SOLVENCY AND FINANCIAL CONDITION REPORT AND QUANTITIATIVE REPORTING TEMPLATES

Financial Year 2017

The Original Holloway Friendly Society Limited
Reporting for the year ended
31 December 2017

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SOLVENCY AND FINANCIAL CONDITION REPORT 2017

Dear Members,

As the people responsible for your Society, the regulator requires us to report to you on the extent to which your benefits are secure in a 'Solvency and Financial Condition Report'. I am delighted to present the report covering the 2017 calendar year.

We ensure that the Society is there for when you need it the most in two main ways. First, we make sure that the Society has a healthy financial position, now and in the future (called 'having sufficient capital'). Second, we make sure that we run the Society properly (called 'having effective governance'). This report describes the work we have done to demonstrate that we have sufficient capital and effective governance.

Running any business involves risk. There is always a risk that that the finances deteriorate or that we fail to run the Society properly. We, the Board, are obliged to take every reasonable step to ensure that we identify and manage the risks that face the Society.

The report is organised in sections. The sections and their contents are set out by the regulator. We have added explanatory boxes throughout this year's report, to explain any new terms as they are used and summarised them in a glossary at the end. We have deliberately avoided technical language as far as possible, but have sometimes had to strike a balance between the regulatory requirements and simplicity of presentation.

I hope you enjoy reading this report. We are always delighted to discuss the Society with our Members at the AGM or at any other time. If you have any comments, questions or suggestions, please do not hesitate to contact me.

Summary

Business and Performance

The Society has performed well during 2017. Sales have grown substantially and overall underwriting performance has been maintained. Investments have performed well, providing income and capital growth. Expenses are in line with the plan. We decided to close Optimal, a subsidiary company that sold group life products, to new business.

Our strategy is to grow by providing useful products to new and existing Members. We sell our products through intermediaries, so it is important that intermediaries know us and feel confident recommending our products. That means we have to be competitive and we have to show how we improve the lives of Members.

We achieve our strategy through our business model. This is jargon for how we will be successful. We think that our best chance of success is to develop new products and product features that Members and intermediaries see as attractive and which are competitively priced. We think we should manage our underwriting and claims handling ourselves, because we have expertise in this work.

A major part of our plan is to build a new administration system. This is a significant project. Much of the planning and design work was done during 2017. The work to build the new system began in 2018. Our plan also includes moving more online and growing Member numbers by developing more relationships with intermediaries.

Finally, given that we are relatively small, our business model includes buying in specialist services which we cannot carry out ourselves.

As a result of our strategy, business model and plans, we expect to grow the value of the Society for our Membership.

Risk Profile

All insurers manage risk. It is management's job to organise the affairs of their firm to ensure that benefits can be paid when the insured event happens and a claim is made.

The regulator is concerned that insurers understand the risks that they face. The regulator has created a formula for insurers to use that calculates the cost of the risks being run, based on the nature of the individual firm. If the firm has enough capital to cover the resulting cost, the benefits are at least 99.5% certain to be paid over the year following the calculation. We think that this formula is the best way of measuring the cost of risk from those available.

We have performed the necessary calculations. The work indicates that **we have more than enough capital to ensure that Members' benefits will be paid** over the next twelve months.

The formula identifies the source of the risks that each firm faces, and calculates a cost for each of them. Using this formula in 2017, we have established that our biggest risks are unchanged from 2016. They are 1. If Members stop their policies sooner than expected, 2. If investments fail, and 3. If Members are sicker than expected (sick more often, or for longer, or both). We know too, from our own assessment, that there is a risk, 4. if we spend more than is planned. **We continually manage these risks**, as well as all of the other risks that we face.

Managing Our Risk Profile

Risk is managed in two ways. The first is by having big enough resources to meet all claims in all circumstances. This is called 'having sufficient capital'. The second is by running the business properly. This is called 'having an effective system of governance'. **We have sufficient capital and an effective system of governance.** This report sets out how we have concluded that this is the case.

Having sufficient capital

Every year, we review the benefits that we owe to Members and the assets that we have to meet them. We allow for future premiums on existing policies, for expected sickness and for a proportion of Members to stop their policies. This review is called the annual valuation. There are a number of rules that have to be followed to make sure that the result of the valuation is correct.

The purpose of the valuation is to establish whether the Society has enough capital to meet the benefits due to Members.

Within the valuation, the risk in the Society's business is calculated using the formula mentioned earlier. The result of the formula is an amount called the Solvency Capital Requirement or SCR. This is a measure of how much extra capital the Society needs to be 99.5% sure that it can meet all Member benefits in the next year. If an insurer has more capital than the SCR, this means that, on this measure, the chance of there being a problem in the next year is even lower.

The Society's Valuation

This year, our annual valuation showed a healthy buffer of assets over liabilities. The difference is called 'Own Funds'.

The SCR is the capital needed to cover the cost of the risks as calculated by the formula. We have done the work to calculate the SCR and are satisfied with the result, but the regulator reserves the right to assess the result and may ask us to amend it.

The surplus capital is the difference between the Own Funds and the SCR. Surplus capital provides extra protection to Members and is available for other purposes (such as investment in the Society's strategy).

Table 1 shows that the Society has more than £20m of surplus capital when it has allowed for the standard-formula costs of the risks that it bears.

Table 1: Surplus Capital, £000

		31 Dec 2017	31 Dec 2016
(a)	Own Funds	50,704	54,125
(b)	Solvency Capital Requirement	27,825	25,893
(c)	Surplus Capital [(a) – (b)]	22,879	28,231

The surplus capital is lower than at the start of the year, because we have sold more business (giving a bigger SCR), because the formula automatically adjusts for the level of investment markets (the 2017 adjustment has increased the SCR from 2016), and because money has been invested in developing the Society.

We expect our surplus capital to reduce over the next four years as we invest more in new business and in developing the Society. Members can expect the SCR to increase and surplus capital to fall. The Board will continue to monitor the SCR and the surplus capital, to ensure that risk does not grow too high and that capital does not fall too much.

The regulator classifies capital into tiers. All of the Society's capital is Tier 1, the best quality capital.

The regulator sets a minimum level of capital called the Minimum Capital Requirement or MCR which, for the Society, is around one quarter of the SCR. If an insurer's capital falls below the MCR, the regulator will intervene. We are a long way from our capital being below this level.

In conclusion, **we have more than enough capital to support the payment of Member benefits.**

Having an effective system of governance

The Society has a strong system of governance.

Pay is subject to appropriate controls and steps are in place to ensure that people working for the Society, especially at a senior level, are fit and proper. The risk management system has been reviewed this year and is effective. An Own Risk and Solvency Assessment has been performed. This work has been enormously useful in helping the Board and others make decisions.

The internal control system has similarly been reviewed and strengthened. A compliance function has been set up and two people are now focused solely on compliance matters.

For over 15 years, Moore Stephens has acted as the Society's Independent Auditor. Recent changes limit the period that a single firm is allowed to do this work and we decided to hold a competitive tender to select our next Independent Auditor. PricewaterhouseCoopers LLP was appointed during August 2017.

For many years, the Society's internal audit has been provided by an external firm. As the current contract came to its natural end, we held a competitive tender to find a new internal auditor. Ernst and Young LLP took up this role early in 2018.

The actuarial function continued to be provided by OAC Plc.

We continue to monitor those firms to whom we have outsourced services.

In conclusion, we are satisfied that our system of governance is effective, given the nature, scale and complexity of the Society's risks.

Our responsibility

The Directors are responsible for preparing this, the 2017 Solvency and Financial Condition Report, so that it meets the regulator's financial reporting rules and the rules that apply to insurance companies (called Solvency II regulations). The Directors are also responsible for making sure that the working environment is robust enough to ensure that this report is accurate and free from any material mistake, from any cause, including fraud or someone's error.

We are satisfied that, throughout 2017, the Society complied in all material respects with the requirements of the regulators' rules and the Solvency II regulations. It is reasonable to believe that the Society has continued to comply since and will continue to do so in future.

Martin Day
Chair of the Board & Director
2 May 2018

Stuart Tragheim
Chief Executive & Director
2 May 2018

Paul Harwood
Company Secretary & Director
2 May 2018

A. BUSINESS AND PERFORMANCE

A.1 Business

The Original Holloway Friendly Society Limited ('the Society') exists to provide a replacement income when you, one of our Members, cannot work because of sickness (illness or injury). We protect your income when you cannot work, and help get you back to work, if we can.

We currently offer two income protection products. Both protect your income up to a pre-agreed amount. Both provide protection until you retire, but one pays a level of replacement income from when you cannot work until your return to work or retire, while the other only pays for up to two years. The second type is cheaper than the first because the benefit payment period is capped and it has different features, so it appeals to different people. Our Members are introduced by intermediaries who help select the right product for them.

We also offer a Holloway product. This product similarly pays you an income if you cannot work, with the additional benefit of some savings and the right to share in the profits created by these products.

What is a Holloway product?

We understand that we were the first organisation to combine income protection and savings. The resulting innovative product, introduced in the 1880s, was named after our founder, George Holloway.

For the last four years, we have offered a Group Life product issued by a company that the Society owns. This company, called HF Life Ltd, was branded as Optimal. The Group Life product provides the death-in-service benefit that many employers offer to their employees.

We may, in the future, offer new products or adjust, or even stop offering, existing products. We stopped offering products through Optimal during 2017. More information about this is provided later.

As you might realise, this is a simplified description. As already noted, our products are available only through appropriately qualified financial intermediaries who can explain our products, how they can be adjusted for your needs and the options available. Intermediaries act for you, not for us, although we do pay commission to them for every new product which is bought. Intermediaries can offer products from a range of providers, not just from us.

We manage a number of different products, some of which are no longer available. These products can be divided into four types: Income Protection products (like the first two mentioned earlier), with profits products (the Holloway product mentioned above is a with profits product), Unit Linked products and Group Life products.

The Unit Linked product and the Group Life product are both now closed to new business. The Unit Linked product was a savings plan where the benefit was linked to investment performance. The Group Life product is that offered by Optimal, described above.

Everyone who has a product issued by the Society becomes a Member. The Society is owned by its Members. It has no shareholders. Therefore, everyone at the Society works for you, our Members. The Society's Board of Management ('Board') makes decisions on your behalf. You elect the Directors who serve on the Board.

What is a Board?

Most companies are run by a Board of Directors. These are the people who direct the company, decide its strategy and its governance. The Board assesses performance and, if not satisfied, makes changes.

The Board is chosen by the owners of the Company, so for us, the Board is chosen by you, our Members.

The Society has Members throughout the UK, the Channel Islands and the Isle of Man. It offers its products throughout the UK and in the Isle of Man. People with a Group Life product (i.e. a product issued by Optimal, rather than the Society) are not Members.

We are, legally speaking, a friendly society, registered and incorporated under the UK Friendly Societies Act 1992, with the registered number 145F. We are authorised and regulated by the Prudential Regulation Authority ('PRA') and regulated by the Financial Conduct Authority ('FCA'). Our Firm Reference Number ('FRN') is 109986, which you can use if you want to write to either regulator.

The PRA is responsible for our financial supervision. You can contact the PRA by writing to Prudential Regulation Authority, 20 Moorgate, London, EC2R 6DA or by calling 0207 601 4878. The FCA is responsible for regulating our conduct. You can contact the FCA by writing to the Financial Conduct Authority, 25 The North Colonnade, Canary Wharf, London, E14 5HS or calling 0207 066 1000.

Our independent auditor up to 7 August 2017 was Moore Stephens, who can be contacted by writing to 30 Gay Street, Bath, BA1 2PA or telephoning 01225 486100. On 8 August 2017, PricewaterhouseCoopers LLP ('PwC') was appointed as independent auditor. PwC can be contacted by writing to 2 Glass Wharf, Bristol, BS2 0FR or telephoning 0117 955 7779.

What is an independent auditor?

An independent auditor is a firm appointed mainly to provide independent assurance to members that a society's accounts are broadly accurate.

In 2016, the Board took time to assess the future of the Society, given its healthy financial position and the needs that its products serve. The Board decided that it wanted to grow the Society and to provide its products to more people.

This ambition requires the Society to grow. In turn, growth requires us to change how we work. We need to do a number of things differently, to change existing activities and to begin new ones. The changes expected include making a significant investment in computer systems, buildings, equipment and people. The changes involve almost every aspect of how we are managed and every one of our colleagues who work for the Society.

2017 was the first year in a five-year plan to grow the Society by number of Members, by the value of the policies being administered, and by reach. We called it our transformation year.

Transformations included a refurbishment of the office, a repricing of one of the products, increasing the number of people working for the Society by around 50%, the creation of a sales team (to find new intermediaries who might be interested in the Society), a marketing team (to provide materials to show the benefits of our products) and a compliance team (to make sure that all the regulations are being followed). Work began to determine what the new systems should look like and who might provide them.

A.2 Underwriting Performance

What is underwriting?

Underwriting is the process of assessing someone's health and lifestyle to decide the best protection that we can offer and the cost and conditions of this protection.

Underwriting success can be judged by the difference between premiums received and claims paid. Underwriting is effective if the premiums received are greater than the claims paid. Table 2 shows the premiums and claims for the four product types described earlier. Reinsurance is included and is explained a little later.

