413
– Past service cost	(438)
Net interest income	(3)
Components of defined benefit costs recognised in profit or loss	**972**

The costs charged to the profit and loss account are recorded under operating expenses as personnel costs.

Amounts recognised in the statement of comprehensive income are as follows:

Post acquisition movement	2017 £000
The return on plan assets (excluding amounts included in net interest expense)	(365)
Actuarial gains and losses arising from changes in assumptions	626
Actuarial gains and losses arising from experience adjustments	794
Adjustment for the effect of asset ceiling test	(895)
Foreign exchange translation	5
Tax effect	(41)
Total profit for the year not recognised in income	**124**

Movements in the present value of defined benefit obligations in the period since acquisition were as follows:

Post acquisition movement	2017 £000
Balance 6 April	44,864
Current service cost	1,413
Interest cost	648
Contributions from the plan participants	270
Actuarial gains and losses arising from changes in assumptions	(626)
Actuarial gains and losses arising from experience adjustments	(794)
Benefits paid	(329)
Individual settlements	640
Past service pension costs	(438)
Foreign exchange translation	1,811
Balance 31 December	**47,459**

Movements in the fair value of plan assets in the period since acquisition were as follows:

Post acquisition movement	2017 £000
Balance 6 April	45,813
Benefits paid	(329)
Contributions from the employer	(176)
Contributions from the plan participants	270
Assets distributed on settlements	640
Interest income	651
The return on plan assets (excluding amounts included in net interest expense)	(365)
Foreign exchange translation	1,850
Balance 31 December	**48,354**

The cost of defined benefit pension amounts:

Post acquisition movement	2017 £000
Pension costs	
Current service pension costs	1,413
Past service pension costs	–
Total pension costs	**1,413**
Net interest	
Interest cost on the present value of promised retirement benefits	648
Interest income on assets	(651)
Interest costs by applying 'Asset Ceiling'	–
Net interest on the net liability defined benefit	(3)
Special events	–
Past service cost	(438)
Total charged to profit and loss account	**972**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

35 Defined benefit obligations (continued)

The principal actuarial assumptions applied to the scheme valuation are as follows:

	31 December 2017	6 April 2017
Discount rate	1.90%	1.90%
Interest income on assets	1.90%	1.90%
General salary increases	2.00%	2.00%
Deferred pension increases	0.60%	0.60%
Inflation	2.00%	2.00%

From the point of acquisition to 31 December 2017, there has been no change to the discount rate.

Distribution of plan assets:

	31 December 2017	6 April 2017
Equity type instruments	8,253	7,413
Fixed interest instruments – Government bonds	39,527	37,484
Cash	196	742
Other	378	174
Total	**48,354**	**45,813**

Period ended 31 December		**Quoted market price in an active market**	
	2017 £000	**Not quoted**	**Quoted**
Equity type instruments	8,253	–	8,253
Fixed interest instruments – Government bonds	39,527	–	39,527
Cash	196	196	–
Other	378	378	–
Total	**48,354**	**574**	**47,780**

The plan assets do not include investments that are issued by the company and do not include assets used by the company.

Post acquisition movement	**2017 £000**
Actual return on plan assets	286

The risks faced by the company in connection with the pension commitments are determined by the duration of these obligations. The table below shows how these obligations are distributed among active and non-active participants.

As at 31 December 2017	Cash value of defined benefit	Duration
Active members	26,264	29.5
Deferred members	10,461	24.4
Wholly or partially disabled members	1,908	18.6
Pensioners	8,826	12.0
Total	**47,459**	**24.7**

The present value of the defined benefit obligations is sensitive to a change in the assumptions used. The table below shows the sensitivity of the value of pension rights and service costs, to changes in the underlying assumptions used:

As at 31 December 2017	Change	Defined benefit obligation change	Funding cost change
Discount rate			
Plus	0.50%	(5,364)	(309)
Minus	0.50%	6,324	373
Salary increase			
Plus	0.50%	792	89
Minus	0.50%	(783)	(88)
Mortality			
Age set back	1 year	1,566	67

The pension fund holds investments which take account of the risk profile of the underlying scheme liabilities, as part of the asset and liability management employed by the scheme.

The employer contribution expected to be paid in respect of 2018 is £1.9m.

Risks associated with the Scildon defined benefit scheme are not considered by the group to be material.

36 Deferred tax assets and liabilities

Deferred tax liabilities comprise:

31 December	2017 £000	2016 £000
Net deferred tax liabilities:		
CA and other group activities	(2,976)	(4,476)
Movestic	(302)	(387)
Waard Group	(455)	(557)
Scildon	(19,061)	–
Total	**(22,794)**	**(5,420)**
Current	(1,184)	(916)
Non-current	(21,610)	(4,504)
Total	**(22,794)**	**(5,420)**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

36 Deferred tax assets and liabilities (continued)

CA and other group activities

(a) Recognised deferred tax assets and liabilities

31 December	2016 Assets/ (liabilities) £000	(Charge) credit in year £000	2017 Assets/ (liabilities) £000
Profit arising on transition to new tax regime	(1,237)	229	(1,008)
Deferred acquisition costs	(469)	81	(388)
Deferred income	877	(138)	739
Acquired value in force	(3,849)	1,192	(2,657)
Unrealised and deferred investment gains	(23,042)	(20)	(23,062)
Excess expenses of management	23,042	20	23,062
Share-based payments	202	136	338
Total	**(4,476)**	**1,500**	**(2,976)**
Comprising:			
Net deferred tax liabilities	(4,476)	1,500	(2,976)
Total	**(4,476)**	**1,500**	**(2,976)**

31 December	2015 Assets/ (liabilities) £000	(Charge) credit in year £000	2016 Assets/ (liabilities) £000
Profit arising on transition to new tax regime	(1,507)	270	(1,237)
Deferred acquisition costs	(572)	103	(469)
Deferred income	1,052	(175)	877
Acquired value in force	(5,167)	1,318	(3,849)
Unrealised and deferred investment gains	(14,859)	(8,183)	(23,042)
Excess expenses of management	14,859	8,183	23,042
Share-based payments	73	129	202
Total	**(6,121)**	**1,645**	**(4,476)**
Comprising:			
Net deferred tax liabilities	(6,121)	1,645	(4,476)
Total	**(6,121)**	**1,645**	**(4,476)**

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	2017 £000	2016 £000
Income tax credit	**1,500**	**1,645**

(b) Items for which no deferred tax asset is recognised

31 December	2017 £000	2016 £000
BLAGAB transitional amounts	2,382	2,858
Unrelieved expenses	87,136	117,517
Total	**89,518**	**120,375**

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. The movement in this balance reflects an increase in deferred deemed gains on Collective Investment Schemes in the period, which has decreased the unrelieved expenses at the balance sheet date.

Movestic
Recognised deferred tax assets and liabilities
As at the balance sheet date, Movestic had a recognised deferred tax liability of £0.3m (31 December 2016: £0.4m), in respect of fair value adjustments arising upon acquisition. Unrecognised deferred tax assets of £0.2m existed at the balance sheet date in respect of corporation tax recoverable (31 December 2016: £0.1m).

