

2017 PRELIMINARY RESULTS



RSA Insurance Group plc

22 February 2018

Premium income up 4% to £6.7 billion, combined ratio 94%, a new RSA record

Underlying EPS 43.5p, up 10%; statutory profit after tax £322m (2016: £20m)

Return on tangible equity¹ 15.5% (2016: 14.2%) versus 13-17% target range

Final dividend 13.0p per share (19.6p total for 2017, up 23%)

Stephen Hester, RSA Group Chief Executive, commented:

“In a tough period for insurance markets, we are delighted to produce another year of growing profits, dividends and return on equity for shareholders. Higher premium income also highlights the positive customer response to what we are offering.

“RSA’s overseas divisions achieved excellent results in 2017, partly offset by poor underwriting figures in our UK/ London market business as flagged earlier in the year. The Group’s performance ambitions remain high and we target further improvement in 2018 and thereafter.”

Trading results

- Underlying pre-tax profits up 12% to £620m (2016: £556m)
- Group operating profit £663m up 1% (2016: £655m): Scandinavia £389m; Canada £159m; UK & International £133m²
- Group underwriting profit of £394m up 4% and a new record for RSA (2016: £380m):
 - Group combined ratio of 94.0% also a record (2016: 94.2%): Scandinavia 82.9%, Canada 93.9% and UK & International 100.5%²
 - Attritional loss ratio improved by 0.1 point versus 2016³ with good progress in all businesses except the UK
 - Group weather costs in line with last year; large losses elevated at 10.8% of premiums (2016: 8.9%)
 - Group prior year underwriting profit of £157m (2016: £109m)
- Total Group premiums of £6.7bn up 4% at reported FX and up 2% at constant FX excluding disposals: Scandinavia up 0.3%, Canada up 5% and UK & International up 2% (all at constant FX)
- Group written total controllable costs down 6%³ to £1,425m. This comprised 8% cost reductions, offset by 2% inflation
- Investment income of £331m (2016: £369m) down 10% versus last year reflecting the impact of disposals and ongoing reinvestment at lower yields

¹ Underlying measure, please refer to pages 30 to 36 for further information

² Proforma for share of aggregate reinsurance recoveries and excludes the impact of the Ogden rate change

³ Group excluding disposals for 2016 and at constant FX

- Below the operating result, interest expense halved following our debt restructuring. Restructuring costs of £155m (2016: £168m) support the existing and increased cost savings targets
- Statutory profit after tax £322m (2016: £20m)
- Underlying earnings per share (EPS) 43.5p, up 10% (2016: 39.5p). Headline EPS 26.3p (2016: 1.8p)
- Final dividend of 13.0p per ordinary share proposed, bringing total 2017 dividends to 19.6p per ordinary share (up 23%) representing a 45% payout ratio of underlying earnings.

Capital & balance sheet

- Solvency II coverage ratio of 163% after final dividend (31 December 2016: 158%), slightly above 130-160% target range
- Tangible equity £2.8bn (31 December 2016: £2.9bn), 270p per share
- Return on tangible equity of 15.5%¹ (2016: 14.2%) in upper half of 13-17% target range.