Table 2: Gross Underwriting Performance – Group £000

Product Type	Premiums received	
	2017	**2016**
Premiums		
Income Protection	2,846	2,125
With profits	2,977	3,639
Group Life	1,553	907
Unit Linked	0	4
Reinsurance	(999)	(902)
Total	**6,376**	**5,774**
Claims paid		
Income Protection	334	195
With profits	757	759
Group Life	1,129	6
Unit Linked	71	147
Reinsurance	(917)	(13)
Total	**1,377**	**1,093**
Net Underwriting Surplus/Difference		
Income Protection	2,509	1,931
With profits	2,220	2,880
Group Life	424	901
Unit Linked	(71)	(143)
Reinsurance	(82)	(889)
Total	**4,999**	**4,681**

Table 2 shows all four business lines together. To understand the business, it is worth separating the components.

First, Income Protection:

Table 3: Gross Underwriting Performance – Society £000, Income Protection				
Product Type	**Premiums received**		**% Surplus**	
	2017	**2016**	**2017**	**2016**
Premiums	2,846	2,125		
Claims Paid	337	195		
Net Underwriting Surplus	**2,509**	**1,931**	**88.2**	**90.8**
Reinsurance is not used for Income Protection business The % Surplus column is Net Underwriting Surplus divided by Premiums				

We have sold more Income Protection policies than last year. Claims increased significantly. Both these changes were expected, because the products were improved and we changed how we dealt with intermediaries and Members, to make the products easier to sell and to make it easier to claim when you are sick (unable to work through illness or injury).

A healthy underwriting surplus was generated from this business for the Society. The surplus meets the expenses of the Society, including the strategic investments, or is retained as value for Members, current and future.

Second, With Profits products:

Table 4: Gross Underwriting Performance – Group £000, With Profits Products		
Product Type	**Premiums received**	
	2017	**2016**
Premiums		
With profits	2,977	3,639
Reinsurance	(65)	(78)
Total	**2,912**	**3,561**
Claims paid		
With profits	757	759
Reinsurance	(7)	(13)
Total	**751**	**746**
Net Underwriting Surplus		
With profits	2,220	2,880
Reinsurance	(58)	(65)
Total	**2,162**	**2,815**

We sold very little With Profits business in 2017. The premium inflow is significant because we have many existing policies that were sold before 2017. These policies continued to pay premiums in 2017. Claims includes the value of the savings part of these policies. We make very little use of reinsurance for With Profits business.

A healthy underwriting surplus was generated from this business for the Society. The surplus meets the expenses of the Society, including strategic expenses, or is retained as value for Members, current and future.

Third, Unit Linked products:

Table 5: Gross Underwriting Performance – £000, Unit Linked Products		
	2017	**2016**
Premiums	0	4
Claims paid	71	147
Difference	**(71)**	**(143)**
Reinsurance is not used for Unit-Linked business		

The Unit Linked product is a savings plan with a small death benefit and with premiums payable for ten years. The last of the ten-year premium-paying periods was reached in 2017, hence the significant drop in premium income. We continue to manage the policy balance until it is claimed by the Member. The Claims shown above reflect Members surrendering their policies to receive their savings benefit.

Finally, Group Life products:

Table 6: Gross Underwriting Performance £000, Group Life (Optimal)		
Product Type	**Premiums received**	
	2017	**2016**
Premiums		
Group Life	1,553	907
Reinsurance	(934)	(824)
Total	**618**	**84**
Claims paid		
Group Life	1,129	6
Reinsurance	(910)	(0)
Total	**219**	**6**
Net Underwriting Profit		
Group Life	424	901
Reinsurance	(22)	(824)
Total	**402**	**78**

Optimal saw a significant increase in premium income, reflecting high repeat and new sales.

Reinsurance is very important for Optimal.

What is reinsurance? *part 1*

Reinsurance is insurance for insurance companies. An insurer can use reinsurance to reduce its own risk, to provide technical support and to help with cash flow. Reinsurance is provided by specialist firms called reinsurers.

The insurer pays a premium to the reinsurer. In return, it receives money from the reinsurer for claims that are made.

Table 6 shows the premiums received from Group Life policyholders, the reinsurance premiums paid and the share of the claims that is met by the reinsurer.

The reinsurance premiums paid in 2017 are higher than 2016 as a direct consequence of the higher new business. Claims paid is much higher. Group Life claims tend to be, for small companies, volatile, and this can be seen in the difference between 2017 and 2016 claims. The reason for having reinsurance is also clear: with the higher claims come higher reinsurance recoveries. The result is that Optimal generated an underwriting surplus in both 2016 and 2017 despite the difference in claims.

This table shows that we are underwriting current business on terms that generate surpluses for the Society and its Members. The surplus contributes to the expenses of running Optimal.

Underwriting in General

With more new Members, we have to underwrite more people. We have therefore recruited a number of experienced underwriters. We expect our underwriting standards to be maintained as we grow.

Managing claims, sometimes called claims underwriting, is an important part of our work. We pride ourselves on working with Members to help them claim quickly and without fuss, and helping them get back to work as soon as they can. We also have to take steps to ensure that our Members' assets are not subject to fraud.

In 2017, we paid out 73% more in income protection benefit on our best-selling products than in 2016.

We continue to develop our underwriting and claims management facilities. We have introduced online data capture of medical information and have made it easier for Members to submit their claim information to us.

A.3 Investment Performance

We classify our investments into three categories: equities (shares), fixed interest (bonds) and cash and property. Table 7 below shows how our investments have performed over 2017.

In numeric terms, the different types of investment return are as shown in Table 7:

Table 7: Investment Performance, £000s - During 2017 & 2016

Asset Type / Return Type	Equities		Fixed Interest		Cash and Property		Total	
	2017	2016	2017	2016	2017	2016	2017	2016
Realised Capital Gain	1,020	476	210	132	0	25	1,229	633
Unrealised Capital Gain	833	1,530	(260)	587	57	0	630	2,117
Income Received	732	564	562	534	67	118	1,361	1,216
Investment Expenses	(85)	(99)	(72)	(68)	(8)	(5)	(166)	(173)
Total	**2,499**	**2,470**	**439**	**1,185**	**116**	**138**	**3,055**	**3,793**

The equity and fixed interest components performed in excess of their benchmark. No benchmark is set for cash or property.

During the year, we asked an external consultancy to consider our investment processes. We are carefully considering its report and expect to make some changes in 2018.

The equities and fixed interest assets are managed by Investec Wealth and Investment Limited. Cash is held in a range of high-quality bank accounts and money-market funds.

At the end of the year, we held no securitised assets (this is a type of investment: the regulations say that we must say whether we hold them).

A.4 Material Income and Expenses

Our main source of income is premiums from Members. We receive income from reinsurers when we pay claims for policies that are reinsured. Details of this income are in section A.2.

We receive income from our investments. Details of this income are in section A.3.

In 2017, we received £5,891 (2016: £28,249) of rent by letting out part of the office.

Table 8 shows the Society's material expenses. We have ignored investment expenses, which are described in section A.3.

Table 8: Material Expenses, £000

	Optimal		Society		Total	
Expenses	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
Commission	205	63	898	616	1,103	679
Sales-related Expenses	556	439	2,903	951	3,459	1,390
Maintenance Expenses	265	176	919	1,051	1,184	1,227
One-off Expenses	0	0	1,870	538	1,870	538
Claims handling costs	0	0	162	72	162	72
Total Expenses	**1,026**	**678**	**6,752**	**3,228**	**7,778**	**3,906**

Our main expenses are sales-related, like commission, day-to-day Head Office expenses and expenses related to investing in the future of the Society.

Commission and other sales-related expenses have increased because sales have increased. Commission is paid when each new policy is accepted. If the early premiums are not received as expected, some of the commission is returned to the Society.

Day-to-day and strategic development expenses have grown, reflecting the investment in our future.

Table 9 below shows the changes in expenses:

Table 9: Expenses – Society, £000

Product Type	**2017**	**2016**	**% change**
Commission	1,103	679	+62.4%
Sales-related Expenses	3,459	1,390	+148.8%
Maintenance Expenses	1,184	1,227	-3.5%
One off Expenses	1,870	538	+247.6%
Claims Handling Costs	162	72	+125.0%
Total Expenses	**7,778**	**3,906**	**+99.1%**

Sales-related expenses have increased because the Society has established a distribution, sales and marketing function. One off expenses have been incurred in the development of new products and the new administration platform.

A.5 Any Other Information

Performance of other activities

The Society set up a company in 2013 called HF Life Ltd, known as Optimal. This company sold Group Life products to companies, rather than Income Protection products to individuals (the Society's main business). The idea was that the Society would be stronger with a second source of income.

As with any young company, we planned to support Optimal financially until it could stand on its own two feet. During 2017, it performed well, attracting many repeat and new customers. Despite this good performance, when we looked closer, it became clear that Optimal could never grow to a size that would allow it to operate as a stand-alone business. As a result, with reluctance, we decided to close the company to new business.

Optimal stopped accepting new business on 27 November 2017. We made sure that existing and renewing customers would be able to find substantially similar products immediately or when their product naturally came to an end. We expect that all of Optimal's customers will have transferred by 31 December 2018.

B. SYSTEM OF GOVERNANCE

What is governance?

Governance describes everything connected with making sure a business is run properly. This includes legal requirements, the need to be fair to Members, and the need to organise affairs sensibly and with proper regard for risk.

B.1 General Information on the system of governance

What is a system of governance?

For the Society, this means everything that is formally in place to make sure that the Society is well governed and does the right thing.

Overview

We have an effective system of governance in place. It ensures that we manage the Society safely and reliably. The system of governance reflects our small size and product range, and our historic expertise in the work that we do. The system of governance for a large company is very different from that of a small company and it is important that the approach chosen fits the company. We think that ours does.

Regulation asks for three things in the system of governance: (a) a transparent organisational structure, (b) clear and appropriate segregation of responsibilities, and (c) a well-established and effective system for ensuring the transmission of information. We think that we have these in place. In short, (a) all of our colleagues know what their jobs are and who else does what else, (b) we don't allow people to do and check their own work or to do work where there might be a conflict, and (c) we work hard to make sure that every colleague knows what is going on, and if not, where to go for help.

The system of governance is regularly reviewed by the Board and its Audit and Risk Committee.

What is the Audit and Risk Committee?

The Board has set up Committees to help it with some of the oversight work that it does. The Audit and Risk Committee oversees internal and external audit, compliance, actuarial and risk management activities. It ensures that the risk management and internal control systems are effective. Details of its terms of reference (the rules it follows) are on our website.

About The Board

The Board is made up of a small group of people, called Directors, who, together, run the Society at a high level. The Board is chosen by our Members and is responsible to Members and to the regulators.

The Board is made up of Non-Executive Directors who are independent (they don't work in the Society other than as Directors, nor do they have any personal interest* in it) and Executive Directors who work in the Society as well as being Directors. There are more Non-Executive Directors on the Board than there are Executive Directors. Thus, if it comes to a vote, Executive Directors cannot out-vote the independent Non-Executive Directors.

* All of the Non-Executive Directors have policies with the Society: as everyone knows about this, it is not believed to be a barrier to them acting and thinking independently. It is explicitly allowed in the Society's Rules.

The Board decides the strategy, hires the Chief Executive and other senior people, and monitors performance. The Board can consider anything it chooses. Mainly, it considers business plan, culture, financial and other reporting, the quality of the system of governance, risk management, the prudential management of the Society and its own succession. The Board is led by the Chair.

What is the Chair?

The Chair is the Non-Executive Director who leads the Board. It is an important role with specific responsibilities to the regulator and to Members.

There are four Board Committees which help the Board do its work.

The Executive Committee is made up of Executive, the most senior people who work for the Society. Senior managers also attend and contribute to these meetings. This Committee considers the Society's day-to-day performance, considers policy, and deals with any matters which need attention but which are not important enough (yet) to need Board attention. It normally meets monthly. The Committee helps the Board by ensuring plans are progressing as expected, and alerting the Board when this is not the case.

What (or who) is the Executive?

The Executive refers to the Chief Executive, the Chief Operating Officer and the Chief Financial Officer.

These are employees who run the Society for the Board, led by the Chief Executive.

The Nomination and Remuneration Committee is two committees sitting at the same time. The Nomination Committee is made up of three independent Non-Executive Directors and the Chief Executive. It considers the Board's performance and its current and future make up. The Remuneration Committee is made up of three independent Non-Executive Directors. It considers all aspects of pay, including executive pay, and bonus plans (short- and long-term and sales). This joint Committee meets at least twice a year. It helps the Board by making sure that the Board and its Committees work effectively, including having a plan for succession, and that there is effective oversight of pay and benefits.

The Investment Committee is made up of three independent Non-Executive Directors and two Executive Directors. It considers the selection and performance of our investments and ensures that they are invested according to the Prudent Person Principle. The Committee meets at least twice a year. It helps the Board to have confidence in the approach to investment and performance of investment managers.

What is the Prudent Person Principle?

This is a phrase in the regulations. It means that investments should be only those that a prudent person would make.

The Audit and Risk Committee (or ARC) is made up of four independent Non-Executive Directors. It considers the effectiveness of our financial management, risk management and internal controls systems and the controls around compliance.
The Committee draws on the work of the independent auditor, the internal auditor, the risk management function, the actuarial function and the compliance function. The Committee meets at least four times every year. It helps the Board have confidence in the quality of our system of governance and the accuracy of our financial statements.

Main Business Areas

There are three main areas of the business: sales and marketing, operations, and finance and risk.

The sales and marketing area is responsible for presenting the Society to Members and intermediaries before and after they have bought a product, dealing with press enquiries, writing and designing material, finding new intermediaries, agreeing commission rates and understanding what products and product features would be attractive to new Members. Its role is to make sure there is a healthy flow of new Members.