Waard Group
Recognised deferred tax assets and liabilities

31 December	2016 assets/ (liabilities) £000	Arising on business combination £000	(Charge) /credit in year £000	Foreign exchange translation difference £000	2017 Assets/ (liabilities) £000
Fair value adjustment on acquisition	(1,378)	–	(165)	(45)	(1,258)
Valuation differences	821	–	(45)	27	803
Total	**(557)**	**–**	**120**	**(18)**	**(455)**
Comprising:					
Net deferred tax liabilities	(557)	–	120	(18)	(455)
Total	**(557)**	**–**	**120**	**(18)**	**(455)**

Scildon
Recognised deferred tax assets and liabilities

31 December	Arising on business combination £000	(Charge) /credit in year £000	Recognised through equity £000	Foreign exchange translation difference £000	2017 Assets/ (liabilities) £000
Fair value adjustment on acquisition	(13,634)	(322)	–	(555)	(14,511)
Deferred acquisition costs	6,587	(708)	–	262	6,141
Defined benefit pension scheme obligations	139	(102)	(41)	4	–
Valuation differences on technical provisions	(5,488)	(453)	–	(222)	(6,163)
Valuation differences on investments at FV through P&L	707	24	–	29	760
Untaxed reserves	(4,136)	(401)	–	(168)	(4,705)
Property and equipment	(560)	30	(30)	(23)	(583)
Total	**(16,385)**	**(1,932)**	**(71)**	**(673)**	**(19,061)**
Comprising:					
Net deferred tax liabilities	(16,385)	(1,932)	(71)	(673)	(19,061)
Total	**(16,385)**	**(1,932)**	**(71)**	**(673)**	**(19,061)**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

37 Reinsurance payables

Payable to reinsurers 31 December	2017 £000	2016 £000
Payables in respect of insurance contracts	10,746	6,264
Payables in respect of investment contracts	14	15
Reinsurers' share of deferred acquisition costs and claims deposits	646	620
Total	**11,406**	**6,899**
Current	11,406	6,179
Non-current	–	720
Total	**11,406**	**6,899**

The carrying value of payables to reinsurers is a reasonable approximation of fair value.

38 Payables related to direct insurance and investment contracts

31 December		2017			2016	
	Gross £000	Reinsurance £000	Net £000	Gross £000	Reinsurance £000	Net £000
Accrued claims	66,785	25,888	40,897	57,781	19,307	38,474
Intermediaries' liabilities	3,650	–	3,650	635	–	635
Policyholder premium liabilities	23,378	–	23,378	418	–	418
Other	3,350	–	3,350	2,582	–	2,582
Total	**97,163**	**25,888**	**71,275**	**61,416**	**19,307**	**42,109**
Current	97,163	25,888	71,275	61,416	19,307	42,109
Non-current	–	–	–	–	–	–
Total	**97,163**	**25,888**	**71,275**	**61,416**	**19,307**	**42,109**

The carrying value of payables related to the direct insurance and investment contracts is a reasonable approximation of fair value.

39 Deferred income

31 December	2017 £000	2016 £000
Balance at 1 January	**5,438**	**6,212**
Release to income	(737)	(774)
Balance at 31 December	**4,701**	**5,438**
Current	634	694
Non-current	4,067	4,744
Total	**4,701**	**5,438**

The release to income is included in fees and commission income (see note 9).

40 Other payables

Group
31 December

	2017 £000	2016 £000
Accrued expenses	13,876	11,931
VAT	53	103
Employee tax	3,240	824
Other	27,815	10,799
Total	**44,984**	**23,657**
Current	44,984	23,657
Non-current	–	–
Total	**44,984**	**23,657**

Company
31 December

	2017 £000	2016 £000
Accrued expenses	2,274	3,275
Other	2,377	1,510
Total	**4,651**	**4,785**
Current	4,651	4,785
Non-current	–	–
Total	**4,651**	**4,785**

The carrying value of other payables is a reasonable approximation of fair value.

41 Share capital and share premium

Group
31 December

	2017		2016	
	Number of shares issued	Share capital £000	Number of shares issued	Share capital £000
Share capital	**149,885,761**	**43,766**	**149,885,761**	**43,766**
		Share premium £000		Share premium £000
		141,983		**142,058**

The number of shares in issue at the balance sheet date included 86,040 shares held in treasury (31 December 2016: 147,535).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

41 Share capital and share premium (continued)

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 £41.5m, 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.

On 15 December 2016, 23.3m new shares were issued to new and existing shareholders, as part of a fund raising exercise in respect of the proposed acquisition of LGN. The gross amount of new equity raised was £70.0m. Transaction costs of £3.3m were incurred in respect of the fund raising and have been deduced from equity.

Company 31 December	2017 Number of shares	2017 Share capital £000	2016 Number of shares	2016 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	149,885,761	7,494	149,885,761	7,494
		Share premium £000		**Share premium £000**
		141,983		**142,058**

The number of shares in issue at the balance sheet date included 86,040 shares held in treasury (31 December 2016: 147,535).

42 Treasury shares

Group and company 31 December	2017 £000	2016 £000
Balance at 31 December	**98**	**161**

43 Other reserves

Group 31 December	2017 £000	2016 £000
Capital redemption reserve	50	50
Foreign exchange translation reserve	27,614	19,250
Balance at 31 December	**27,664**	**19,300**

Company 31 December	2017 £000	2016 £000
Capital redemption reserve	**50**	**50**

44 Retained earnings

Group 31 December	2017 £000	2016 £000
Retained earnings attributable to equity holders of the parent company comprise:		
Balance at 1 January	**188,598**	**177,021**
Profit for the year	78,434	35,280
Revaluation of pension obligations	124	–
Share based payment	669	478
Dividends		
Final approved and paid for 2015	–	(15,586)
Interim approved and paid for 2016	–	(8,595)
Final approved and paid for 2016	(19,002)	–
Interim approved and paid for 2017	(10,482)	–
Balance at 31 December	**238,341**	**188,598**

The interim dividend in respect of 2015, approved and paid in 2016 was paid at the rate of 6.80p per share. The final dividend in respect of 2016, approved and paid in 2017, was paid at the rate of 12.69p per share so that the total dividend paid to the equity shareholders of the parent company in respect of the year ended 31 December 2016 was made at the rate of 19.49p per share.

A final dividend of 13.07p per share in respect of the year ended 31 December 2017 payable on 23 May 2018 to equity shareholders of the parent company registered at the close of business on 13 April 2018, the dividend record date, was approved by the directors after the balance sheet date. The resulting total final dividend of £19.6m has not been provided for in these financial statements and there are no income tax consequences.

The interim dividend in respect of 2017, approved and paid in 2017, was paid at the rate of 7.00p per share to equity shareholders of the parent company registered at the close of business on 8 September 2017, the dividend record date.

The following summarises dividends per share in respect of the year ended 31 December 2017 and 31 December 2016:

Year ended 31 December	2017 P	2016 P
Interim – approved and paid	7.00	6.80
Final – proposed/paid	13.07	12.69
Total	**20.07**	**19.49**

Company Year ended 31 December	2017 £000	2016 £000
Balance at 1 January	**164,921**	**166,313**
Profit for the year	22,465	22,311
Share based payment	669	478
Dividends paid		
Final approved and paid for 2015	–	(15,586)
Interim approved and paid for 2016	–	(8,595)
Final approved and paid for 2016	(19,002)	–
Interim approved and paid for 2017	(10,482)	–
Balance at 31 December	**158,571**	**164,921**

Details of dividends, approved and paid, are set out in the 'group' section above.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

45 Employee benefit expense, including directors

Year ended 31 December	CA £000	Movestic £000	Waard Group £000	Scildon £000	Other group activities £000	2017 £000	2016 £000
Wages and salaries	2,104	9,061	1,084	7,343	3,190	22,782	12,248
Social security costs	255	3,295	153	986	387	5,076	3,679
Pension costs–defined contribution plans	137	1,804	105	–	209	2,255	2,071
Pension costs–defined benefit plans	–	–	–	806	–	806	–
Total	**2,496**	**14,160**	**1,342**	**9,135**	**3,786**	**30,919**	**17,998**
Monthly average number of employees							
Company						34	29
Subsidiaries						295	172
Total						**329**	**201**

Directors
Note 46 provides detail of compensation to directors of the company.

UK
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 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. Options have been granted to executive directors in the period, in relation to the share-based payment components of the new executive incentive schemes that was introduced under the 2014 Terms. Further details can be found in the Directors' Remuneration Report Section and in note 46 – Share Based Payments on page 167.

Waard
The Waard business participates in a defined contribution scheme.

Scildon
Scildon has a defined benefit plan. The pension scheme is an indexed average pay scheme with a pension of 1.7% per year of service. Indexation is conditional since 1 January 2013. The pension scheme is administered by Stichting Pensionfonds Legal & General Nederland. The company has agreed to contribute to the premium for the unconditional part of the pension. Apart from the obligations which may arise from the collective agreement provisions, the company is not obliged to make additional contributions to the claims brought under the pension fund. The company is not entitled to refunds or discounts.