Strategic and market update

- Balance sheet restructuring is now complete. 2017 actions comprised the £834m disposal of UK Legacy liabilities (announced in February); issuance of c.£300m of restricted tier 1 notes in Scandinavia and the retirement of c.£640m of existing high coupon debt. These actions reduced risk, improved capital resilience, and lowered interest costs
- RSA's entire focus is on the drive for outperformance in our markets. In that context, our many performance improvement initiatives continue to deliver progress; targeted at customer service, underwriting capabilities and costs
- The improved premium trends we report for 2017 reflect the service enhancements we have been implementing. Pleasingly, trends are better in every region versus 2016
- Underwriting capabilities continue to advance across the Group. These include more sophisticated and agile pricing models, underwriter training and portfolio discipline, and technology driven insights. Progress on attritional loss ratios can be volatile but is on track overall, except for UK Household where improvement measures are in train. Underwriting actions to improve large loss performance are being actively implemented - 2017 setbacks showed the need to remediate in places
- Group written controllable costs for 2017 were down 6%² year-on-year to £1,425m (comprising 8% cost reductions, offset by 2% inflation). Group headcount was down 6% versus 2016 and 23%² since the beginning of 2014. We are raising our savings ambition for a fourth time and now target over £450m gross savings by 2019 (£395m achieved to date). We do not expect to book further 'below the line' restructuring costs to achieve these savings
- Excellent progress has been made towards our best-in-class combined ratio ambitions across the Group, except in the UK. Scandinavia and Canada have passed the targeted threshold, although in both regions we see scope for further improvements. Ireland has returned to underwriting profit (COR 97%) and we expect good continued progress. In the UK, our performance ambition remains unchanged, although its achievement may take longer than originally hoped. Determined action is underway in order to get back on track
- Insurance market pricing and volumes have started 2018 with comparable trends to 2017, save for classes particularly impacted by poor loss experience
- Bond market yield increases, if sustained, allow upgrades to investment income outlook plus reduced capital drag from bond pull-to-par impacts. Conversely, vigilance will be needed to price for any changes in insurance claims inflation.

¹ Underlying measure, please refer to pages 30 to 36 for further information

² Group excluding disposals for 2016 and, where relevant, at constant FX

MANAGEMENT REPORT – KEY FINANCIAL PERFORMANCE DATA

Management basis

£m (unless stated)	FY 2017	FY 2016
Profit and loss		
Group net written premiums	6,678	6,408
<i>Core Group net written premiums</i>		6,281
Underwriting profit \diamond	394	380
Combined operating ratio \diamond	94.0%	94.2%
Investment result \diamond	284	298
Operating result \diamond	663	655
Profit before tax	448	91
Underlying profit before tax \diamond	620	556
Profit after tax	322	20
Net attributable profit \diamond	269	18
Metrics		
Stated earnings per share (pence)	26.3p	1.8p
Underlying earnings per share (pence) \diamond	43.5p	39.5p
Interim dividend per ordinary share (pence)	6.6p	5.0p
Final dividend per ordinary share (pence)	13.0p	11.0p
Underlying return on tangible equity (%) \diamond	15.5%	14.2%
Balance sheet		
Net asset value (£m)	3,653	3,715
Tangible net asset value (£m) \diamond	2,765	2,862
Net asset value per share (pence) \diamond	345p	352p
Tangible net asset value per share (pence) \diamond	270p	281p
Capital		
Solvency II surplus (£bn)	1.1	1.1
Solvency II coverage ratio	163%	158%

\diamond Alternative performance measures:

The Group uses Alternative Performance Measures (marked \diamond throughout), including certain underlying measures, to help explain business performance and financial position. Where not defined in the body of this announcement, further information is set out in the appendix on pages 30-36.

CHIEF EXECUTIVE'S STATEMENT

In 2017, RSA delivered growth in premiums, profits and dividends and an improved 15.5% return on tangible equity¹ – all compared to an extremely strong 2016 result.

We are pleased to report record underwriting profits. However, the year also had some disappointment relative to our ambitions. Excellent underwriting results in Scandinavia, Canada, Middle East and Ireland were partly offset by poor UK (and related London market) results. It is our task in 2018 to deliver a bounce-back in the latter whilst sustaining underlying progress across the Group as a whole.

Strategy & focus

RSA is a focused international insurer. We have complementary leadership positions in the major general insurance markets of the UK, Scandinavia and Canada, together with supporting 'London market' and international business. The Group is well balanced between personal and business customers, across our geographies, product lines and distribution channels.

Our business strategy is to sustain a disciplined focus on RSA's existing areas of market leadership, whilst driving intense operating improvement in pursuit of best-in-class performance levels.

External conditions

General insurance markets are relatively mature, consolidated and stable, though with some inevitable underwriting volatility. Attractive performance can be achieved through intense operational focus within a disciplined strategic framework.