The operations function is responsible for the handling of the Society's Head Office activities involving Members and their policies. It includes dealing with Members, underwriting, administration and handling claims when Members are sick. This function keeps the IT systems going and manages new IT developments. It looks after all aspects of the Head Office building. It is responsible for disaster recovery planning, that is, how the Society would cope in an emergency. It handles people management and project and change management. In summary, the role of the operations function is to handle all aspects of managing products after sale, as well as the computer systems, buildings and so on.

The finance and risk function is responsible for the money, be it money coming in (as premiums), money being paid to Members who are ill or injured, or money being paid to cover wages, suppliers, training, insurance, consultancy fees etc.. Part of this responsibility is the proper accounting for every penny received and spent. The finance and risk function is responsible for the Society's risk management systems (does the Society understand the risks it is running?, has it thought about how to manage risks to prevent a problem?), which includes the compliance function (does the Society comply with the rules?) and the company secretarial function (are Board and Committee meetings being run properly?) and liaises with external and internal audit and the actuarial functions. Its role is to ensure that the Society is managed and controlled to the high standards expected of an insurer.

How the system of governance has changed during 2017

Once the Board decided to grow the Society, we made a number of changes including:

- we appointed a new Chair of the ARC
- we implemented new bonus plans for sales, for all colleagues and for the Executive
- we revised our approach to risk management and internal control, and
- we appointed a Compliance Officer and a Compliance Expert.

The Compliance Officer took responsibility for compliance, financial crime prevention and data protection. He has been nominated as our Head of Internal Audit, subject to the regulator agreeing to this appointment. The Finance and Risk Director is the appointed Fraud Officer.

Review of the System of Governance

Every three years, Boards are expected to be reviewed by someone who is independent and external. The idea is to ensure that the Board and its Committees are effective. The Society's Board underwent this process in September 2017.

The results were that "…on the whole, Holloway has a robust and reliable governance structure and follows best practice in all of the key processes identified…".

This was an excellent result. The review mentioned several minor points which are being considered and, where appropriate, progressed.

Remuneration Policy and Practice

We will only be successful if our people work hard and do a good job. The Society's future is in the hands of its employees, whom we call colleagues, who need to be rewarded properly for doing a good job.

The Remuneration Policy describes a company's approach to paying its employees. Our Remuneration Policy tries to make sure that the right behaviour at work is rewarded. This is a balance between continuing doing everyday work to the right standards as well as coping with the changes that growth requires.

We have a clear idea why the Society exists (to be there when Members need us the most – our mission) and what it has to be if it is to grow (to be the most recommended provider – our vision). We also have a clear idea of what makes the Society special (our values). The Remuneration Policy supports the mission, vision and values, and tries to recognise and reward those who support them through their behaviour at work.

Rewards have to be in proportion to the overall success of the Society; they have to reflect each person's contribution.

Our Remuneration Policy is based on the following:

- there needs to be a balance between achievements and risk taking
- rules must be met, values demonstrated and standards maintained
- no-one should benefit through an accident or because the rules did not cover every possible situation (so payments are discretionary), and
- everyone should have the opportunity to earn a bonus based on how well they work.

Pay at the Society is made up of (i) salary, benefits and pension, (ii) either a sales incentive plan or an annual bonus plan and (iii) a long-term incentive plan.

(i) Salary, benefits and pension are paid to all Society employees.

The salary, benefits and pension are competitive. They are regularly compared with the pay and benefits of similar organisations, at every level.

Benefits include car allowance, private medical and dental and other standard benefits (death-in-service, paid holiday, sick pay etc.). The benefits offered differ according to role and seniority.

(ii) The sales incentive plan is open to all colleagues working directly in the sales function. All other colleagues (directly employed by the Society) are eligible for the annual bonus plan.

The sales incentive plan generates bonuses based on quarterly and annual sales performance, and performance on a number of conduct and capability measures.

The annual bonus plan requires threshold sales and expense targets to be hit. If they are, a bonus becomes payable depending on performance against a number of numeric and activity targets.

(iii) The long-term incentive plan is open to members of the Executive Committee.

The long-term incentive plan considers performance over three-yearly periods. It pays a bonus if the Society's value is higher than agreed targets each year for three years. Any bonus is decided upon after the three years is over, is at the Remuneration Committee's discretion, and is paid over the two years following the end of the performance period. There is a plan in place for the period 2017-2019 and a separate plan in place for 2018-2020.

The Purpose of Remuneration

We use pay to attract and keep good people who have the skills and experience that the Society needs to grow. Salary, pension and benefits are set in comparison with similar firms and to attract people to the Society.

The annual bonus plan and the sales bonus plan should encourage the activities needed for the Society to grow.

Terms of Appointment of Executive Directors and Other Members of the Executive

The employment terms, including pay, for the Society's most senior executive functions are overseen by the Nomination and Remuneration Committee. No individual Executive is involved in setting her or his own remuneration. We expect variable remuneration to form a significant part of executive remuneration.

The long-term incentive plan should allow us to attract and retain Executives of the right quality, and should encourage them to focus on building the Society's long-term value. The Nomination and Remuneration Committee is responsible for all payments under this bonus plan. It can choose to ignore the amounts calculated from the bonus formulas, and instead to increase or reduce bonuses payable. It is expected that this would only happen to fairly reflect contributions made, where not to do so would be harmful to the Society's long-term success. The Committee can also reduce, withdraw or claw back any payments under the long-term incentive plan in certain circumstances.

No executive service agreement has a notice period longer than one year and there are no loss-of-office or other benefits linked to resignation, except pay during notice periods. Any severance package for an Executive is subject to agreement by the Nomination and Remuneration Committee. There are no early retirement or supplementary pension schemes.

Terms of Appointment of Non-Executive Directors

Non-Executive Directors are paid on a fixed fee basis. The fees are set to reflect the work required of each individual (chairing committees etc.). Two Non-Executive Directors are eligible for healthcare benefits, but these benefits are not currently offered to new Non-Executive Directors. The notice period is one month. There are no loss-of-office or other benefits linked to resignation from the Board. Re-election varies depending on time served, but no Director may serve for more than three years following their election at the Society's AGM. There are no early retirement or supplementary pension schemes.

Remuneration throughout the Society

The remuneration policy generally applies to all colleagues. The annual bonus plan is open to all. The resulting bonus is expected to form no more than 50% of annual pay.

Transactions with Connected Parties

During 2017, the Society did not do any paid work with people or firms which are closely connected with its Directors or senior managers.

B.2 Fit and proper requirements

We need members of the Executive and Senior Leadership Team to have the skills, knowledge and expertise to run the Society properly and to develop and implement our strategy. The most important quality is experience. Professional qualifications are important, as is a willingness to make the changes necessary to allow us to be there for our Members in their times of need and to demonstrate our strengths to intermediaries.

What is the Senior Leadership Team?

This is the group of people who work for members of the Executive. On a day-to-day basis, the Senior Leadership Team makes sure that the Society is properly run. Members of this team attend the monthly Executive, and some other Committee, meetings and, depending on their job, may occasionally attend or present at Board meetings.

Our Board ensures that those running the Society are properly qualified and have the knowledge and experience to do their work properly. They must have good reputations and have integrity. The regulator calls this being fit and proper. For the most senior people, the Nomination Committee ensures that applicants are fit and proper. For other roles, the Executive has this responsibility.

The regulator is kept up to date with all changes in senior management, including key function holders (the regulator's label for specific functions). We share the information used to confirm that someone is fit and proper. In particular, if someone was thought to be no longer fit and proper, we would tell the regulators.

When someone joins our Executive or Senior Leadership team for a role that requires regulatory approval, a specialist firm is hired to collect the information needed to decide whether they are fit and proper. This firm considers fitness mainly by validating statements made by the candidate, including qualifications earned. It considers proper-ness by searching for flags of poor behaviour. It asks for references from previous employers, although some employers are reluctant to provide detailed references. The Board ultimately decides whether it feels that someone at this level is fit and proper. For these roles, having made its assessment, the Board has to propose the individual to the regulator to be approved before the person can begin in the role.

In all other roles, the checking process is tailored for the role.

B.3 Risk management system including the own risk and solvency assessment

(a) Risk Management System

Insurers are required to have an effective risk management system. It must include strategies, processes and reporting procedures necessary to identify, measure, monitor, manage and report, on a continuous basis the risks, at an individual and at an aggregated level, to which they are or could be exposed, and their interdependencies. This statement of what must be covered by the risk management system is taken from the regulations.

We reorganised our Risk Management System completely during 2017.

Our risk management system is built around the business plan. Risks to the plan are automatically considered when the business plan is developed. The Risk Management System also covers the plans to improve governance and monitors the insurance risk elements of the Solvency Capital Requirement ('SCR').

What is the Solvency Capital Requirement?

This is the amount that the regulator says the Society has to hold to ensure policyholder benefits are secure in most circumstances over one year. It is calculated using a formula provided by the regulator. It is sometimes shortened to SCR.

The size of the SCR depends on the cost of the risk in the business. Is a high cost of risk a bad thing? Only if you do not have enough capital to meet the cost of risk.

A higher risk cost means a bigger SCR. If a firm can meet its risk cost, any surplus capital provides additional security for policyholders or can be used for other purposes.

The Board is satisfied that the new Risk Management System is effective. It is well integrated into the Board processes and is becoming embedded into other parts of the Society. It covers the risks used in the calculation of the SCR.

The Society's Risk Management System starts by defining the risks that the Society faces, split into risks to the business plan, governance risks, insurance risks (as defined in the formula used to calculate the SCR) and operational risks. A risk tolerance is defined for each risk. The tolerance links back to the business plan, governance plans, SCR and risk profile, or operational thresholds. Management then reports to the Board if one or more threshold is, or looks like it might be, exceeded.

What is a risk tolerance?

Most measures of performance have an expected value or target. The risk is that the actual value is higher or lower than the target, to an extent that might cause harm or cause the plan to be re-considered.

A risk threshold is, for a given measure, the value at which action is needed to prevent harm or to reconsider the plan.

The Executive team continually monitors risks, including operational risks, that come to light. Where appropriate, reports are made to the Board, to ensure that Directors are informed about risks materialising and about risk management.

What is operational risk?

Operational risk is the risk of some planned activity going wrong because a process fails, a system fails or someone does something wrong. Operational risk includes errors caused by processes, systems or people not doing something, as well as doing something wrong.

For insurers, the regulator suggests that fraud and legal problems are included as operational risks.

Operational risk and the internal control system is the subject of a separate regular management meeting of senior leaders throughout the Society. At these meetings, control management is discussed along with assessments of control quality by accountable individuals. In this way, there is a very clear line from control quality to control manager, which matches the regulatory emphasis on individuals taking responsibility.

The Society maintains a risk register.

What is a risk register?

The Society's risk register is a list of the risks that we face with details of how the risks are identified, measured, monitored, managed and reported.

We have established a management committee called the Risk and Controls Committee to review risk and internal control information, and to decide what should be passed to the Board and when.

The risk management function is led by the Chief Risk Officer ('CRO'). As a member of the Executive, the CRO is always involved in discussions and decisions about strategy and tactics. The CRO makes sure that risk consequences are considered and sometimes has to respond to challenges about risk. At a day-to-day level, there is a manager responsible for operational risk, who makes sure that risk consequences and challenges are raised and handled. In both cases, there is reporting through the Risk and Controls Committee. We regularly discuss how risk might affect outcomes and our solvency, even if no change is expected. We especially consider risk and the impact on solvency when developing new products.

What is solvency?

When a risk event happens, often (but not always) the simplest solution is money. Regulators recognise that the more surplus money a firm has, the more secure the policyholder benefit. 'Solvency' is the jargon used by insurers to mean the surplus capital that a firm has in excess of that needed to meet Member claims.

Insurers talk about capital rather than money. Capital is defined a little later on.

When considering a risk, insurers look at the impact the risk might have on their surplus capital: hence, the impact on solvency.

Generally, high or increasing solvency is a good thing, low or declining solvency is a concern, unless the change was planned or there is a good reason for it.

When the Board or a Committee has a decision to make, the papers describing the decision include CRO comment. The CRO is expected to cover the impact of the decision on our risks and our solvency. The result is that the Board makes decisions in full knowledge of the possible impacts of the decision on risk, on solvency and on the system of governance, assuming a number of different outcomes.

(b) Risk Management Function

Insurers are required to have a risk management function as part of their risk management system. The Society's Finance and Risk Director serves as Chief Risk Officer ('CRO') and runs the risk management function. The risk management function is responsible for making sure that the risk management system works properly.

As noted above, the Society's risk management system is very tightly aligned to its business planning. Business planning includes considering how the Society might perform in different scenarios, including if its risks materialise. There is a high degree of overlap between business planning and risk management, and thus the performance of both functions by the same person, given the Society's size, can be justified.

The CRO reports to the Chair of the ARC on risk matters. He is a director of the Society. These arrangements provide the authority necessary for the role.

The CRO regularly discusses the work required of the risk management function and the resources available to maintain it and the risk management system with the ARC.

(c) Own Risk and Solvency Assessment

What is an ORSA?

The regulation requires insurers to undertake an Own Risk and Solvency Assessment, or ORSA, whenever its risks change, or at least annually.

The ORSA is a judgement by the Board of the insurer's risks and the impact on the insurer's solvency. Importantly, it is the Board's view, not the regulator's (and not the view using the regulatory formula).

The starting point for the Own Risk and Solvency Assessment (ORSA) is the ORSA policy. This is a document required by the regulator to set out how an ORSA is to be done.