Part of the plan consists a defined contribution scheme. The company pays a contribution to the scheme and subsequently has no further financial obligations with respect to this part of the scheme. This contribution is recognised as an expense when paid.

The costs of the defined benefit plan are calculated using the projected unit credit method. This means that the cost of providing pensions charged to the income statement are placed over the service lives of employees, according to actuarial calculations. The obligations are calculated as the difference between the present value of pension obligations, net of the fair value of the existing plan assets.

The present value of pension liabilities is determined by discounting the expected future retirement benefits at the rate of return on high quality corporate bonds in euros, which have a similar remaining period to when the pension payments are expected to be incurred. Any deficiency is recognised as a liability in the consolidated balance sheet. Any surplus is recognised as a receivable. A claim however, will only be considered if the company can enforce law in the form of refunds or reductions in future contributions.

Actuarial gains and losses arising from deviations from expected outcomes are recognised as revaluations under IFRS through other comprehensive income and recognised directly in equity.

The company commissions Milliman to produce an annual scheme valuation report. The last available valuation report was as at 31 December 2017.

Further information is shown in note 35 Defined benefit obligations.

Movestic

The Swedish business participates in a combined defined benefit and defined contribution scheme operated by Försäkringsbranschens Pensionskassa, 'FPK' (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 1971 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 1972 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 2016, totalled £3.1m. During 2017, further contributions of £0.6m were made.

The employers within the Scheme are collectively responsible 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 2016.

The annual report states that the Scheme's surplus is £162.5m (£117.6m as at 31 December 2016).

As at 31 December 2016, the fund had assets under management of £1.3bn (£1.3bn as at 31 December 2016). During 2016, there have been 126 (129) employer insurance companies participating in the Scheme and 26,000 (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.

46 Share-based payments

The group issues equity-settled share-based payments to the two executive directors based on the 2014 Terms. Equity settled share-based payments are measured at fair value at the date of the grant, and expensed on a straight-line over the vesting period, based on the group's estimate of shares that will eventually vest. The executive bonus scheme consists of two components:

(a) Short-Term Incentive Scheme (STI)

(b) Long-Term Incentive Scheme (LTI)

The STI scheme is based upon a one year performance period measured against IFRS, EcV operating profit and strategic group objectives. In relation to 2017, upon meeting the necessary performance targets, the company granted an award in the form of a right to receive a cash amount of up to 75% of the gross salary. In the event that the gross cash payment due is greater than £20,000, a mandatory 35% of the cash award was deferred into shares, which had a vesting period of three years. Therefore the award was 65% settled in cash and 35% settled by a share option award, which cannot be exercised for three years.

Under the LTI scheme, options are granted with a vesting period of three years. These awards are subject to performance conditions tied to the company's financial performance in respect of growth in Economic Value and total shareholder return ('TSR').

For schemes with market performance criteria, the number of options expected to invest is adjusted only for expectations of leavers prior to vesting. Fair value of the options is measured by use of the Monte Carlo model at the issuing date.

The LTI Scheme also contains a target of Economic Value growth. As this is a non-market performance condition, the number of options expected to vest is recalculated at each balance sheet date based on expectations of performance against target. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in reserves.

If the options remain unexercised after a period of 10 years from the date of grant, the options expire. Furthermore, options are forfeited if the employee leaves the group before options vest and is deemed to be a 'bad' leaver.

(a) 2017 award under the Short-Term Incentive Scheme (STI)

Details of the short-term incentive awards made in the year are as follows:

2017 Short-Term Incentive Scheme Awards made in year	2017 £000	2016 £000
Amount paid as cash bonus through the income statement (65%)	376	521
Amount deferred into shares for three years and subject to forfeiture (35%)	203	281
Total bonus award for the year	579	802
Amount of deferred expense recorded in the current year	48	66

The deferred share award will be made following the end of the performance period by the Remuneration Committee. The deferred amount will be divided by the share price on the award date and the number of share awards will be awarded. The share awards will be accounted for per IFRS 2, under Equity Settled share-based payments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

46 Share-based payments (continued)

(b) 2017 award made under the Long-Term Incentive (LTI) Scheme

In April 2017, the group granted 174,000 nil priced share options with a vesting period of three years. These awards were subject to performance conditions tied to the company's financial performance in respect of growth in embedded value and total shareholder return ('TSR').

The fair value of the non-market base condition was determined to be 382.75p, which was the share price as at 28 April 2017, the grant date of the options.

Details of the share options outstanding during the year are as follows:

2017 Long-Term Incentive Scheme

	Options number 000	Weighted average exercise price £
Outstanding at the beginning of the year	–	–
Granted during the year	174	–
Outstanding at the end of the year	174	–
Exercisable at the end of the year	–	–

The weighted average contractual life is 10 years.

The inputs into the Monte Carlo model are as follows:

Valuation method	Monte Carlo
Weighted average share price (pence)	382.75
Weighted average exercise price (pence)	Nil
Weighted average fair value of options granted (pence)	211.73
Expected volatility	26.97
Expected life	3 years
Risk free rate	0.70%
Expected dividend yield	0%

Expected volatility was determined by calculating the historical volatility of the company's share price over the previous 10 years.

The group recognised total expense of £0.1m related to equity-settled share based payments transactions in 2017.

(c) 2016 award made under the Short-Term Incentive (STI) Scheme

The group has recorded an expense of £66,000 with regards to the 35% element that has been deferred over the vesting period.

(d) 2016 award made under the Long-Term Incentive Scheme (LTI)
In April 2016, the group granted 255,000 nil priced share options with a vesting period of three years. These awards were subject to performance conditions tied to the company's financial performance in respect of growth in embedded value and total shareholder return ('TSR').

The fair value of the non-market base condition was determined to be 312.00p, which was the share price as at 28 April 2016, the grant date of the options.

Details of the share options outstanding during the year are as follows:

2016 Long-Term Incentive Scheme

	2017 Options number 000	2017 Weighted average exercise price £	2016 Options number 000	2016 Weighted average exercise price £
Outstanding at the beginning of the year	255	–	–	–
Granted during the year	(34)	–	255	–
Forfeited during the year	–	–	–	–
Exercised during the year	–	–	–	–
Outstanding at the end of the year	221	–	255	–
Exercisable at the end of the year	–	–	–	–

The weighted average contractual life is 10 years.

The inputs into the Monte Carlo model are as follows:

Valuation method	Monte Carlo
Weighted average share price (pence)	312.00
Weighted average exercise price (pence)	Nil
Weighted average fair value of options granted (pence)	179.72
Expected volatility	28.07
Expected life	3 years
Risk free rate	0.86%
Expected dividend yield	0%

Expected volatility was determined by calculating the historical volatility of the company's share price over the previous 10 years.

The group recognised total expense of £0.2m related to equity-settled share based payments transactions in 2017.

(e) 2015 award under the Short-Term Incentive Scheme (STI)
The group has recorded an expense of £40,000 with regards to the 35% element that has been deferred over the vesting period.

(f) 2015 award made under the Long-Term Incentive Scheme (LTI)
In April 2015, the group granted 181,000 nil priced share options with a vesting period of three years. These awards were subject to performance conditions tied to the company's financial performance in respect of growth in embedded value and total shareholder return ('TSR').

The fair value of the non-market base condition was determined to be 319.00p, which was the share price as at 28 April 2015, the grant date of the options.

Details of the share options outstanding during the year are as follows:

2015 Long-Term Incentive Scheme

	2017 Options number 000	2017 Weighted average exercise price £	2016 Options number 000	2016 Weighted average exercise price £
Outstanding at the beginning of the year	181	–	–	–
Granted during the year	–	–	181	–
Forfeited during the year	(16)	–	–	–
Exercised during the year	–	–	–	–
Outstanding at the end of the year	165	–	181	–
Exercisable at the end of the year	–	–	–	–

The weighted average contractual life is 10 years.