For the insurance industry, 2017 was a year with some major external underwriting challenges. At a global level, it seems likely to have been one of the worst loss years in recent times due particularly to three major US/ Caribbean hurricanes and Mexico earthquakes. On a lesser scale, UK market losses around the Ogden discount rate change and Household insurance 'escape of water' inflation also dented domestic insurance results. Notwithstanding these factors, market capacity remains high, and there are limited signs of price inflation more broadly.

Conversely, financial markets during 2017 were more stable, at least as impacting RSA. Bond yields are off their lows and global central bank action to wean markets off QE gives some optimism that coming years might offer return upside for insurers' portfolios. However, tight credit spreads continue to hurt, especially on UK pension accounting. RSA makes a majority of profit outside the UK, so FX rates versus sterling are also important. During 2017 impacts were limited despite swings, although the Brexit process continues to have the potential to deliver volatility.

2017 actions

2017 was another year of intense activity at RSA. The great majority of our efforts were focused on operational improvement in pursuit of our best-in-class ambitions. We also delivered the final pieces of RSA's balance sheet restructuring successfully. We look forward to 2018 as the first clean 'business as usual' year since 2012.

Financial strength: RSA's 'A' grade credit ratings are where we want them. The Solvency II capital ratio at 163% (2016: 158%) is in a good place. The £834m disposal in February of our UK Legacy insurance liabilities removed a source of long-tail risk whilst funding a £640m retirement of high cost subordinated debt capital. This was the final piece of balance sheet work on our agenda. While we aspire to grow 'core tier 1' capital coverage further, the active phase of balance sheet repair is now complete.

¹ Underlying measure, please refer to pages 30 to 36 for further information

Business improvement: Our goal is to systematically and determinedly hunt down performance improvement opportunities across the business to move RSA's capabilities and then outcomes towards best-in-class levels. This involves particular focus on improving three areas; service to customers, underlying underwriting results and cost efficiency.

Personal Lines policy count rose at RSA in 2017 for the first time in four years as customers reacted positively to the many improvements we are putting through. The important home partnership with Nationwide commenced business in December. Operational initiatives also contributed, spanning service improvements via digital capabilities in claims and policy servicing, through to capability and proposition uplifts across our business lines. RSA will not chase unprofitable growth. We prize quality of customer relationship over quantity. But nevertheless, serving customers well remains at the heart of all we seek to achieve.

RSA's most important capability lies in our underwriting judgement. Across the Group multiple improvements continued in areas like portfolio discipline, data and model improvement, machine learning and skills enhancement. Attritional loss ratios improved in every business except the UK. Here our attritional results experienced significant setback, largely through Household 'escape of water' claims, which we expect to rectify for 2018/ 2019. The Group attritional loss ratio was slightly better than prior year as a result, not quite as good as hoped for although still substantially better than historically achieved.

Cost efficiency remains a critical performance lever. We have now achieved £395m annual gross savings and are able to raise our savings targets for a fourth time to over £450m by 2019. Digitisation, lean operations, site consolidation, enhanced purchasing, robotics, zero based budgeting – all the tools in modern corporate armouries to boost people productivity - are being deployed effectively across our regions.

Financial results 2017

Underlying earnings per share rose 10% to 43.5p. This produced a return on tangible equity¹ of 15.5% (2016: 14.2%), versus our target range of 13-17%.

At a statutory level, net profit before tax rose to £448m (2016: £91m) reflecting a lower level (though still significant) of restructuring charges. It remains our ambition that 2017 be the last year of such charges.

Premium income was up 4%, in line with our plan, featuring modest policy count increases together with price and FX benefits.

Underwriting profits posted a new record at £394m, up 4% versus our record year in 2016. The combined ratio of 94.0% was also a new record for RSA. Underlying pre-tax profits rose 12%, benefiting from resilient investment income and lower interest expense.