The ORSA process follows a series of steps. The Board and others consider all of the risks that we face and their possible impact. The impact of each risk might be how it affects capital, how management have to behave to contain the risk, or a mixture of both.

What is capital?

Capital is the regulatory name for the resources available to meet the Society's outgoings.

For the Society, capital is made up of cash, investments or the difference between premiums and claims on existing business.

We design a number of risk tests. Some just look at a single risk and suggest to what extent a risk might occur. Others look at groups of risks occurring together. The tests are used to see the impact on the Society if risks occur as suggested. The Board considers the results and may ask for new tests when it sees what the first round of tests reveals.

When the Board is satisfied that it has considered all possible risks, it can start to think about the right level of solvency given those risks. The question the Board is trying to answer is how much surplus capital we need to be confident that we can meet all Member benefits and withstand all of the risks that we face, given the business plan.

What is surplus capital?

Surplus capital is the capital over and above that is needed to meet expected Member benefits.

We then perform a number of routine checks before drawing up a draft ORSA report for the ARC to consider. Based on the Committee's views, a final report is presented to the Board. This final report includes the Board's proposal on the necessary level of surplus capital that we need to have confidence that Member benefits can be paid. Once agreed by the Board, the report is sent to the regulator.

Throughout this process, an ORSA record is kept containing details of the intermediate results and discussions on risk matters.

Once the ORSA report is agreed, the Board conducts a review of the process. The results of the review are fed into the review of the ORSA policy and the next scheduled ORSA.

The results of the ORSA have to be shared throughout the Society. Integrating the ORSA is part of the risk management function work described earlier.

The ORSA happens at least once per year. A new ORSA is organised immediately if our risk profile is expected to change dramatically. In 2017, we performed the ORSA between September and November. This was useful because it supported the major decision to invest in a new computer system.

The ORSA is now considered as part of the Society's strategic planning and the results are routinely used in business decisions and business projections.

In conclusion, the Society has decided, following its 2017 ORSA, that it has enough capital to meet its needs over its five-year business plan (from 1 January 2017), given its risk profile. It is the Society's plan to operate within its own capital resources: thus plans for capital do not affect our planned risk management.

(d) Decision Making

Insurers are required to write down their decision-making procedure as part of their risk management system. We have done this.

We have taken steps to ensure that the Board does not make decisions without understanding the risks to that decision. One of the purposes of the risk management system is to ensure that all of the risks affecting major decisions are understood and that ways to manage or remove risks are considered before the decision is made. Thinking about risk as a day-to-day feature of decisions, rather than something separate, should improve the quality of the work done by the Board and its Committees.

B.4 Internal Control System

(a) About the Internal Control System

Insurers are expected to have an effective internal control system.

We have an effective internal control system, which covers administrative and accounting procedures, an internal control framework, appropriate reporting arrangements at all levels of the undertaking and a compliance function. These are regulatory requirements.

Our internal controls are generally managed by the person responsible for each function. These managers are responsible for making sure that there is the right mix of controls and for managing changes safely within their functions. The controls are labelled as directive (saying what should happen), preventative (stopping the wrong things happening), detective (finding out when something has gone wrong) and corrective (ensuring that corrections happen accurately and without affecting anything else).

There is a regular meeting of managers to consider the Internal Control System. Senior leaders and members of the risk and compliance functions are invited. The nature of internal control and operational risk is discussed. Each manager assesses the effectiveness of their controls and discusses its plans to improve control where necessary. After each meeting, a report is produced for the Risk and Controls Committee, which in turn produces a report for the ARC.

The Head of Operational Risk is responsible for the documentation and management of internal controls.

These structures and accountabilities (regulatory language) form the Society's internal control system.

In conclusion, the Board is satisfied that the Society has an effective internal control system.

(b) Compliance Function

The regulator requires that every insurer has an effective compliance function.

During 2017, a dedicated compliance function was set up. A compliance plan was produced and considered by the ARC.

The role of the compliance function includes advising the Board on the Society's compliance with the laws, regulations and rules of Solvency II. It includes considering changes in regulations and how they might affect the Society. Compliance risk is also considered.

What is Solvency II?

Solvency II is the name given to the European regulations that UK insurers have to follow. It sets out what insurers have to do to protect policyholder benefits.

The areas discussed in this document are all required under Solvency II, as is the production of this document.

The compliance function is available to all other areas of the Society to offer advice. It reports progress on its work plan at regular ARC meetings. The Head of Compliance is appointed by the Committee and has a direct reporting line to the Chair of the Committee and the Chief Executive as well as a day-to-day reporting line to the Finance and Risk Director. These arrangements provide the authority necessary for the role.

The Head of Compliance is industry experienced, has a development plan agreed and in place, and has access to external support should it be needed.

It is important that, while the Head of Compliance is employed by the Society, he can independently decide whether something is in compliance with the rules, without being swayed by his manager or by wider management. The Board is satisfied that the Head of Compliance has operational independence by his nature and professional training, and that it is maintained through the reporting line to the ARC.

The Society's planned compliance activities are set out in an annual compliance plan that is considered by the ARC.
The activities selected for inclusion in the plan depend on the Head of Compliance's assessment of the areas that require review in the light of both the Society's business plan and emerging issues, which may be unexpected but which have a compliance implication. The Head of Compliance regularly considers whether he has enough time and resource to ensure that the Society is appropriately compliant, and reports his conclusions on this subject to the ARC.

In conclusion, the Board is satisfied that the Society has an effective compliance function.

B.5 Internal Audit Function

The regulator requires that every insurer has an effective internal audit function.

The internal audit function considers the adequacy and effectiveness of the internal control system and other elements of the system of governance. It is objective and independent from the operational functions. These are regulatory requirements.

Internal audit agrees what areas it will investigate with the ARC. It produces a report after each investigation describing its findings and its recommendations. This report is presented to the ARC, which ensures that appropriate actions are taken within an appropriate timescale.

The internal audit function has, since 1 January 2005, been provided by an accountancy firm called Hurst.

Over a three-year cycle, Hurst agreed the risks to be investigated with the ARC and produced a work plan. Hurst typically visited the Society twice each year for on-site inspection and investigation, as well as reviewing materials produced by us.
A report was produced after each visit as well as an annual report.

Hurst was contracted until 31 December 2017. Given that the contract was coming to its natural end, we took the opportunity to review the provision of internal audit. We thought about a number of different ways to manage an internal audit function and decided that using an external firm was the right way for us, given the nature, scale and materiality of our activities. We identified a number of firms that could provide this function and invited them to present to some of the ARC members. After this process, and on the recommendation of those Committee members, the Board appointed Ernst and Young LLP ('EY') as its new provider of internal audit. Work is now going on to introduce EY to the Society and to develop the detailed internal audit plan for 2018 and the high-level plan for 2018-2021.

Historically, the internal audit function reported to the Finance and Risk Director. With effect from April 2017, the Compliance Officer has taken on the role of Head of Internal Audit, subject to regulatory agreement. The Head of Internal Audit reports to the chair of the ARC and has a direct reporting line to the Chief Executive in matters regarding Internal Audit. These arrangements ensure that the function has appropriate authority.

By using an external firm, we judge that internal audit is independent and objective. Hurst provides and has provided payroll services for the Society for some time. This activity is not thought to have prevented it from being independent and objective when doing internal audit work.

The Head of Internal Audit regularly considers whether he has enough time himself, and enough resource in terms of days of EY time, directed to internal audit work, and reports his conclusions on this subject to the ARC.

In conclusion, the Board is satisfied that the Society has an effective internal audit function.

B.6 Actuarial Function

The regulator requires that every insurer has an effective actuarial function.

We contract with an external actuarial consulting firm, OAC plc ('OAC'), to provide the actuarial function and to provide our Chief Actuary and With Profits Actuary (currently the same person fulfils both roles). The contract is an annual one, which has been in place since 1 January 2010.

The actuarial function carries out a number of tasks set out in the regulations and provides a number of required reports to the regulator on our behalf.

The Chief Actuary heads the actuarial function and reports to the Finance and Risk Director, with explicit additional reporting lines to the ARC. These arrangements ensure that the function has appropriate authority.

OAC maintains a small team focused on the Society's affairs, led by the Chief Actuary. Members of the team also do work for other OAC clients. OAC takes steps to ensure that there is no conflict, which it discusses with the ARC.
The OAC team liaises with the Society's finance

function to plan the work required over each year and to ensure that there is sufficient resource available to do it to the appropriate standard. He reports his conclusions on this subject to the ARC.

The Chief Actuary liaises with the ARC and the Board throughout the year, especially when there are decisions to be made that require actuarial advice.

The Chief Actuary is always available to members of the Executive and Board to discuss matters of actuarial interest.

By using an external firm, we judge that the actuarial function is independent and objective.

In conclusion, the Board is satisfied that the Society has an effective actuarial function.

B.7 Outsourcing

We outsource some areas of our business, including:

- investment services
- computer system development (part)
- hosting of web-based services
- telephone interviewing and data collection
- actuarial services, and
- internal audit.

In all cases, we remain fully responsible to our Members for the quality of the service.

We do not outsource critical or important operational functions or activities if we judge that the result would be a poorer system of governance, would unduly increase operational risk, would reduce the regulator's ability to oversee the extent of our compliance with its rules, or would undermine continuous and satisfactory service to Members.

We outsource typically to UK-based organisations, although some work may be done elsewhere in the EU or the world. In these cases, we take steps to ensure that the provider agrees that no personal data is sent outside the EU.

We alert our regulator prior to any outsourcing of critical or important functions or activities as well as to any subsequent material developments regarding those functions or activities.

B.8 Any Other Information

Adequacy of System of Governance

Our Board is satisfied that our system of governance is adequate given the nature, scale and complexity of the risks in our business.

C. RISK PROFILE

The Society's risks are not unusual. They are managed transparently.

C.1 Underwriting Risk

We don't know who will buy our products. Underwriting is, as described earlier, how we assess someone's health and lifestyle so that we can decide the best protection that we can offer and the cost and conditions of this protection. Underwriting risk is the risk that the people who buy our products are different from those that we expect. As a result, we may find that we have charged too much or too little, we might not apply the right extra conditions, or might apply them wrongly.

Nature of Underwriting Risk

The nature of our underwriting risk has changed as our new business has increased and as we have made changes to our underwriting approaches. During 2017, we have extensively reviewed our underwriting standards. We always monitor experience carefully, and will be focusing even more intently this year as a result of the changes made.

Managing Underwriting Risk

We regularly compare the sickness and other benefit payments that are made with those that were assumed when the products were designed and that are assumed in the annual valuation. If the number or value of claims is higher than estimated, we will consider what changes need to be made.

What is a valuation?

Every year, we are required to calculate the value of the policies that we administer, primarily to make sure that we have enough capital to meet the benefits that are due to Members. This process is called the valuation.

We use a rich set of data for underwriting. Only some of this data is used in the valuation. Often the data is not stored in ways that can be used in a valuation system. We are taking steps to develop the data stored so that it might be better used in the annual valuation.

Our processes for managing claims have been reviewed during 2017, including by a third party. A number of changes have been made to improve them. We have looked at every part of the processes, from start to finish, including those involving helping Members who are off sick for a considerable time to return to work.

Our business primarily concerns the risk that a Member cannot work. The financial consequences to the Society of this risk materialising depend on the product chosen. In some cases, the Society pays a benefit in lieu of proportion of salary until the Member's retirement. In others, it pays for a maximum of two years.

The most significant risk for the Society's business is that of worsening sickness experience compared to the pricing. Specifically, this might arise because more Members are sick and/or are sick for longer. We use the term 'sickness' to cover absence from work, whether due to illness or injury.

We assess the risk of worsening sickness by close monitoring of new claims and active management of existing claims.

We mitigate it by better underwriting at point of sale, better pricing and effective underwriting at claims stage.

The most significant risk for business introduced through Optimal, which covers the death-in-service benefit offered by employers to their employees, is that an employee dies.

The risks in the Society's and Optimal's products are mainly controlled by the product terms and conditions. We do not offer products with significant options or guarantees, so there is no chance that more Members than expected could decide to choose an option and so generate a significant cost for the Society.

We do not allow for expected investment returns when we set our product prices.

Reinsurance

We have not generally used reinsurance, other than for Optimal, although we may do in future. The reason we don't is (for Income Protection policies) because we have a strong track record of underwriting and of managing sickness claims for the policies that we sell.

We have some reinsurance in place, to protect us from a sudden increase in claims on certain product types, but it has very little financial impact.

The situation is different for Optimal, which was a new line of business for us. The idea was that Optimal's reinsurance arrangement would reduce our risk by limiting claims to around 18% of the face value of the death benefit due. In this way, we could learn about the market without undue risk to the Society.

There are four other long-standing reinsurance arrangements, all of which operate properly, but overall have a negligible effect on our financial position. Details of the reinsurance that we have are in section D.2 section 8.

What is reinsurance? *part 2*

Reinsurance, as described earlier, is insurance for insurance companies.

Insurers are always responsible to their policyholders for the risk that they take on. Reinsurance might provide some security, especially when the products being sold are new. This explains why we have very little reinsurance for our income protection business, but do for our newer group life business.

Risk Sensitivity

The Society is sensitive to more or fewer Members becoming sick, or Members being sick for longer or shorter periods. Table 10 shows the impact on Surplus Capital of changes in numbers of bouts of sickness, or duration of time off work, or the lifespan of Members.