46 Share-based payments (continued)

(f) 2015 award made under the Long-Term Incentive Scheme (LTI) (continued)

The inputs into the Monte Carlo model are as follows:

Valuation method	Monte Carlo
Weighted average share price (pence)	319.00
Weighted average exercise price (pence)	Nil
Weighted average fair value of options granted (pence)	187.62
Expected volatility	30.21
Expected life	3 years
Risk free rate	1.07%
Expected dividend yield	0%

Expected volatility was determined by calculating the historical volatility of the company's share price over the previous 10 years.

The group recognised total expense of £0.2m related to equity-settled share based payments transactions in 2017.

(g) 2014 award under the Short-Term Incentive Scheme (STI)

The group has recorded an expense of £21,000 with regards to the 35% element that has been deferred over the vesting period.

(h) 2014 award made under the Long-Term Incentive Scheme (LTI)

In May 2014, the group granted 169,000 nil priced share options with a vesting period of three years. These awards were subject to performance conditions tied to the company's financial performance in respect of growth in embedded value and total shareholder return ('TSR').

Fair value is measured by use of the Monte Carlo model of the TSR condition. The LTI Scheme also contains embedded value growth. As these are non-market performance conditions they are not included in the determination of fair value of share options at the grant date. The fair value of the non-market base condition was determined to be 310.25p, which was the share price as at 20 May 2014, the grant date of the options.

Details of the share options outstanding during the year are as follows:

2014 Long-Term Incentive Scheme	2017 Options number 000	2017 Weighted average exercise price £	2016 Options number 000	2016 Weighted average exercise price £
Outstanding at the beginning of the year	91	–	91	–
Granted during the year	–	–	–	–
Forfeited during the year	(33)	396.74	–	–
Exercised during the year	(58)	–	–	–
Outstanding at the end of the year	–	–	91	–
Exercisable at the end of the year	–	–	–	–

The weighted average contractual life is 10 years.

The inputs into the Monte Carlo model are as follows:

Valuation method	Monte Carlo
Weighted average share price (pence)	310.25
Weighted average exercise price (pence)	nil
Weighted average fair value of options granted (pence)	183.08
Expected volatility	32.10%
Expected life	3 years
Risk free rate	1.46%
Expected dividend yield	0%

Expected volatility was determined by calculating the historical volatility of the company's share price over the previous 10 years.

The group recognised total expense of £31,000 related to equity-settled share based payments transactions in 2017.

47 Earnings per share

Earnings per share are based on the following:

Year ended 31 December	2017	2016
Profit for the year attributable to shareholders (£000)	78,434	35,280
Weighted average number of ordinary shares	149,749,517	127,488,681
Basic earnings per share	52.38p	27.67p
Diluted earnings per share	52.13p	27.56p

The weighted average number of ordinary shares in respect of the years ended 31 December 2017 is based upon 149,885,761 shares in issue less 86,040 own shares held in treasury. The weighted average number of ordinary shares in respect of the years ended 31 December 2017 was based upon 149,885,761 shares in issue less 147,535 own shares held in treasury.

There were 877,000 share options outstanding at 31 December 2017 (2016: 526,000). Accordingly, there is dilution of the average number of ordinary shares in issue in respect of 2016.

48 Operating leases

Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

Operating lease rentals Year ended 31 December	2017 Non-investment properties £000	2017 Motor vehicles £000	2017 Total £000	2016 Non-investment properties £000	2016 Motor vehicles £000	2016 Total £000
Less than one year	922	139	1,061	953	196	1,149
Between one and two years	815	142	957	798	141	939
Between two and five years	60	99	159	868	129	997
More than five years	–	–	–	–	–	–
Expenses recognised in the year in respect of operating leases	**1,071**	**188**	**1,259**	**976**	**146**	**1,122**

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.

49 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.

50 Capital commitments

There were no capital commitments as at 31 December 2017 or as at 31 December 2016.

51 Related parties

(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;

(iv) other companies over which the directors have significant influence; and

(v) transactions with persons related to key management personnel

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

51 Related parties (continued)

(b) Related party transactions

(i) Transactions with key management personnel.

Key management personnel comprise of the directors of the company. Key management compensation is as follows:

	2017 £000	2016 £000
Short-term employee benefits	1,324	1,849
Post-employment benefits	66	84
Total	**1,390**	**1,933**

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:

	2017 £000	2016 £000
Annual bonus scheme (included in the short-term employee benefits above)	**376**	**521**

These amounts have been included in accrued expenses as disclosed in note 40. The amounts payable under the annual bonus scheme were payable within one year.

(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	2017 £000	2016 £000
Recovery of expenses	**3,272**	**3,470**

(iii) Transactions with associate

Movestic Livförsäkring AB and its associate Modernac SA

Year ended 31 December	2017 £000	2016 £000
Reinsurance premiums paid	(9,667)	(9,245)
Reinsurance recoveries received	5,820	4,983
Reinsurance commission received	(2,843)	1,761
	(6,690)	(2,501)
Amounts outstanding as at balance sheet date	**(2,442)**	**(3,570)**

Movestic Livförsäkring AB had the following amounts outstanding at the balance sheet date:

	2017		2016	
	Amounts owed by associate £000	Amounts owed to associate £000	Amounts owed by associate £000	Amounts owed to associate £000
Modernac S.A.	**–**	**2,442**	**–**	**3,570**

These amounts have been included in other payables as disclosed in note 40 and other receivables as disclosed in note 27.

(iv) Transactions with persons related to key management personnel

During the year, the company engaged the professional services of Clare Rimmington, who is related to David Rimmington. Clare Rimmington is an on-line marketing expert with many years of experience developing and managing web based solutions in the financial services sector.

In the year an amount of £20,708 was paid by the company to Clare Rimmington for web-site related consultancy services. These amounts have been included in administration expenses in note 15.

52 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	Ownership interest 31 December 2017	Ownership interest 31 December 2016	Functional Currency
Countrywide Assured plc	United Kingdom	100% of all share capital (1)	100% of all share capital (1)	Sterling
Countrywide Assured Life Holdings Limited	United Kingdom	100% of all share capital	100% of all share capital	Sterling
Countrywide Assured Services Limited	United Kingdom	100% of all share capital	100% of all share capital	Sterling
Countrywide Assured Trustee Company Limited	United Kingdom	100% of all share capital	100% of all share capital	Sterling
Registered address 2nd Floor, Building 4, West Strand Business Park West Strand Road, Preston, Lancashire PR1 8UY				
Movestic Livförsäkring AB	Sweden	100% of all share capital	100% of all share capital	Swedish krona
Movestic Kapitalförvältning AB	Sweden	100% of all share capital (2)	100% of all share capital (2)	Swedish krona
Registered address Box 7853, S-103 99 Stockholm, Sweden				
Modernac S.A.	Luxembourg	49% of all share capital (2)	49% of all share capital (2)	Swedish krona
Registered address BP 593 L-2015 Luxemburg, Luxembourg				
Chesnara Holdings B.V.	Netherlands	100% of all share capital (3)	100% of all share capital (3)	Euro
Waard Leven N.V.	Netherlands	100% of all share capital (4)	100% of all share capital (4)	Euro
Waard Schade N.V.	Netherlands	100% of all share capital (4)	100% of all share capital (4)	Euro
Tadas Verzekering	Netherlands	100% of all share capital (4)	100% of all share capital (4)	Euro
Hollands Welvaren Leven N.V.	Netherlands	100% of all share capital (5)	100% of all share capital (5)	Euro
Registered address Geert Scholtenslaan II 1687 CL Wognum, Netherlands				
Scildon N.V	Netherlands	100% of all share capital (4)	100% of all share capital (4)	Euro
Registered address Laapersveld 68 Hilversum, Netherlands				

(1) Held indirectly through Countrywide Assured Life Holdings Limited.