Excellent underwriting results were achieved in absolute and relative terms across many of our businesses. Scandinavia led the way with a combined ratio of 82.9%. Canada also improved, in a challenging market, to a combined ratio of 93.9%. Middle East had record results (COR 87.7%) and the Irish turnaround delivered its first profits since 2012 (COR 97.0%).

The disappointment was our UK business (including its European branches and London market Commercial Lines business). A COR of 102.0%² reflected three major loss items; £72m of losses from US/ Caribbean hurricanes and Mexican earthquakes (net of GVC recovery), elevated Household 'escape of water' inflation and significant adverse large loss volatility versus long-term averages. Underwriting action is well underway to improve results in 2018.

¹ Underlying measure, please refer to pages 30 to 36 for further information; ² Proforma for share of aggregate reinsurance recoveries and excludes the impact of the Ogden rate change

Reflecting RSA's overall progress in 2017, a final dividend of 13.0p per share is proposed, making 19.6p per share total for 2017, up 23%. This represents a 45% payout of underlying EPS (higher than 2016 but in line with stated policy). RSA's focused business strategy is designed to generate attractive levels of free cash flow, after meeting organic growth needs. With rising earnings targeted, no more restructuring costs and as bond pull-to-par impacts recede in coming years, RSA should have the potential for attractive further growth in shareholder distributions.

Looking forward

Our performance target of 13-17% return on tangible equity represents attractive shareholder return both relative to cost of capital and insurance industry norms. To the extent that RSA's underwriting performance progresses well towards our best-in-class combined ratio ambitions, even better returns are possible. We will try to achieve just that. For 2018, the key tasks are to re-establish respectable performance in our UK business whilst continuing underlying progress in our overseas markets where the majority of the Group trades.

Thanks

RSA made good progress with customers and for shareholders in 2017, despite significant external challenges. In achieving this, we owe thanks to all stakeholders for their support. But most particularly to my colleagues at RSA, who have embraced our best-in-class ambition so effectively, go my sincere thanks and appreciation.

Stephen Hester
Group Chief Executive
21 February 2018

MANAGEMENT REPORT

SEGMENTAL INCOME STATEMENT

Management basis – 12 months ended 31 December 2017

	Scandinavia £m	Canada £m	UK & International £m	Central functions £m	Group 2017 £m	Group 2016 £m
Net written premiums	1,833	1,619	3,199	27	6,678	6,408
Net earned premiums	1,836	1,591	3,196	(18)	6,605	6,528
Net incurred claims	(1,197)	(1,039)	(2,199)	85	(4,350)	(4,215)
Commissions	(59)	(212)	(638)	(2)	(911)	(941)
Operating expenses	(265)	(242)	(441)	(2)	(950)	(992)
Underwriting result \diamond	315	98	(82)	63	394	380
UK & International proforma ¹ \diamond			(16)			
Investment income	102	66	163	-	331	369
Investment expenses	(4)	(2)	(7)	-	(13)	(12)
Unwind of discount	(24)	(3)	(7)	-	(34)	(59)
Investment result \diamond	74	61	149	-	284	298
Central expenses	-	-	-	(15)	(15)	(23)
Operating result \diamond	389	159	67	48	663	655
UK & International proforma ¹ \diamond			133			
Interest					(43)	(99)
Adjustment for Legacy sale					-	(204)
Other non-operating charges					(172)	(261)
Profit before tax					448	91
Tax					(126)	(71)
Profit after tax					322	20
Non-controlling interest					(33)	7
Other equity costs ²					(20)	(9)
Net attributable profit \diamond					269	18
Underlying profit before tax \diamond					620	556
Loss ratio (%)	65.2	65.3	68.8	-	65.9	64.6
Weather loss ratio	0.1	3.7	4.8	-	2.6	2.5
Large loss ratio	5.7	7.7	15.5	-	10.8	8.9
Current year attritional loss ratio \diamond	62.6	56.8	50.1	-	55.3	55.2
Prior year effect on loss ratio	(3.2)	(2.9)	(1.6)	-	(2.8)	(2.0)
Commission ratio (%)	3.2	13.4	20.0	-	13.7	14.4
Expense ratio (%)	14.5	15.2	13.8	-	14.4	15.2
Combined ratio (%) \diamond	82.9	93.9	102.6	-	94.0	94.2
UK & International proforma (%) ¹ \diamond			100.5			
Earned controllable expense ratio (%) \diamond	23.3	18.7	20.8	-	21.5	23.3