Table 10: Impact of Changes to Assumptions on Surplus Capital, £000 Underwriting

Assumption	Change	Impact (£000s)
Bouts of sickness	10% less sickness	+729
	10% more sickness	(729)
Length of sickness	Sickness bouts are 10% shorter	+2,280
	Sickness bouts lasts 10% longer	(3,397)
Death rate	10% more Members die	+215
	10% fewer Members die	(153)

The Impact column shows the change in Surplus Capital

Outlook

Underwriting risk is expected to increase as a result of the Society's growth plans. We will be underwriting more business for different types of product.

C.2 Market Risk

Market risk is the risk that assets do not perform as expected. Usually, market risk refers to assets falling in value. The size and nature of our market risk depends on the assets that we hold.

We expect to use our assets to meet future commission for new business and to meet ongoing expenses, as well as providing support for Member benefits. As a result, there will be smaller asset balances to be invested. If we decide to invest these smaller asset balances in cash and fixed interest assets, rather than equities, the cost of market risk calculated using the regulatory formula will be lower.

Ideally, assets are selected which match liabilities. For example, assets can be matched to liabilities by nature (if the liabilities are inflation-linked, the assets should be inflation-linked), by term (if the liabilities are expected to be due in one year, the assets should be chosen to perform at the one-year point), by currency (if the liabilities are in pounds sterling, the assets should be too).

What is an asset and a liability?

Accountants talk about assets and liabilities.

For the Society, our policies are labelled as liabilities. They are the commitments we have to meet.

The accumulated premiums less outgoings are labelled as assets. We use the proceeds of the assets to meet the liabilities.

Matching to the nature of our liabilities is difficult for us, because there is no obvious factor that can be identified in the liability profile which can be matched in the asset profile. There is no asset that increases in value when someone cannot work.

Matching by term is also difficult, but not impossible. We may have to pay a benefit tomorrow, or in 50 years' time, and have to be able to do both. We can work out roughly how much we might be called upon to pay and at what times, based on assumptions about Member behaviour. We also know, from our business plan, how much we expect to spend on commission and day-to-day expenses. With this information, we can make sure that we strike the right balance between immediately available, short-term assets and assets invested for the longer term.

Matching by currency is straightforward. All of our liabilities are denominated in Great British Pounds ('GBP'), so we match by investing in GBP-denominated assets. We do buy a small amount of non-GBP asset, where we judge that the extra return promised outweighs the currency mismatch risk (we have time to convert them to GBP before the cash is needed).

We mitigate market risk by ensuring that our investment policy is set with a proper understanding of the nature of the Society's liabilities and its future cash demands, by specifying the degree of diversification required, selecting suitable benchmarks and by monitoring the activity of the selected investment managers.

We invest in a wide range of assets to reduce the chance that poor performance or the failure of a single asset could have a significant impact on the performance overall. Section D.1 describes the portfolio in terms of the different types of asset.

Sometimes, we hold equities and bonds that are issued by the same firms. Our biggest holdings by value are set out in Table 11 below:

Table 11: Equities By Holding, £000

Rank	Asset	Equity Value	Bond Value
1	Lloyds Banking Group plc	633	152
2	Royal Dutch Shell plc	721	0
3	HSBC Holdings plc	427	212
	Balance of portfolio	18,455	12,313
	Total	**20,236**	**12,677**

70% of the equities we hold are UK based. Around 7% are US based, 4% registered in Jersey. The remaining 19% are registered in other countries.

Risk Sensitivity

The Society is sensitive to changes in a number of economic factors. Table 12 shows the impact on Surplus Assets of changes in these factors.

Table 12: Impact of Changes to Assumptions on Surplus Capital, £000 Investment

Assumption	Change	Impact
Risk-free yields	Risk-free yields increase by regulatory shock	(3,828)
	Risk-free yields reduce by regulatory shock	+1,689
Fixed interest	fixed interest assets fall by 10%	(1,938)
Equities	equity values fall by 10%	(2,024)
Property values	property values fall by 10%	(80)
The Impact column shows the change in Surplus Capital		

Required Statements

There is no dependency between different risks of different insurance obligations. We have no off-balance-sheet exposures. We do not use any techniques to mitigate the natural performance of assets and liabilities.

There is no mismatch between asset and liability by term or currency. There are no deliberate mismatches permitted.

Outlook

Market risk is expected to reduce over the business plan term because the value of assets is expected to reduce as more money is paid out as commission for new business, to meet the higher expense base and as an investment in the Society's strategy, and the assets are expected to move to less volatile asset categories.

C.3 Credit Risk

Credit risk is the risk that someone owes you money and cannot pay.

We invest some of our cash with banks and into cash funds. This is a credit risk – the risk that the banks or funds cannot repay our money with the agreed interest on demand. We think that this risk is low because we only use banks and funds with higher credit ratings and we spread the money around to avoid concentration in just one firm or fund.

Table 13: S&P Credit Rating of Fixed Interest Assets and Cash, £000

Rating	31 Dec 2017		31 Dec 2016	
	Value	%age	Value	%age
AAA	165	-	15	-
AA	2,185	11%	1,931	9%
A	8,437	42%	8,059	38%
BBB	7,800	38%	7,882	37%
BB	569	3%	151	1%
B	202	1%	172	1%
NR	1,127	6%	2,954	14%
Total	**20,321**	**100.0%**	**21,164**	**100.0%**

Table 13 shows that, during 2017, the bonds held have been moved towards the middle of the credit rating band: fewer non-rated and fewer AAA/AA rated bonds and a significant increase in BBB rated bonds.

We mitigate credit risk by investing in a diverse pool of quality assets, using professional investment managers to ensure good market understanding.

Other Sources of Credit Risk

Other sources of credit risk are commission balances with intermediaries and reinsurance recoveries. These are small in value terms.

We pay commission to intermediaries assuming that a number of premiums will be paid by the Members that they introduce. If a Member ceases to pay premiums early in the policy lifetime, we expect the intermediary to re-pay some of the commission that they received. This is a credit risk – the risk that the intermediary will not have the money. We think that this risk is low because we choose intermediaries carefully and continually monitor the amounts owing.

We have some agreements with reinsurers. We expect them to pay a proportion of claims on some products. This is a credit risk – the risk that the reinsurer cannot pay us. We think that this risk is low because we only use reinsurers with the higher credit ratings.

C.4 Liquidity Risk

What is liquidity and liquidity risk?

Liquidity is the term used to describe how easy it is to get hold of cash when it is needed. Liquidity changes when the economy changes: for example, when property is hard to sell, it is illiquid.

Liquidity risk for us occurs when a benefit cannot be paid because we cannot physically get hold of the cash to pay. We take steps to make sure that this can never happen, as far as we can tell.

Liquidity risk for us would arise if we could not pay a claim when it becomes payable because we could not physically provide the cash, even though we have enough cash in the bank and sufficient other assets.

Our sources of cash are premiums, investment income, sale of investments, reinsurance payments and the surpluses that we generate. Generally, premiums are a reliable and high quality source of liquidity. The liquidity expected from investment income and assets sales depends on the instructions we give to investment managers. We want to invest in high quality assets with good liquidity, but we do know that we don't need all of our assets to be in cash immediately. By investing to match the expected claims, we can increase the return expected without affecting our ability to pay Member benefits.

We invest our cash and near-cash across many reputable institutions with high credit ratings and thus high liquidity over the short term. The quality is measured by the banks' credit rating. We choose a mix to reduce our reliance on a single bank. Surpluses are a further source of liquidity, but these will already be invested in one or more of the assets mentioned.

As a result of this management, our liquidity risk is low and is expected to remain low.

C.5 Operational Risk

Operational risk is a wide category of risk. It is the risk of something going wrong. This might be people working in the society doing things wrong, or not doing things that they should. It might be a process that is faulty or a process that is missing. It might be a computer program that goes wrong or a computer system that crashes. It might arise from a fraud, from a reputational failing or from poor strategy. There doesn't tend to be an upside from operational risk.

Our exposure to operational risk is higher because we are changing so much of what we do. Change always invokes risk, because the consequences of plans are seldom absolutely as expected. One consequence of our strategy is an increase in operational risk. We seek to manage this risk by planning carefully, thinking about risks, and managing people and projects with sensitivity and understanding. We try and make sure that we consider what might go wrong before we make a change, that we test and check things while in development, and that when a change is finally introduced, we monitor it carefully to make sure the expected outcome results.

The SCR Operational Risk calculation is determined by a regulatory formula.

We measure operational risk through the Internal Control System (see B.3). By its nature, we are managing a number of often-very-different risks under the heading of operational risk. The measures used are particular to the individual risk.

The impact of operational risk on the business plan is considered in the ORSA. For most operational risks, when they materialise, the effect is on the level of sales or expense or both.

We have no particular concentration to operational risk.

We protect ourselves against legal challenges (using directors' and officers' insurance), and fire, theft etc. (using an appropriate insurance policy).

The Society's risk management and internal control systems make sure that operational risk is managed to levels acceptable to the Board.

C.6 Other Material Risks

(a) Material Risks

We assess material risks in our ORSA. We consider the business plans and the areas where results are uncertain. We then consider the range of possible results within normal conditions allowing for individual risks and for groups of risks happening together. The risks that have the greatest impact on solvency are the most material risks.

The material risks that we face are:

(i) Lapse risk: higher lapses than expected
(ii) Expense risk: spending more than expected
(iii) Discovery of an unknown risk

What is a lapse?

When a Member decides not to continue with their policy, we say that the policy has 'lapsed'.

Policies may also end because the Member dies, the Member reaches retirement or the policy reaches its maturity date.

The solvency impact of higher lapse risk has increased over the year because our overhead expenses have increased. Every policy that lapses leaves fewer to bear the remaining expense. Thus, lapse risk and expense risk are connected.

The strategy is designed to mitigate these risks, because the Membership is projected to increase and the value of the policies being administered eventually will be greater than the strategic investment being made.

There is no obvious concentration of risk, other than by product. Product risk is implicit in how we operate.

(b) Assessing and Mitigating Material Risks

(i) Lapse risk: higher lapses than expected

We assess lapse risk by closely monitoring premium collections and other processes which might lead a Member to decide not to continue with their policy.

Lapse risk is mitigated by prompt service, sensitive review of individual cases (recognising that lapse may be appropriate in some circumstances) and by thinking about how to ensure that Members keep their policy going where is it sensible for them to do so.

(ii) Expense risk: spending more than expected

Expense risk is the risk of spending too much.

We assess this risk by monitoring expenses against budget.

We mitigate it by careful use of resource and improvements to planning.

(iii)Discovery of an unknown risk

The Board has to assess all of our risks continually. That said, there is the possibility that an unexpected risk emerges. A risk assessment would be incomplete if it did not mention this possibility.

(c) Liquidity Risk

The regulators require us to note that the valuation of the income protection policies includes expected profit in future premiums of £36.695m (2016: £32.439m). This is important because this amount is available to meet Member benefits over time regardless of how liquid our assets are. That said, this amount arises over the lifetime of the policies, so it may not be available when it is needed. Other ways of managing liquidity risk have to be considered.

(d) Assets and Prudent Person Principle

We invest our assets in line with the Prudent Person Principle, as required by regulation.

We ensure this by carefully selecting investment managers and designing their instructions to cover the security, quality, liquidity and profitability of the assets they select. Assets are always invested in the best interests of Members.

We only invest in assets where we can properly identify, measure, monitor, manage, control and report, and appropriately take into account their risks in our assessment of solvency.

C.7 Any Other Information

Nothing additional to note.

D. Valuation for Solvency Purposes

D.1 Assets

The value of our assets on a Solvency II basis is shown in Table 14:

Table 14: Assets, £000 at 31 December

Asset Type	31 Dec 2017	31 Dec 2016
Property office, own use	800	750
Equities – Listed	11,466	10,849
Bonds – Government	4,938	5,111
Bonds – Corporate	8,597	8,107
Bonds – Other	157	339
Collective Investment Undertakings	13,813	17,222
Assets held for unit-linked contracts	1,124	1,158
Cash and cash equivalents	8,678	8,113
Reinsurance recoverables	77	106
Other	795	273
Total	**50,446**	**52,027**

The office property is revalued every three years by a qualified valuer at open market value; desktop valuation in the interim. It was last valued in November 2017.

Equities, Government Bonds and Collective Investment Undertakings are valued using quoted market prices in active markets provided by third party pricing sources.

Corporate and other bonds are valued using prices from a single broker. The prices are thus from an external source.

Cash and cash equivalents are included at face value.

There have been no changes to the valuation approach used and no significant exercise of judgement in arriving at the values shown.

The Society holds no unlisted equities, derivatives, loans or mortgages. Reinsurance recoveries as at the balance sheet date are shown in the 2017 financial statements (see www.holloway.co.uk) as are leasing arrangements. The Society has no deferred tax assets.

We use the same bases, methods and main assumptions to value assets for solvency purposes as we use in our financial statements, other than the exceptions shown below in Table 15 which reconciles the differences.

Table 15: Asset Reconciliation, £000

	31 Dec 2017	31 Dec 2016
Value of assets presented in financial statements	**54,393**	**56,929**
Intangible assets: policy administration system	270	0
Intangible assets: product and software development	210	12
Prepayments	106	0
Technical provisions gross of reinsurance	3,361	4,890
Solvency II value of assets	**50,446**	**52,027**

The rules for considering solvency are different from the rules for presenting financial information. The solvency rules are concerned with policyholder protection. The financial information presentation rules are concerned with providing a true and fair view. One difference in practice is that what can be treated as an asset is different. Solvency assets cannot include intangible assets (for us, work done to develop products or systems that are not yet live) and some prepayments. Solvency assets cannot include technical provisions.