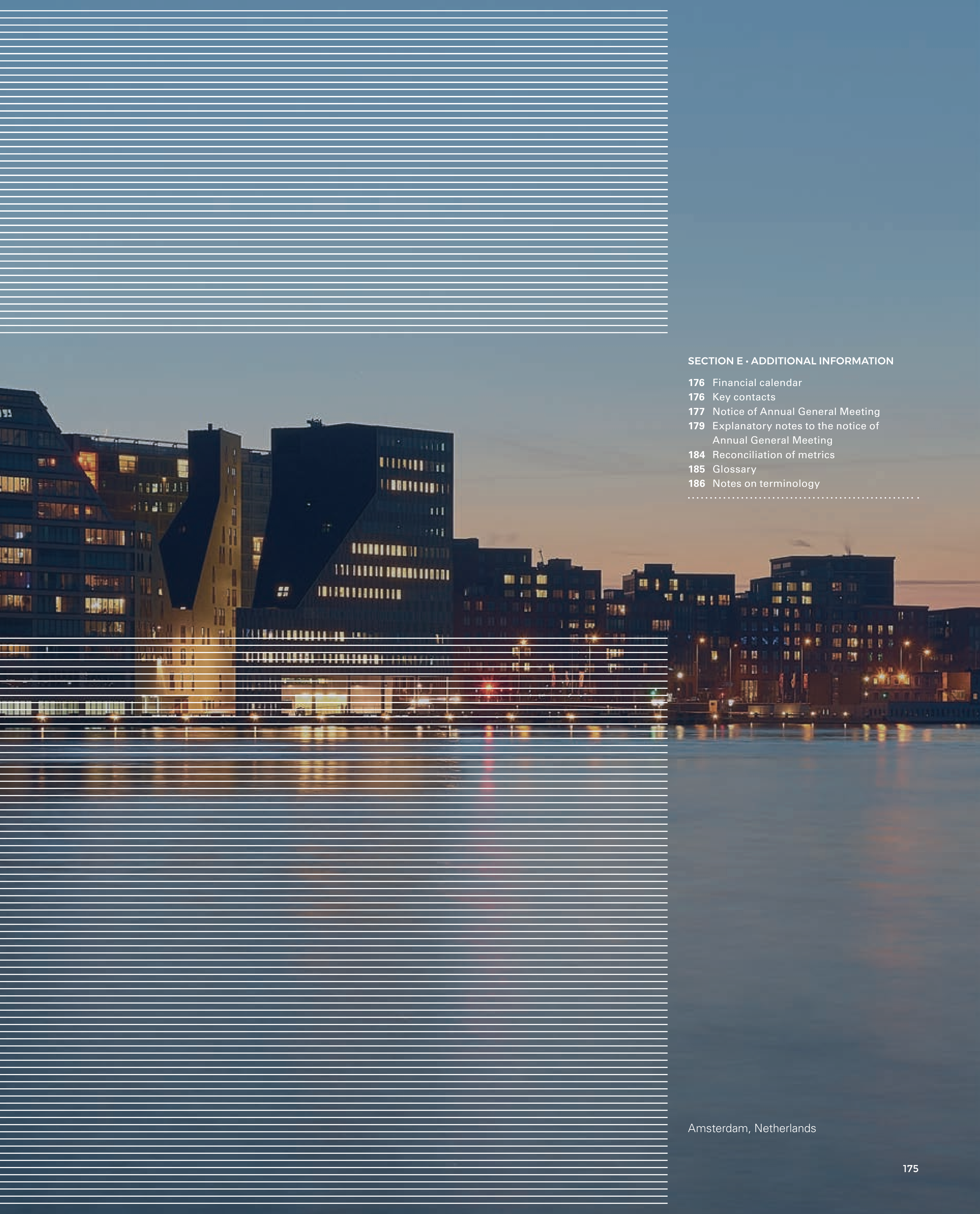
(2) Held indirectly through Movestic Livförsäkring AB.

(3) Company formed on 25 November 2014.

(4) Held indirectly through Chesnara Holdings B.V.

(5) Held indirectly through Waard Leven N.V.

SECTION E: ADDITIONAL INFORMATION



SECTION E • ADDITIONAL INFORMATION

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Amsterdam, Netherlands

FINANCIAL CALENDAR

29 March 2018
Results for the year ended 31 December 2017 announced

12 April 2018
Ex dividend date

13 April 2018
Dividend record date

17 April 2018
Published Report & Accounts issued to shareholders

16 May 2018
Annual General Meeting

23 May 2018
Dividend payment date

30 August 2018
Half year results for the 6 months ending
30 June 2018 announced

KEY CONTACTS

Registered and head office
2nd Floor, Building 4
West Strand Business Park
West Strand Road
Preston
Lancashire
PR1 8UY

Tel: 01772 972050
www.chesnara.co.uk

Advisors
Ashurst LLP
Broadwalk House
5 Appold Street
London
EC2A 2HA

Addleshaw Goddard LLP
One St Peter's Square
Manchester
M2 3DE

Auditor
Deloitte LLP
Statutory Auditor
2 Hardman Street
Manchester
M3 3HF

Registrars
Capita Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent
BR3 4TU

Joint stockbrokers
Panmure Gordon
One New Change
London
EC4M 9AF

Shore Capital Stockbrokers Limited
Bond Street House
14 Clifford Street
London
W1S 4JU

Bankers
National Westminster Bank plc
135 Bishopsgate
London
EC2M 3UR

The Royal Bank of Scotland
8th Floor, 135 Bishopsgate
London
EC2M 3UR

Lloyds Bank plc
3rd Floor, Black Horse House
Medway Wharf Road
Tonbridge
Kent
TN9 1QS

Public relations consultants
FWD
145 Leadenhall Street
London
EC3V 4QT

Corporate advisors
Shore Capital Stockbrokers Limited
Bond Street House
14 Clifford Street
London
W1S 4JU

NOTICE OF THE 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 advisor.

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.

Chesnara plc has a policy of not paying to have access to governance and sustainability analysts' databases on which voting recommendations and reports are produced. We encourage early, open and timely engagement to ensure the accuracy of the information contained in any analysis and reports issued in respect of Chesnara plc.

Company No. 4947166

Notice is given that the 2018 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 2018 at 11am. For the business set out below. Resolutions 1 to 14 inclusive will be proposed as ordinary resolutions and resolutions 15 to 18 inclusive will be proposed as special resolutions.

1. To receive and adopt the audited accounts for the financial year ended 31 December 2017, together with the reports of the directors and auditor thereon.

2. To approve the Directors' Remuneration Report (other than the part of it which contains the Directors' Remuneration Policy) for the year ended 31 December 2017.

3. To declare a final dividend of 13.07 pence per ordinary share for the financial year ended 31 December 2017.

4. To re-elect John Deane as a director.

5. To re-elect David Rimmington as a director.

6. To re-elect Jane Dale as a director.

7. To re-elect Peter Mason as a director.

8. To re-elect Veronica Oak as a director.

9. To re-elect David Brand as a director.

10. To re-elect Mike Evans as a director.

11. 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.

12. To authorise the directors to determine the auditor's remuneration.

13. That, from the passing of this resolution 13 until the earlier of the close of business on 28 June 2019 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 £50,000, with the individual amount authorised for each of (a) to (c) above being limited to £50,000. 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.

14. That the directors be and they are hereby generally and unconditionally authorised in accordance with section 551 of the Companies Act 2006 (the 'Act'), to exercise all the powers of the company, to allot shares in the company and/or to grant rights to subscribe for or to convert any security into shares in the company ('Allotment Rights'):

(a) comprising equity securities up to an aggregate nominal amount of £2,495,637 such amount to be reduced by the nominal amount of any equity securities allotted pursuant to the authority in paragraph (b) below in excess of £2,495,637; and

(b) comprising equity securities (as defined by section 560 of the Act) up to an aggregate nominal amount of £4,991,274 (such amount to be reduced by the nominal aggregate amount of any shares allotted or rights granted pursuant to the authority in paragraph (a) above) in connection with an offer by way of a rights issue:

(i) to holders of ordinary shares in proportion (as nearly as may be practicable) to their respective holdings; and

(ii) to holders of other equity securities as required by the rights of those securities or as the directors otherwise consider necessary,

NOTICE OF THE ANNUAL GENERAL MEETING (CONTINUED)

but subject to such exclusions or other arrangements as the directors may deem necessary or expedient in relation to treasury shares, fractional entitlements, record dates, legal or practical problems in or under the laws of any territory or the requirements of any regulatory body or stock exchange, provided that this authority shall, unless renewed, varied or revoked by the company, expire at the conclusion of the 2018 Annual General Meeting (or, if earlier, at the close of business on the date which is 15 months after the date on which this resolution is passed) save that the company may, before such expiry, make offers of agreements which would or might require securities to be allotted and the directors may allot securities in pursuance of such offer or agreement notwithstanding that the authority conferred by this resolution.

15. That, subject to the passing of resolution 14 in this notice, the directors be and are hereby empowered pursuant to section 570 of the Companies Act 2006 ('the Act') to allot equity securities (as defined in section 560 of the Act) for cash, pursuant to the authority conferred on them by resolution 14 of this notice or by way of a sale of treasury shares as if section 561 of the Act did not apply to any such allotment, provided that this power is limited to:

(a) the allotment of equity securities 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 (other than pursuant to paragraph (a) above) with an aggregate nominal value of £374,346.

16. That, subject to the passing of resolution 14 of this notice and, in addition to the power contained in resolution 15 of this notice, the directors be and are hereby empowered pursuant to section 570 of the Companies Act 2006 ('the Act') to allot equity securities (as defined in section 560 of the Act) for cash, pursuant to the authority conferred on them by resolution 14 of this notice or by way of sale of treasury shares as if section 561 of the Act did not apply to any such allotment, provided that this power is:

(a) limited to the allotment of equity securities up to an aggregate nominal value of £374,346; and

(b) used only for the purposes of financing (or refinancing, if the power is to be exercised within six months after the date of the original transaction) a transaction which the directors determine to be an acquisition or other capital investment of a kind contemplated by the Statement of Principles on Disapplying Pre-Emption Rights most recently published by the Pre-Emption Group prior to the date of the notice of this meeting, and shall expire on the revocation or expiry (unless renewed) of the authority conferred on the directors by resolution 14 of this notice 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 after such expiry and the directors may allot equity securities under any such offer or agreement as if the power had not expired.

17. That the company be and is hereby generally and unconditionally authorised for the purposes of section 701 of the Companies Act 2006 ('the Act') to make one or more market purchases (as defined in section 693(4) of the Act) of ordinary shares in the capital of the company, provided that:

(a) the maximum aggregate number of ordinary shares hereby authorised to be purchased is 14,988,576;

(b) the minimum price (exclusive of expenses) which may be paid for such ordinary shares is its nominal value;

(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 at the conclusion of the company's next Annual General Meeting to be held in 2019 (or, if earlier, at the close of business on 28 June 2019); and

(e) the company may enter into contracts 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

Zoe Kubiak
Company secretary

2nd Floor, Building 4,
West Strand Business Park,
West Strand Road,
Preston
PR1 8UY
28 March 2018

EXPLANATORY NOTES TO THE NOTICE OF ANNUAL GENERAL MEETING

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. You will not receive a form of proxy for the AGM in the post. Instead, you will receive instructions to enable you to vote electronically and how to register to do so. You will still be able to vote in person at the AGM, and may request a physical copy proxy form directly from the registrars, Link Asset Services, 34 Beckenham Road, Beckenham, BR3 4TU (telephone number: 0781 664 0300). The return of the form of proxy will not, however, prevent you from attending the Meeting and voting, in person, should you wish to do so.

3. 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. Members may appoint a proxy online by following the instructions for the electronic appointment of a proxy at www.signalshares.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 11am on Monday 14 May 2018. 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.

4. 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 11am on Monday 14 May 2018, 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.

5. 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.

EXPLANATORY NOTES TO THE NOTICE OF ANNUAL GENERAL MEETING (CONTINUED)

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 close of business on Monday 14 May 2018. 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 23 March 2018 (being the last practicable date prior to the publication of this document), the company's issued share capital consisted of 149,885,761 ordinary shares, carrying one vote each. 83,679 shares were held by the company in treasury. Therefore, the total voting rights in the company as at 23 March 2018 (being the last practicable date prior to the publication of this document) were 149,802,082.

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 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 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.

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 the Directors' Strategic Report. In accordance with the UK Corporate Governance Code 2014 (the 'Code'), the company proposes, as an ordinary resolution, a resolution on its Annual Report and Accounts for the year ended 31 December 2017.

Resolution 2:

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 2017. The Directors' Remuneration Report can be found on pages 62 to 79 of the 2017 Report and Accounts and, for the purposes of this resolution, does not include the parts of the Directors' Remuneration Report containing the Directors' Remuneration Policy set out on pages 73 to 79. The vote on this resolution is advisory only and the directors' entitlement to remuneration is not conditional on it being passed. The Companies Act 2006 requires the Directors' Remuneration Policy to be put to shareholders for approval annually unless the approved policy remains unchanged, in which case it need only be put to shareholders for approval at least every three years. The company is not proposing any changes to the Directors' Remuneration Policy approved at the Annual General Meeting in 2017.

Resolution 3:

Final dividend
The declaration of the final dividend requires the approval of shareholders in general meeting. If the 2018 Annual General Meeting approves resolution 2, the final dividend of 13.07 pence per share will be paid on 23 May 2018 to ordinary shareholders who are on the register of members at the close of business on 13 April 2018 in respect of each ordinary share.

Resolutions 4 – 10 inclusive:

Election and re-election of directors
The company's Articles of Association provide that any director who has not been elected or re-elected by the shareholders at either of the two preceding Annual General Meetings is required to retire at the next annual general meeting. Additionally, the Articles of Association require such further directors to retire at the Annual General Meeting as would bring the total number of directors retiring up to one-third of their number.

Notwithstanding the provisions of the company's Articles of Association, the board of directors has determined that all the directors shall retire from office at this year's Annual General Meeting in line with best practice recommendations of the UK Corporate Governance Code. Each of the directors intends to stand for re-election by the shareholders. Biographical details of each director can be found on pages 50 and 51 of this document. The Chairman confirms that each of the directors proposed continues to make an effective and valuable contribution and demonstrates commitment to their responsibilities. This is supported by the annual performance evaluation that was undertaken recently. The board unanimously recommend that each of these directors be re-elected as a director of the company.

In accordance with the Code, the board has reviewed the independence of its non-executive directors and has determined that they remain fully independent of management. The Code states that whilst the Chairman should, on appointment, meet the Code's independence criteria, thereafter the tests of independence are not appropriate in relation to that post. Peter Mason did meet the Code's independence criteria upon his election as Chairman.

Resolutions 11 and 12:

Re-appointment and remuneration of auditor
In the group's Half-Year Report issued on 31 August 2017, the board announced its intention to put the company's external audit contract out to tender during the second half of 2017. A formal competitive tender process was completed in November, overseen by the group's Audit & Risk Committee. On the recommendation of the Audit & Risk Committee, the board is proposing to shareholders the re-appointment of Deloitte LLP as the company's auditor to undertake the audit of the group's financial statements for the financial year ending 31 December 2018.

Resolution 11, therefore, proposes Deloitte's reappointment as auditor to hold office until the next general meeting at which the company's accounts are laid before shareholders. Resolution 12 authorises the directors to determine the auditor's remuneration. Details of the tender process and the Committee's recommendation are provided in the Audit & Risk Committee's Report on page 82 of this document.

EXPLANATORY NOTES TO THE NOTICE OF ANNUAL GENERAL MEETING (CONTINUED)

Resolution 13:

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 ('the Act') 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, the 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.