D.2 Technical provisions

We have to calculate two numbers that measure the value of our policies: the Best Estimate and the Risk Margin. Added together, these numbers are called the Technical Provisions. The Best Estimate is the Society's realistic assessment of every policy's worth when administered by the Society. The Best Estimate includes a small adjustment called 'Incurred but not reported' which is described a little later on.

The Risk Margin is the extra money that a third party would require to take on the Society's policies. It is calculated using a formula set by EIOPA, the European Insurance and Occupational Pensions Authority, a European regulatory body.

The Technical Provision calculations are done by the actuarial function. The approach is well established.

We have to calculate the Technical Provisions for all of our policies. Since the Society began in the 1800s, it has offered a number of different products. We continue to administer all of these for as long as our Members wish to keep their policies going, whether or not we currently offer them to new Members.

There are four main types of product:

1. Income Protection (or IP) products, which pay the income of Members who are sick
2. With profits (or WP) products which, like IP products, pay the income of sick Members, and include a savings element
3. Unit-linked (or UL) products, which are savings contracts
4. Group Life (or GL) products, which pay the death-in-service benefits for companies that wish to offer this benefit to their employees (introduced via Optimal)

Table 16 summarises the Technical Provisions:

Table 16: Summary of Technical Provisions, £000

	31 Dec 2017					31 Dec 2016				
Business Line	**IP**	**WP**	**UL**	**Group Life**	**Total**	**IP**	**WP**	**UL**	**Group Life**	**Total**
Best Estimate	(36,696)	13,716	1,022	91	(21,867)	(32,439)	11,250	1,065	125	**(19,999)**
Risk Margin	11,742	7,646	0	0	19,388	9,710	6,323	0	0	**16,034**
Incurred but not reported		83		57	140		81		59	140
Technical Provisions	**(24,954)**	**21,444**	**1,022**	**149**	**(2,339)**	**(22,729)**	**17,654**	**1,065**	**184**	**(3,825)**

More detail about how we do these calculations is set out below.

(a) How are the calculations done? The Best Estimate

1. Income Protection (or IP) Products

We calculate the expected expenses and claims costs for each policy and deduct the expected premiums. The difference between the two numbers is the net cash outflow. We calculate the net cash outflow for each policy, month by month.

The net cash outflow is made up from all the possible things that might happen on a policy. We start by assuming that all Members are healthy at 31 December. Then, for each policy, for every future month, we calculate the net cash outflow in that month:

Net Cash Outflow = expected monthly sickness benefit
\+ expected maturity and withdrawal benefits
\+ expected expenses (to cover investment and administration)
\- expected premiums

The calculations include assumptions about the probability that a Member becomes sick, or that their policy lapses or ends for any other reason.

The monthly cash flows are added up and converted to today's value: that is, a lump sum now equivalent to all future cash flows. This value is the Best Estimate for these policies.

To convert the future cash outflows to today's value, we use interest rates provided by EIOPA. All insurers use the same rate. A positive lump sum value is a liability that the Society has to meet, a negative value is an asset. The Society's IP business is written to generate a surplus, thus each policy is an asset.

The technical name for this approach is the gross premium valuation. The technique being used to calculate a lump sum is called 'discounting projected monthly net cashflows'. The interest rates are 'risk free'. A sample of the rates used is set out below:

Table 17: Selected Discount Rates, % As dictated by EIOPA

Duration (year)	1	2	3	4	5	10	15	20	25	30	50
31 Dec 2017	0.555	0.684	0.788	0.866	0.937	1.188	1.330	1.378	1.365	1.340	1.166
31 Dec 2016	0.382	0.439	0.520	0.607	0.694	1.079	1.263	1.316	1.290	1.264	1.082

2. With Profits (or WP) Products

The calculations for these products are identical to the calculations for IP products, except that the different benefits are allowed for. Typically, Holloway products have some benefits that are guaranteed on maturity or death. We have some discretion over the payment of a final bonus on death or maturity, and on payments on lapse.

Each year, the benefits on these policies are increased by an interest bonus, reflecting investment returns over the year, and an apportionment bonus, reflecting sickness experience, is added to the benefit payment due.

The probability of these events and the possibility of future increases to the values guaranteed are allowed for in calculating the monthly cash flows. We assume that the interest bonus will be 2% per year and that the final bonuses will remain equal to the rates declared as at 31 December 2017.

3. Unit-linked (or UL) Products

The Best Estimate for these policies is the value of the benefit payable on request. No new premiums are expected on these policies.

4. Group Life (or GL) Products

The Best Estimate for these products is the expected cost of claims arising – that is, the benefit that we expect to pay. These tend to be one-year products, so the Best Estimate is the premiums or part-premium due to be received after 31 December, less the share of commission and expenses.

(b) How are the calculations done? The Risk Margin

The Risk Margin is an amount over and above the Best Estimate equal to the amount that another insurer would need to take on the Society's business.

The regulator's formula used in for the calculations assumes that the amount is equal to the SCR, excluding the market risk component, required in every future year allowing for a required return of interest of 6% per year.

We are allowed to consider how the SCR might reduce in the future, but we choose not to (which means the Risk Margin is higher than it could be). We are allowed to assume that management takes action to reduce the SCR, but again, we choose not to (and the result is that the SCR used is higher than it could be). Not taking these permitted actions means a higher Risk Margin, that is, the Risk Margin is higher, and we hold more capital, in lieu of documenting how we might manage any future transfer.

We have to calculate the amount needed for every future year and discount it, as we discounted the Best Estimate, to give today's lump sum value.

The full formula is quite onerous for an insurer as small as us. The regulator recognises this, and has allowed a simpler formula to be used for smaller insurers. We have decided to use 'simplification 2', which estimates the future SCR in proportion to the Best Estimate.

The Risk Margin at 31 December 2017 is £19.388m (2016: £16.034m). In Table 17, it has been split between the product types in proportion to future premiums.

(c) Adjustments to the Technical Provisions

We calculate the Technical Provisions for each policy of each product type, assuming that there are no claims being paid from them at the year-end date (31 December). This assumption is unrealistic, so the Technical Provisions have to be adjusted for several real-life situations. The situations are labelled from 5. onwards, because they continue on from the description of the valuation by product type in points 1. to 4.

Adjustments

5. **Sickness Claims in payment**
6. **Incurred But Not Reported (IBNR)**
7. **Allowance for expenses**
8. **Reinsurance**

5. Sickness Claims in payment

When a claim is being paid to a Member on a policy at 31 December, an additional process is followed to adjust the Best Estimate. For these policies, we calculate the amount we expect to pay our Member every month until the Member returns to work, the policy ends, or it reaches the maximum payment allowed, or the Member reaches retirement.

6. IBNR

We recognise that some Members may be sick but have not yet had time to inform us, or have told us that they are sick but we have not yet confirmed that we can pay a benefit. Similarly, for Optimal, an employee may have died but the company sponsoring the scheme has not yet had time to tell us.

We ring fence capital to cover the likely Member benefit. How do we decide how much capital is needed? For the Society, we calculate the average of annual sickness claims over the last three years and divide by 12 to give a monthly amount (we are assuming that all claims will be known about within one month). For Optimal, we calculate one month’s risk cost before reinsurance (again assuming that all such claims are reported within a month). The insurance jargon for the claims covered by this capital is ‘Incurred-But-Not-Reported’ claims, or IBNR Claims.

7. Allowance for expenses

We meet the Society’s running expenses, including ensuring that its assets are properly invested. In determining the Best Estimate, we assume that each policy bears an equal share of the total expenses for every month and that the total expenses are covered in full. In these calculations, we expect new policies to bear their share of future expenses, and we allow for policies that end, whatever the reason. We plan new business over four years from the 31 December at which the calculations are done. After this point, expenses are increased in line with an expense inflation assumption.

8. Reinsurance

We have five reinsurance arrangements in place. Three of these cover policies providing an income when a Member is sick, one covering policies providing a payment to Members' estate on death and one covering the Group Life business.

Company:	*Description of Reinsurance Arrangement*
Hannover Re	covering the Premier Plan, paying 50% of the sickness benefit and 100% of the waiver of premium benefit paid after at least 13 weeks of sickness.
GenRe	covering the PIP product, paying 50% of the sickness benefit paid. covering the CI-IP and EIIP products, paying 50% of the sickness benefit paid. covering Optimal, paying 90% of claims up to £50,000, and 100% thereafter.
Swiss Re	covering PRFS death benefit, paying 100% of all death claims.

The GenRe agreement for Optimal is a material agreement and is allowed for in the valuation. The other arrangements are not material because they cover only a small number of policies and the chance of a payment being triggered is very low. They have therefore been ignored in the valuation.

(d) Assumptions

The calculations need a number of things to be assumed, specifically:

A1. if and when Members might fall sick and how quickly they might recover
A2. if and when Members might stop their policies
A3. how much it will cost to run the Society and implement its strategy
A4. how expenses and benefits will grow with inflation, and
A5. if and when policies might end because of death.

A1. if and when Members might fall sick and how quickly they might recover

We investigate our sickness experience every year, although there are relatively few cases. We look at how many Members become sick and how long it takes them to recover. The low number of cases means that it is harder to use the experience to decide on an assumption. We therefore consult industry data which suggests rates of sickness and recovery. The tables we use are called CMIR12.

Table 18: Assumed Sickness Rates

Assumption	31 Dec 2017	31 Dec 2016
Inception Rate[1]	30%	30%
Recovery Rates[2]		
0-4 weeks	60%	60%
4-13 weeks	125%	125%
13 weeks+	200%	200%

[1]of DP1, Part C, section 9.1 CMIR12 (inceptions)
[2]of graduated recovery rates, Table B6(a) CMIR12 (recovery basis)

A2. if and when Members might stop their policies

If a Member stops their policy, the policy is said to have lapsed. The lapse rate is the proportion of policies that lapse during a given period. The assumed rates of lapse and withdrawal used for the valuation are set out in the following table.

Table 19: Assumptions: Lapse Rates, % pa

Product	31 Dec 2017	31 Dec 2016
Income Protection (IP)	7.5%	7.5%
Commuted IP	2.5%	2.5%
Short term IP		
Year 1	20%	20%
Year 2	17.5%	17.5%
Year 3	15%	15%
Year 4	12.5%	12.5%
Year 5+	10%	10%

A3. how much it will cost to run the Society and implement its strategy

In the valuation, we work out the expense that we expect to incur in the four years from 1 January 2018, based on the activities we expect to carry out.

A4. how expenses and benefits will grow with inflation

We assume that expenses increase each year. Some products have benefits that increase with inflation. We make assumptions about these different types of inflation as set out below:

Table 20: Assumptions: Expense Inflation Rate, % pa

Assumption	31 Dec 2017	31 Dec 2016
Expense Inflation	3.1%	3.8%
RPI Inflation	3.3%	2.9%

The type of expense is important. Some expenses are expected to occur every year (for example, the expense of people to look after Member queries). Some expenses are linked to sales and only happen once in a policy lifetime. Others are one-off, such as the investment in the new administration system. The projections that we use take into account the different type of expenses and the different types of activity. In this way, we try to make sure that our projections are a good approximation to the actual business activity expected.

A5. if and when policies might end because of death

We use industry tables to assess if and when policies might end due to death, although the impact on the Best Estimate is very small.

We assume 50% AMC00 except for policies where a claim is being paid, when we assume 100% CMIR12 mortality rates. AMC00 is a standard mortality table.

(e) Some Technical Points that we are required to mention

Differences between Solvency Valuation and Financial Statement Valuation

We use the same bases, methods and main assumptions to value liabilities for solvency purposes as we use in our financial statements.

Currency

Our liabilities are all recorded in Great British Pounds, sometimes shortened to GBP.

Options and guarantees

None of our policies has any options which are financially significant or any guaranteed surrender values.

Uncertainty associated with the value of Technical Provisions

Calculating Technical Provisions involves predicting the future. The early values are better known than the later values. Later values are determined using assumptions, which may not work out in practice.

The uncertainties include economic uncertainty (what will interest rates be?), Member behaviour (when might Members make withdrawals from their policies) and fate (when might a Member fall sick?). In practice, the uncertainties might increase or reduce the cash flows, and hence increase or reduce the Best Estimate.

We are particularly sensitive to:

- Expense Assumptions, given the scale of the change that the Society is undergoing
- Sickness Assumptions, given the lack of data to support the assumption setting, and
- Lapse Assumptions, given the lack of data to support the assumption setting and the sensitivity of lapse rates to changes in regulation and general economic health.

Differences with the financial statements

There are no differences, material or otherwise, between the way in which the Technical Provisions are calculated and the calculations that underpin the financial statements.

What are the financial statements?

Financial statements are the reports that we are required to produce. They are available on our website or on request. They are sometimes referred to as the Report and Accounts. They include a balance sheet and profit and loss account.

Use of Transitional Measures

The regulator allows insurers to use 'transitional measures' or a 'volatility adjustment' if they need to. We do not need to, but we have to state this in this document. The Society has not used transitional measures or the volatility adjustment.

D.3 Other liabilities

The financial statements include 'Other liabilities'. Table 21 shows these liabilities.

Table 21: Other liabilities, £000 at 31 December		
Liability Type	31 Dec 2017	31 Dec 2016
Arising out of direct insurance operations	108,000	-
Arising out of reinsurance operations	97,794	192,913
Claims outstanding	112,190	118,010
Other creditors including tax and social security	1,762,757	1,416,572
Total	**2,080,741**	**1,727,495**

There is no observable market for these specific liabilities or any similar liabilities that could be regarded as a suitable basis for the valuation. The value is therefore based on an estimate of the expected cash flows, i.e. the settlement value. No account has been taken of the effect of discounting short-dated payables as the effect is deemed to be immaterial.