Resolution 14:

Power to allot shares
The Companies Act 2006 provides that the directors may only allot shares if authorised by shareholders to do so. The directors current allotment authority is due to lapse at the 2018 Annual General Meeting. The board is, therefore, seeking to renew its authority over shares having an aggregate nominal amount of £2,495,637, representing approximately one-third of the issued ordinary share capital of the company (excluding treasury shares) as at 23 March 2018 (being the latest practicable date prior to the publication of this document). The board is also seeking authority to allot shares having an aggregate nominal amount of £4,991,274, representing approximately two-thirds of the issued share capital of the company (excluding treasury shares) as at 23 March 2018 by way of a rights issue.

The allotment authority sought is in line with the Share Capital Management guidelines issued by the Investment Association. For the avoidance of doubt, the authority sought pursuant to this resolution will give the directors the ability to allot shares (or grant rights to shares) up to a maximum aggregate nominal amount of £4,991,274.

As at 23 March 2018, the company held 83,679 treasury shares, being approximately 0.05% of the total ordinary share capital in issue (calculated exclusive of treasury shares).

The authority will expire at the earlier of the conclusion of the 2019 Annual General Meeting of the company and the close of business on 28 June 2019.

Passing resolution 14 will ensure that the directors have flexibility to take advantage of any appropriate opportunities that may arise. At present the directors have no intention of exercising this authority.

Resolution 15 and 16:

Disapplication of statutory pre-emption rights
The directors are currently authorised, subject to certain limitations, to issue shares for cash without first offering them to existing shareholders in proportion to their existing shareholdings. That authority will expire at the conclusion of the 2018 Annual General Meeting and, in accordance with the Statement of Principles issued by the Pre-Emption Group, resolutions 15 and 16 (which will be proposed as special resolutions) seek to renew the directors' authority to disapply pre-emption rights as referenced below.

Resolution 15, if passed, will allow the directors to (a) allot shares in the company for cash in connection with a rights issue or other pre-emptive offer; and (b) otherwise allot shares in the company for cash up to a maximum aggregate nominal value of £374,346, in each case as if the pre-emption rights of section 561 of the Companies Act 2006 did not apply. This aggregate nominal amount equates to approximately 5% of the issued ordinary share capital of the company (excluding treasury shares) as at 23 March 2018 (being the latest practicable date prior to the publication of this notice of annual general meeting).

Resolution 16 is proposed as a separate special resolution. In line with the Pre-Emptions Group's Statement of Principles, the company is seeking authority, to issue up to an additional 5% of its issued ordinary share capital for cash without pre-emption rights applying. In accordance with the Statement of Principles, the company will only allot shares under this additional authority in connection with an acquisition or specific capital investment (within the meaning given in the Statement of Principles) which is announced contemporaneously with the allotment, or which has taken place in the preceding six-month period and is disclosed in the announcement of the allotment.

The board also confirms its intention to follow the provisions of the Statement of Principles regarding cumulative usage of authorities within a rolling three year period. Those provisions provide that no more than 7.5% of the issued share capital will be issued for cash on a non pre-emptive basis during any rolling three-year period, other than to existing shareholders, without prior consultation with shareholders. This limit excludes any ordinary shares issued pursuant to a general disapplication of pre-emption rights in connection with an acquisition or specified capital investment.

Resolution 17:

Authority to purchase own shares
This resolution, which will be proposed as a special resolution, seeks to renew the company's authority to purchase its own shares. It specifies the maximum number of shares which may be acquired as 10% of the company's issued ordinary share capital (excluding treasury shares) as at 23 March 2018, being the latest practicable date prior to the publication of this document, and specifies the minimum and maximum prices at which shares may be bought.

The directors will only use this authority if, in the light of market conditions prevailing at the time, they believe that the effect of such purchases will be (where such shares are to be purchased for cancellation) to increase earnings per share, and that taking into account other investment opportunities, purchases will be in the best interests of the shareholders generally. Any shares purchased in accordance with this authority will be cancelled or held in treasury for subsequent transfer to an employee share scheme. The directors have no present intention of exercising this authority, which will expire at the earlier of the conclusion of the 2019 Annual General Meeting and the close of business on 28 June 2019.

The company has options and awards outstanding under existing share schemes over an aggregate of 715,417 ordinary 5p shares, representing 0.48% of the company's issued ordinary share capital (excluding treasury shares) as at 23 March 2018 (the latest practicable date prior to the publication of this document). This would represent approximately 0.53% of the company's issued share capital (excluding treasury shares) if the proposed authority being sought at the Annual General Meeting to buy back 14,988,576 ordinary shares was exercised in full (and all of the repurchased ordinary shares were cancelled).

Resolution 18:

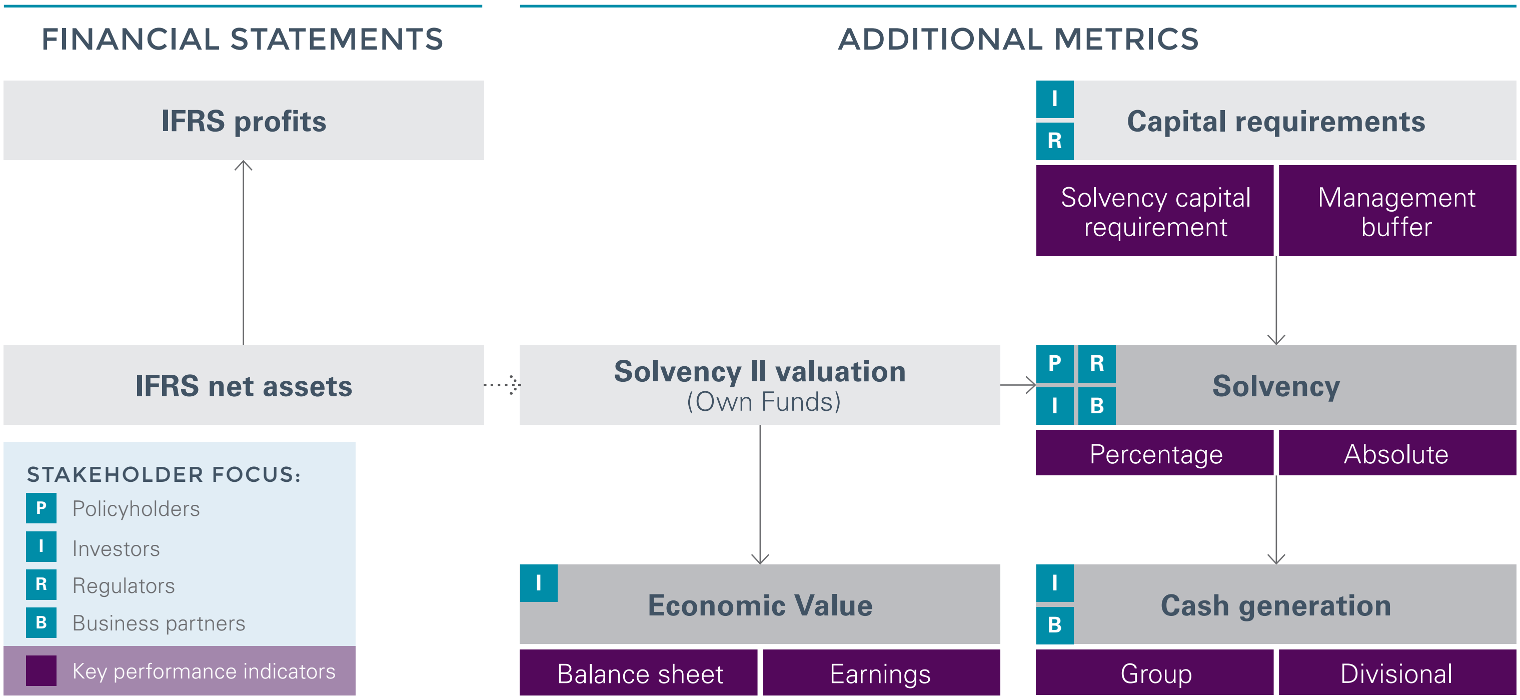
Notice of general meetings
The Companies Act 2006 requires the notice period for general meetings of the company to be at least 21 days, but, as a result of a resolution which was passed by the company's shareholders at last year's Annual General Meeting, the company is currently able to call general meetings (other than an Annual General Meeting) on not less than 14 clear days' notice. In order to preserve this ability, shareholders must once again approve the calling of meetings on not less than 14 clear days' notice. Resolution 17 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 statutory requirements for electronic voting 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.