We have some obligations that we have to meet within the next 12 months. Their value has been calculated in accordance with the principles used in our Report and Accounts. The full Report and Accounts document which includes our accounting policies, is available on our website, www.holloway.co.uk

D.4 Alternative methods for valuation

We value our property by asking an external and independent professional property consultant, who offers a property valuation service, to provide us with a value. The valuer looks at other, similar properties and considers their price (where they have recently been sold) and their rental value.

We value our corporate and other bonds using prices from a single broker. The prices are thus from an external source.

We don't use any other alternative methods for valuation.

D.5 Any other information

No other information is supplied.

E. CAPITAL MANAGEMENT

E.1 Own funds

We are governed by the Friendly Societies Act 1992. Under that Act, the Society is an incorporated society with a single Members' fund and no defined mutual member fund. As such, it has no shareholders and our Members are the ultimate owners of the business. The Society's organisation is very simple: all its capital is held in tangible and realisable assets.

Table 22 below shows the Own Funds and Surplus Capital:

Table 22: Own Funds, £000

Item	31 Dec 2017	31 Dec 2016
Own Funds	50,704	54,125
Solvency Capital Requirement	27,825	25,893
Surplus Capital	22,879	28,231

What are Own Funds?

This is jargon for an insurer's total assets, counted using the rules of Solvency II.

Own Funds, used in this report, can be linked back to the Fund for Future Appropriations, again by removing the intangible assets and prepayments.

Table 23: Reconciliation of the Fund for future appropriations to Own Funds, £000

	31 Dec 2017	31 Dec 2016
Fund for future appropriations	**51,290**	**54,137**
Intangible assets: policy administration systems	270	0
Intangible assets: product and software development	210	12
Prepayments	106	0
Own Funds	**50,704**	**54,125**

Own Funds – Objectives, Policies and Processes

Own Funds – Objectives

We manage our Own Funds according to our investment policy. Broadly, this requires us to invest to ensure we can pay all Member benefits as they fall due, to invest in ways that treat Members fairly and meet their expectations, to invest to meet all solvency requirements and, having met these criteria, to invest to maximise returns.

The strategy builds on the investment policy by recognising that the best return on surplus capital is achieved by investing in new business.

Given the strategy, we aim to invest to meet the Society's requirements for cash over the business plan period (1 January 2017 – 31 December 2021), bearing in mind the premiums we expect to receive, the claims that we expect and the new policies that we expect to go on risk.

We aim to generate a return on the assets held. We aim to be always able to meet the benefits due to Members.

Own Funds – Policies

Investment Policy: From time to time, the Board agrees the Society's investment policy. This describes the powers and limits of authority of the Society's selected investment managers. The Investment Committee makes sure that the Investment Policy is followed.

ORSA Policy: The regulator requires us to produce a policy setting out how we will run our ORSA. At least once a year, we run our ORSA process (see Section B.3). Part of this process is to allow the Board to assess the level of future Surplus Capital expected allowing for all sorts of different risks over time. The Board wants to be sure that it always has enough capital to pay policyholder benefits, and that it knows which risks could threaten this position.

The ORSA process includes the testing of many different risks. It allows the Board to understand where there might be a problem and to draw up plans to deal with it. The plans will depend on the situation, but might include a change of strategy, re-pricing or re-designing our products, or changing how we organise the business (usually so it runs at a lower cost). More dramatic action includes closing to new business or transferring the business to another organisation.

Knowing how the Own Funds can be sorted between surplus capital and assets backing the SCR over the business plan period allows the Society to consider if a different investment approach is better suited to protecting Member benefits.

Own Funds – Processes: At least three times every year, the Society reviews the performance of its investment managers to ensure that the investment policy is being followed and to assess performance.

Material Changes

There have been no changes to the investment policy or the objectives, policies or processes used in investing the Own Funds during 2017.

Capital Tiers

The regulations classify capital in different tiers. All of the Society's Own Funds are Tier 1 (the highest quality tier of capital) and have always been Tier 1.

At 31 December, our Tier 1 capital was £50.704m (2016: £54.125m). There are no restrictions on how we might use our Own Funds; they are fully available to cover the SCR and the MCR.

What is the MCR?

The MCR, or Minimum Capital Requirement, is the threshold at which the regulator is allowed to take over the running of an insurer. It is much lower than the SCR (about a quarter of the amount).

The level of Own Funds and of Surplus Assets has changed over the reporting period reflecting the progress of the strategy and the investment in new business.

Required Statements

The regulations require us to set out a number of points about our Own Funds. Specifically:

- The material differences between the equity in the Society's financial statements and the free capital for solvency purposes are shown in Table 23
- There are no Own Fund items subject to a transitional arrangement.
- Under the rules, insurers are allowed to hold Ancillary Own Funds. Ancillary Own Funds count as capital, but are slightly less easy to get hold of. We don't have any Ancillary Own Funds.
- There are no deductions from our Own Funds and no restrictions on their availability and transferability.

E.2 Solvency Capital Requirement and Minimum Capital Requirement

The following table summarises the Society's SCR and MCR.

Table 24: Solvency and Minimum Capital Requirement, £000

	31 Dec 2017	31 Dec 2016
Market risk	10,498	9,463
Counterparty default risk	809	876
Life underwriting risk	4	5
Health underwriting risk	22,695	21,279
Diversification across all risks	(6,464)	(5,984)
Basic Solvency Capital Requirement	**27,541**	**25,638**
Operational risk	285	255
Solvency Capital Requirement	**27,825**	**25,893**
Minimum Capital Requirement	**6,956**	**6,473**

We are allowed to take credit for any action that we might take to improve our capital position. We have decided not to use this option at the moment.

We are satisfied with the result of the calculations to give the SCR and MCR. The regulator reserves the right to assess the result and ask us to amend it. If this happens, we will amend this document and describe the changes.

Required Statements

The regulations insist that we set out a number of points about our SCR and MCR. Specifically:

- There are no simplifications applied to the SCR calculation.
- There are no undertaking-specific parameters used in the SCR calculation.
- The MCR for the Society is 25% of the calculated SCR.

The MCR is calculated using a regulator-provided formula. It varies between 25% and 40% of the SCR. The parameters used in its calculation include the size of the technical provisions and the capital at risk on death/disability. 25% of the SCR is the minimum, subject to a minimum of £3.125m.

There has been no material change to the SCR or the MCR in the reporting period.

E.3 Duration-based equity risk sub-module in the calculation of the SCR

The regulations allow the SCR to be calculated using something called the duration-based equity risk sub-module. We don't use this, and have to state that this is the case.

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

We calculate our SCR using the standard formula, as set out by the regulator.

Insurers are allowed to use an internal model, which is an approach that is tailored to the individual insurer. We judge that using such a model would not produce a better result for the Society and would be much more expensive than the approach we have taken, so we don't use an internal model.

The regulations require us to describe the differences between the standard formula and the internal model, but that does not apply to us.

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

We complied with the rules regarding the maintenance of the SCR and the MCR continuously throughout 2017.

E.6 Any other information

None.

Quantitative Reporting Templates Financial Year 2017

Important Note

As more than 90% of gross written premiums originate from the UK., the Society is not required to complete Quantitative Reporting Template S.05.02.01

The Original Holloway Friendly Society Limited
Reporting for the year ended
31 December 2017

Balance sheet

S.02.01.02

		Solvency II value
	Assets	C0010
R0030	Intangible assets	
R0040	Deferred tax assets	
R0050	Pension benefit surplus	
R0060	Property, plant & equipment held for own use	968
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	38,972
R0080	Property (other than for own use)	0
R0090	Holdings in related undertakings, including participations	0
R0100	Equities	11,466
R0110	*Equities - listed*	11,466
R0120	*Equities - unlisted*	0
R0130	Bonds	13,692
R0140	*Government Bonds*	4,938
R0150	*Corporate Bonds*	8,597
R0160	*Structured notes*	157
R0170	*Collateralised securities*	0
R0180	Collective Investments Undertakings	13,813
R0190	Derivatives	
R0200	Deposits other than cash equivalents	0
R0210	Other investments	0
R0220	Assets held for index-linked and unit-linked contracts	1,124
R0230	Loans and mortgages	0
R0240	Loans on policies	0
R0250	Loans and mortgages to individuals	
R0260	Other loans and mortgages	
R0270	Reinsurance recoverables from:	77
R0280	Non-life and health similar to non-life	0
R0290	*Non-life excluding health*	
R0300	*Health similar to non-life*	
R0310	Life and health similar to life, excluding index-linked and unit-linked	77
R0320	*Health similar to life*	0
R0330	*Life excluding health and index-linked and unit-linked*	77
R0340	Life index-linked and unit-linked	0
R0350	Deposits to cedants	0
R0360	Insurance and intermediaries receivables	
R0370	Reinsurance receivables	97
R0380	Receivables (trade, not insurance)	
R0390	Own shares (held directly)	0
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	0
R0410	Cash and cash equivalents	8,678
R0420	Any other assets, not elsewhere shown	530
R0500	**Total assets**	**50,446**

Balance sheet

S.02.01.02

		Solvency II value
	Liabilities	C0010
R0510	Technical provisions - non-life	0
R0520	Technical provisions - non-life (excluding health)	0
R0530	*TP calculated as a whole*	
R0540	*Best Estimate*	
R0550	*Risk margin*	
R0560	Technical provisions - health (similar to non-life)	0
R0570	*TP calculated as a whole*	
R0580	*Best Estimate*	
R0590	*Risk margin*	
R0600	Technical provisions - life (excluding index-linked and unit-linked)	-3,361
R0610	Technical provisions - health (similar to life)	-3,510
R0620	*TP calculated as a whole*	0
R0630	*Best Estimate*	-22,897
R0640	*Risk margin*	19,388
R0650	Technical provisions - life (excluding health and index-linked and unit-linked)	149
R0660	*TP calculated as a whole*	0
R0670	*Best Estimate*	148
R0680	*Risk margin*	0
R0690	Technical provisions - index-linked and unit-linked	1,022
R0700	TP calculated as a whole	0
R0710	Best Estimate	1,022
R0720	Risk margin	0
R0740	Contingent liabilities	
R0750	Provisions other than technical provisions	
R0760	Pension benefit obligations	
R0770	Deposits from reinsurers	
R0780	Deferred tax liabilities	
R0790	Derivatives	
R0800	Debts owed to credit institutions	
R0810	Financial liabilities other than debts owed to credit institutions	
R0820	Insurance & intermediaries payables	1,047
R0830	Reinsurance payables	
R0840	Payables (trade, not insurance)	106
R0850	Subordinated liabilities	0
R0860	*Subordinated liabilities not in BOF*	
R0870	*Subordinated liabilities in BOF*	0
R0880	Any other liabilities, not elsewhere shown	928
R0900	**Total liabilities**	-258
R1000	**Excess of assets over liabilities**	50,704

Premiums, claims and expenses by line of business

Life

		Line of Business for: life insurance obligations						Life reinsurance obligations		Total
		Health insurance	Insurance with profit participation	Index-linked and unit-linked insurance	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	Health reinsurance	Life reinsurance	
		C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0300
	Premiums written									
R1410	Gross	5,822		0	1,293					7,115
R1420	Reinsurers' share	64		0	935					999
R1500	Net	5,758		0	358			0	0	6,115
	Premiums earned									
R1510	Gross	5,822		0	1,293					7,115
R1520	Reinsurers' share	64		0	935					999
R1600	Net	5,758		0	358			0	0	6,115
	Claims incurred									
R1610	Gross	2,767		71	1,129					3,967
R1620	Reinsurers' share	7		0	910					917
R1700	Net	2,760		71	219			0	0	3,050
	Changes in other technical provisions									
R1710	Gross									0
R1720	Reinsurers' share									0
R1800	Net	0		0	0			0	0	0
R1900	**Expenses incurred**	5,564		0	7			0	0	5,571
R2500	**Other expenses**									2,111
R2600	**Total expenses**									7,682

Life and Health SLT Technical Provisions

S.12.01.02

		Insurance with profit participation	Index-linked and unit-linked insurance			Other life insurance			Annuities stemming from non-life insurance contracts and relating to insurance obligation other than health insurance obligations	Accepted reinsurance	Total (Life other than health insurance, including Unit-Linked)	Health insurance (direct business)			Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Health reinsurance (reinsurance accepted)	Total (Health similar to life insurance)
				Contracts without options and guarantees	Contracts with options or guarantees		Contracts without options and guarantees	Contracts with options or guarantees					Contracts without options and guarantees	Contracts with options or guarantees			
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0150	C0160	C0170	C0180	C0190	C0200	C0210
R0010	**Technical provisions calculated as a whole**									0	0						0
R0020	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole									0	0						0
	Technical provisions calculated as a sum of BE and RM																
	Best estimate																
R0030	**Gross Best Estimate**			1,022			148			0	1,171		-36,696	13,798			-22,897
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default						77			0	77						0
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re			1,022	0		71	0		0	1,093		-36,696	13,798		0	-22,897
R0100	**Risk margin**					0				0	0	19,388					19,388
	Amount of the transitional on Technical Provisions																
R0110	Technical Provisions calculated as a whole										0						0
R0120	Best estimate										0						0
R0130	Risk margin										0						0
R0200	**Technical provisions - total**		1,022			149				0	1,171	-3,510				0	-3,510

Own Funds

	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
R0010	Ordinary share capital (gross of own shares)	0	0		0	
R0030	Share premium account related to ordinary share capital	0	0		0	
R0040	Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings	0	0		0	
R0050	Subordinated mutual member accounts	0		0	0	0
R0070	Surplus funds	0				
R0090	Preference shares	0		0	0	0
R0110	Share premium account related to preference shares	0		0	0	0
R0130	Reconciliation reserve	50,704	50,704			
R0140	Subordinated liabilities	0		0	0	0
R0160	An amount equal to the value of net deferred tax assets	0				0
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	0	0	0	0	0
R0220	**Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds**	0				
R0230	**Deductions for participations in financial and credit institutions**	0				
R0290	**Total basic own funds after deductions**	50,704	50,704	0	0	0
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	0				
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand	0				
R0320	Unpaid and uncalled preference shares callable on demand	0				
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	0				
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	0				
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	0				
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0				
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0				
R0390	Other ancillary own funds	0				
R0400	**Total ancillary own funds**	0			0	0
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	50,704	50,704	0	0	0
R0510	Total available own funds to meet the MCR	50,704	50,704	0	0	
R0540	Total eligible own funds to meet the SCR	50,704	50,704	0	0	0
R0550	Total eligible own funds to meet the MCR	50,704	50,704	0	0	
R0580	**SCR**	27,825				
R0600	**MCR**	6,956				
R0620	**Ratio of Eligible own funds to SCR**	182.22%				
R0640	**Ratio of Eligible own funds to MCR**	728.90%				

	Reconcilliation reserve	C0060
R0700	Excess of assets over liabilities	50,704
R0710	Own shares (held directly and indirectly)	0
R0720	Foreseeable dividends, distributions and charges	
R0730	Other basic own fund items	0
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	0
R0760	**Reconciliation reserve**	50,704
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) - Life business	36,696
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	
R0790	Total Expected profits included in future premiums (EPIFP)	36,696

Solvency Capital Requirement - for undertakings on Standard Formula

S.25.01.21

		Gross solvency capital requirement	USP	Simplifications
		C0110	C0090	C0120
R0010	Market risk	10,498		
R0020	Counterparty default risk	809		
R0030	Life underwriting risk	4	9	
R0040	Health underwriting risk	22,694	9	
R0050	Non-life underwriting risk	0	9	
R0060	Diversification	-6,464		
R0070	Intangible asset risk	0		
R0100	**Basic Solvency Capital Requirement**	27,541		

	Calculation of Solvency Capital Requirement	C0100
R0130	Operational risk	285
R0140	Loss-absorbing capacity of technical provisions	0
R0150	Loss-absorbing capacity of deferred taxes	0
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	0
R0200	**Solvency Capital Requirement excluding capital add-on**	27,825
R0210	Capital add-ons already set	0
R0220	**Solvency capital requirement**	27,825
	Other information on SCR	
R0400	Capital requirement for duration-based equity risk sub-module	0
R0410	Total amount of Notional Solvency Capital Requirements for remaining part	0
R0420	Total amount of Notional Solvency Capital Requirements for ring fenced funds	0
R0430	Total amount of Notional Solvency Capital Requirements for matching adjustment portfolios	0
R0440	Diversification effects due to RFF nSCR aggregation for article 304	0

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

S.28.01.01

	Linear formula component for non-life insurance and reinsurance obligations	C0010
R0010	MCR_{NL} Result	0

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0020	C0030
R0020	Medical expense insurance and proportional reinsurance		
R0030	Income protection insurance and proportional reinsurance		
R0040	Workers' compensation insurance and proportional reinsurance		
R0050	Motor vehicle liability insurance and proportional reinsurance		
R0060	Other motor insurance and proportional reinsurance		
R0070	Marine, aviation and transport insurance and proportional reinsurance		
R0080	Fire and other damage to property insurance and proportional reinsurance		
R0090	General liability insurance and proportional reinsurance		
R0100	Credit and suretyship insurance and proportional reinsurance		
R0110	Legal expenses insurance and proportional reinsurance		
R0120	Assistance and proportional reinsurance		
R0130	Miscellaneous financial loss insurance and proportional reinsurance		
R0140	Non-proportional health reinsurance		
R0150	Non-proportional casualty reinsurance		
R0160	Non-proportional marine, aviation and transport reinsurance		
R0170	Non-proportional property reinsurance		

	Linear formula component for life insurance and reinsurance obligations	C0040
R0200	MCR_{L} Result	193

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
		C0050	C0060
R0210	Obligations with profit participation - guaranteed benefits		
R0220	Obligations with profit participation - future discretionary benefits		
R0230	Index-linked and unit-linked insurance obligations	1,022	
R0240	Other life (re)insurance and health (re)insurance obligations		
R0250	Total capital at risk for all life (re)insurance obligations		265,958

	Overall MCR calculation	C0070
R0300	Linear MCR	193
R0310	SCR	27,825
R0320	MCR cap	12,521
R0330	MCR floor	6,956
R0340	Combined MCR	6,956
R0350	Absolute floor of the MCR	3,251
R0400	**Minimum Capital Requirement**	6,956

Report of the Independent Auditor Financial Year 2017

Report of the external independent auditors to the Directors of The Original Holloway Friendly Society Limited ('the Society') pursuant to Rule 4.1 (2) of the External Audit Part of the PRA Rulebook applicable to Solvency II firms

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

Opinion

We have audited the following documents prepared by the Society as at 31 December 2017:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Society as at 31 December 2017, **('the Narrative Disclosures subject to audit')**; and

- Company templates S.02.01.02, S.12.01.02, S.23.01.01, S.25.01.21 and S.28.01.01 **('the Templates subject to audit')**.

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

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

- The 'Summary', 'Business and performance', 'System of governance' and 'Risk profile' elements of the Solvency and Financial Condition Report;

- Company templates S.05.01.02 and S.05.02.01;

- The written acknowledgement by management of their responsibilities, including for the preparation of the Solvency and Financial Condition Report **('the Responsibility Statement')**.

In our opinion, the information subject to audit in the relevant elements of the Solvency and Financial Condition Report of the Company as at 31 December 2017 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) including ISA (UK) 800 and ISA (UK) 805, and applicable law. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the Solvency and Financial Condition Report in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the directors' use of the going concern basis of accounting in the preparation of the Solvency and Financial Condition Report is not appropriate; or

- the directors have not disclosed in the Solvency and Financial Condition Report any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the Solvency and Financial Condition Report is authorised for issue.

Emphasis of Matter - Basis of Accounting

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

Other Information

The Directors are responsible for the Other Information.

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

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

Responsibilities of Directors for the Solvency and Financial Condition Report

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

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

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

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

Our objectives are to obtain reasonable assurance about whether the relevant elements of the Solvency and Financial Condition Report are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with ISAs (UK) 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 decision making or the judgement of the users taken on the basis of the Solvency and Financial Condition Report.

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

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

Report on Other Legal and Regulatory Requirements

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

PricewaterhouseCoopers LLP
Chartered Accountants
Bristol
3 May 2018

Glossary

The notes are not intended to be definitions, nor are they very technical. They have been provided to aid understanding. If you would like a technical definition or to understand more about the limits of the explanation, we would be happy to provide more details.

Term	Explanatory Note
Assets	Accountants talk about assets and liabilities. The accumulated premiums less outgoings are labelled as assets. We use the proceeds of the assets to meet the liabilities.
Audit and Risk Committee	The Board has set up Committees to help it with some of the oversight work that it does. The Audit and Risk Committee oversees internal and external audit, compliance, actuarial and risk management activities. It ensures that the risk management and internal control systems are effective. Details of its terms of reference (the rules it follows) are on our website.
Board	Most companies are run by a Board of Directors. These are the people who direct the company, decide its strategy and its governance. The Board assesses performance and, if not satisfied, makes changes. The Board is chosen by the owners of the Company, so for us, the Board is chosen by you, our Members.
Capital	Capital is the regulatory name for the resources available to meet the Society's outgoings. For the Society, capital is made up of cash, investments or the difference between premiums and claims on existing business.
Chair	The Chair is the Non-Executive Director who leads the Board. It is an important role with specific responsibilities to the regulator and to Members.
Executive	The Executive refers to the Chief Executive, the Chief Operating Officer and the Chief Financial Officer. These are employees who run the Society for the Board, led by the Chief Executive.
Independent auditor	An independent auditor is a firm appointed mainly to provide independent assurance to members that a society's accounts are broadly accurate.
Financial statements	Financial statements are the reports that we are required to produce under company law. They are available on our website or on request. They are sometimes referred to as the Report and Accounts. They include a balance sheet and profit and loss account.
Governance	Governance describes everything connected with making sure a business is run properly. This includes legal requirements, the need to be fair to Members, and the need to organise affairs sensibly and with proper regard for risk.
Holloway product	We understand that we were the first organisation to combine income protection and savings. The resulting innovative product, introduced in the 1880s, was named after founder, George Holloway.
Lapse	When a member decides not to continue with their policy, we say that the policy has 'lapsed'. Policies may also end because the Member dies, the Member reaches retirement or the policy reaches its maturity date.
Liabilities	Accountants talk about assets and liabilities. For the Society, our policies are labelled as liabilities. They are the commitments we have to meet.
Liquidity	Liquidity is the term used to describe how easy it is to get hold of cash when it is needed. Liquidity changes when the economy changes: for example, when property is hard to sell, it is illiquid.
Liquidity risk	Liquidity risk for us occurs when a benefit cannot be paid because we cannot physically get hold of the cash to pay. We take steps to make sure that this can never happen, as far as we can tell.
MCR	The MCR, or Minimum Capital Requirement, is the threshold at which the regulator is allowed to take over the running of an insurer. It is much lower than the SCR (about a quarter of the amount).
Operational risk	Operational risk is the risk of some planned activity going wrong because a process fails, a system fails or someone does something wrong. Operational risk includes errors caused by processes, systems or people not doing something, as well as doing something wrong. For insurers, the regulator suggests that fraud and legal problems are included as operational risks.
ORSA	The regulation requires insurers to undertake an Own Risk and Solvency Assessment, or ORSA, whenever its risks change, or at least annually. The ORSA is a judgement by the Board of the insurer's risks and the impact on the insurer's solvency. Importantly, it is the Board's view, not the regulator's (and not the view using the regulatory formula).

Glossary	
The notes are not intended to be definitions, nor are they very technical. They have been provided to aid understanding. If you would like a technical definition or to understand more about the limits of the explanation, we would be happy to provide more details.	
Term	**Explanatory Note**
Own funds	This is jargon for an insurer's total assets, counted using the rules of Solvency II.
Prudent Person Principle	This is a phrase in the regulations. It means that investments should be only those that a prudent person would make.
Reinsurance	Reinsurance is insurance for insurance companies. An insurer can use reinsurance to reduce its own risk, to provide technical support and to help with cash flow. Reinsurance is provided by specialist firms called reinsurers. The insurer pays a reinsurance premium to the reinsurer. In return, it receives money from the reinsurer for claims that are made. Insurers are always responsible to their policyholders for the risk that they take on. Reinsurance might provide some security, especially when the products being sold are new. This explains why we have very little reinsurance for our income protection business, but do for our newer group life business.
Risk register	The Society's risk register is a list of the risks that we face with details of how the risks are identified, measured, monitored, managed and reported.
Risk tolerance	Most measures of performance have an expected value or target. The risk is that the actual value is higher or lower than the target, to an extent that might cause harm or cause the plan to be re-considered. A risk threshold is, for a given measure, the value at which action is needed to prevent harm or to reconsider the plan.
Senior Leadership Team	This is the group of people who work for members of the Executive. On a day-to-day basis, the Senior Leadership Team makes sure that the Society is properly run. Members of this team attend the monthly Executive, and some other, Committee meetings and, depending on their job, may occasionally attend or present at Board meetings.
Solvency	When a risk event happens, often (but not always) the simplest solution is money. Regulators recognise that more surplus money a firm has, the more secure the policyholder benefit. 'Solvency' is the jargon used by insurers to mean the surplus capital that a firm has in excess of that needed to meet Member claims. Insurers talk about capital rather than money. Capital is defined a little later on. When considering a risk, insurers look at the impact the risk might have on their surplus capital: hence, the impact on solvency. Generally, high or increasing solvency is a good thing, low or declining solvency is a concern, unless the change was planned or there is a good reason for it.
Solvency II	Solvency II is the name given to the European regulation that UK insurers have to follow. It sets out what insurers have to do to protect policyholder benefits. The areas discussed in this document are all required under Solvency II, as is the production of this document.
Solvency Capital Requirement	This is the amount that the regulator says the Society has to hold to ensure policyholder benefits are secure in most circumstances. It is calculated using a formula provided by the regulator. It is sometimes shortened to SCR. The size of the SCR depends on the cost of the risk in the business. Is a high cost of risk a bad thing? Only if you do not have enough capital to pay the cost of risk. A higher risk cost means a bigger SCR. If a firm can meet its risk cost, any surplus capital provides additional security for policyholders or can be used for other purposes.
Surplus capital	Surplus capital is the capital over and above that needed to meet expected Member benefits.
System of governance	For the Society, this means everything that is formally in place to make sure that the Society is well governed and does the right thing.
Underwriting	Underwriting is the process of assessing someone's health and lifestyle to decide the best protection that we can offer and the cost and conditions of this protection.
Valuation	Every year, we are required to calculate the value of the policies that we administer, primarily to make sure that we have enough capital to meet the benefits that are due to Members. This process is called the valuation.