Directors' recommendation
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 (save in respect of those matters in which they are interested), and consider that all resolutions are in the best interests of the company and its shareholders as a whole.

RECONCILIATION OF METRICS

Within these Report & Accounts and as described on page 10, we use alternative performance measures to detail the position and performance of the group and its divisions. We believe that these measures are of greater commercial relevance than IFRS to the users of the Report & Accounts. The diagram below shows the interaction between the measures:



As shown above, the key interaction between our statutory reporting rules under IFRS and the alternative performance measures is with the Solvency II valuation and the Own Funds balance. A reconciliation from IFRS net assets to Solvency II Own Funds is shown below:

£m	31 Dec 2017	31 Dec 2016	Rationale
Group IFRS net assets	**451.7**	**393.6**	
Removal of intangible assets; AVIF, DAC and DIL	(182.6)	(113.4)	Intangible assets that cannot be sold separately have no intrinsic value under Solvency II rules.
Removal of IFRS reserves, net of reinsurance	7,378.9	5,208.4	Actuarial reserves are calculated differently between the two methodologies and hence IFRS reserves are replaced with Solvency II technical provisions. The main differences in methodology are discussed further below.
Inclusion of SII technical provisions, net of reinsurance	(6,968.9)	(4,949.8)	
Other valuation differences	2.5	4.4	Other immaterial valuation differences
Deferred tax valuation differences	(20.3)	(7.9)	These are the deferred tax impacts as a result of the adjustments above.
Foreseeable dividends	(19.6)	(19.0)	Under Solvency II rules, future 'foreseeable dividends' are required to be recognised within own funds. Under IFRS rules, dividends are recognised when paid.
Ring-fenced surpluses	(26.5)	(10.6)	Solvency II requires that own funds are reduced by any surpluses that are restricted. For Chesnara this relates to surpluses within the two S&P with-profits funds, which are temporarily restricted. These restrictions are removed through periodic capital transfers.
Group Solvency II Own Funds	**615.2**	**505.6**	

The main differences between the two methodologies for calculating actuarial reserves are as follows:
- IFRS reserves continue to be largely based on the Solvency I regimes in place in each of the divisions. The main difference between IFRS and Solvency I is the inclusion of an additional cost of guarantee reserve in each of the with-profit funds in CA plc.
- IFRS assumptions contain prudence margins, whereas the Solvency II assumptions are best estimate.
- Solvency II requires the establishment of contract boundaries to determine whether an insurance obligation or reinsurance obligation is to be treated as existing or future business, with only existing business considered in scope for the calculation of technical provisions.
- Solvency II requires the inclusion of a risk margin to reflect inherent uncertainties within the estimated liabilities.
- Other valuation differences, such as IFRS future liability cash flows are discounted using a valuation rate of interest based on the risk-adjusted yield on held assets, whereas Solvency II uses a swaps-based risk-free discount curve, as prescribed by EIOPA.

GLOSSARY

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.
CA	Countrywide Assured plc.
CALH	Countrywide Assured Life Holdings Limited and its subsidiary companies.
BAU Cash Generation	This represents divisional cash generation plus the impact of non-exceptional group activity.
Cash Generation	This represents the operational cash that has been generated in the period. The cash generating capacity of the group is largely a function of the movement in the solvency position of the insurance subsidiaries within the group, and takes account of the buffers that management has set to hold over and above the solvency requirements imposed by our regulators. Cash generation is reported at a group level and also at an underlying divisional level reflective of the collective performance of each of the divisions prior to any group level activity.
Divisional Cash Generation	This represents the cash generated by the three operating divisions of Chesnara (UK, Sweden and the Netherlands), exclusive of group level activity.
DNB	De Nederlandsche Bank is the central bank of the Netherlands and is the regulator of our Dutch subsidiaries.
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.
Dutch Business	Scildon and the Waard Group, consisting of Waard Leven N.V., Hollands Welvaren Leven N.V., Waard Schade N.V. and Waard Verzekeringen B.V.
EcV	Economic Value is a financial metric that is derived from Solvency II own funds that is broadly similar in concept to European Embedded Value. It provides a market consistent assessment of the value of existing insurance businesses, plus adjusted net asset value of the non-insurance business within the group.
FCA	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.
FSMA	The Financial Services and Markets Act 2000 of England and Wales, as amended.
Group	The company and its existing subsidiary undertakings.
Group Own Funds	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.
Group SCR	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 Solvency	Group Solvency is a measure of how much the value of the company exceeds the level of capital it is required to hold in accordance with Solvency II regulations.
HCL	HCL Insurance BPO Services Limited.
IFRS	International Financial Reporting Standards.
IFA	Independent Financial Adviser.
KPI	Key Performance Indicator.
LGN	LGN or Legal & General Nederland refers to the legal entity Legal & General Nederland Levensverzekering Maatschappij N.V acquired by Chesnara in April 2017.
London Stock Exchange	London Stock Exchange plc.
LTI	Long-Term Incentive Scheme – A reward system designed to incentivise executive directors' long-term performance.
Movestic	Movestic Livförsäkring AB.
Modernac	Modernac SA, an associated company which is 49% owned by Movestic.
New business	The present value of the expected future cash inflows arising from business written in the reporting period.
Official List	The Official List of the Financial Conduct Authority.
Ordinary Shares	Ordinary shares of five pence each in the capital of the company.
Own Funds	Own Funds – 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 company in those capital resources.
ORSA	Own Risk and Solvency Assessment.
PRA	Prudential Regulation Authority.
QRT	Quantitative Reporting Template.
ReAssure	ReAssure Limited.
Resolution	The resolution set out in the notice of General Meeting set out in this document.
RMF	Risk Management Framework.
Scildon	Scildon.
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 and has replaced the Solvency I requirements.
SICAV	A type of open-ended investment fund in which the amount of capital in the fund varies according to the number of investors. Shares in the fund are bought and sold based on the fund's current net asset value.
STI	Short-Term Incentive Scheme – A reward system designed to incentivise executive directors' short-term performance.
SCR	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.
Swedish Business	Movestic and its subsidiaries and associated companies.
S&P	Save & Prosper Insurance Limited and Save & Prosper Pensions Limited.
TCF	Treating Customers Fairly – a central PRA principle that aims to ensure an efficient and effective market and thereby help policyholders achieve fair outcomes.
Total Cash Generation	This represents the absolute cash generation for the period at total group level, comprising divisional cash generation as well as both exceptional and non-exceptional group activity.
TSR	Total Shareholder Return, measured with reference to both dividends and capital growth.
UK	The United Kingdom of Great Britain and Northern Ireland.
UK Business	CA and S&P.

NOTE ON TERMINOLOGY

As explained in Note 8 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; City of Westminster Assurance Company Limited, which was acquired by the group in 2005, 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; and Protection Life Company Limited which was acquired by the group in 2013, the long-term business of which was transferred into Countrywide Assured plc in 2014;
Movestic	which was purchased on 23 July 2009 and comprises the group's Swedish business, Movestic Livförsäkring AB and its subsidiary and associated companies;
The Waard Group	which was acquired on 19 May 2015 and comprises three insurance companies;Waard Leven N.V., Hollands Welvaren Leven N.V. and Waard Schade N.V.; and a service company, Tadas Verzekering; and a service company, Tadas Verzekering; and
Scildon	which was acquired on 5 April 2017; and
Other group Activities	which represents the functions performed by the parent company, Chesnara plc. Also included in this segment are consolidation adjustments.

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Registered and Head Office
Building Four, West Strand Business Park,
West Strand Road, Preston, Lancashire PR1 8UY
T +44 (0)1772 972050 **F** +44 (0)1772 482244
www.chesnara.co.uk

Registered Number: 4947166
Designed by The Chase