Notes:

UK & International comprises the UK (and European branches), Ireland and the Middle East
Please refer to appendix for 2016 comparatives

¹ Proforma for share of aggregate reinsurance recoveries and excludes the impact of the Ogden rate change; ² Preference dividends of £9m and coupons of £11m paid on 2017 issued restricted tier 1 securities

Premiums

Group net written premiums of £6.7bn were up 6%¹ at reported FX and up 2%¹ at constant FX.

Foreign exchange provided a 4% benefit to premiums year-on-year, down from 8% for the first half of the year.

We have seen a strengthening of underlying customer activity as capability improvements take effect. Customer retention trends are improving and satisfaction levels remain good. Overall, Group retention improved to 80.2% (2016: 79.5%).

Our goal remains to serve customers well but profitably.

Regional trends for 2017 include:

- Scandinavian premiums were up 7% at reported FX and up 0.3% at constant FX. Growth in Sweden and Norway was partly offset by a small contraction in Denmark. Personal Lines policy counts were up 1%, while Commercial Lines volumes (excluding rate) were down 3%
- Canadian premiums were up 12% at reported FX and 5% at constant FX. The region reported the fourth quarter of consecutive growth in Q4, with Personal Lines policy counts up 3% and Commercial Lines volumes up 1%. There was good growth in our broker channel (policy count up 4% in Personal broker) and our direct channel, Johnson, also returned to organic growth in 2017
- UK & International premiums were up 4% at reported FX and up 2% at constant FX. UK premiums were up 3%, with Personal up 7% (policy counts up 2%) and Commercial flat. Premiums in Ireland were down 7% at constant FX, while Middle East premiums were up 6%.

More detail is provided in the regional reviews on pages 14 to 19.

¹ Group excluding disposals for 2016

Underwriting result

Group underwriting profit of £394m was up 4% year-on-year:

£m	Total UW result ◊		Current Year UW ◊		Prior Year UW ◊	
	2017	2016	2017	2016	2017	2016
Scandinavia	315	239	255	213	60	26
Canada	98	74	56	6	42	68
UK & International ¹	(16)	88	(60)	82	44	6
Central functions ¹	(3)	(9)	(14)	(28)	11	19
Total Group ex. disposals	394	392	237	273	157	119
Disposals	-	(12)	-	(2)	-	(10)
Total Group	394	380	237	271	157	109

Current year profit was £237m (2016: £271m):

- The Group attritional loss ratio of 55.3% was 0.1 point better than 2016² at constant FX. Scandinavia was 1.6 points better, while Canada was 1.0 point better. UK & International was 1.1 points higher than a year ago as improvements in UK Personal Motor, Ireland and the Middle East were offset by a higher attritional loss ratio in UK Household
- Group weather costs were £168m or 2.6% of net earned premiums (2016: 2.6%² at constant FX; five year average: 3.2%²). Three major US/ Caribbean hurricanes and Mexico earthquakes cost £72m net of reinsurance in 2017 (£115m gross). 2016 was also a year with natural catastrophe losses including the Alberta wildfires, UK & European floods and a US hurricane
- Group large losses were £713m or 10.8% of net earned premiums (2016: 9.1%² at constant FX; five year average: 9.0%²). This elevated large loss experience was driven by the UK and Canada. While substantial elements of this are volatile, underwriting interventions have also been made to target recovery in 2018 and beyond.

Group prior year profit was £157m, pleasingly higher than our planning assumption and providing a 2.8 point benefit (2016: 2.2² points at constant FX) to the Group combined ratio. This included positive development from each region.

The 2017 underwriting result included a £23m net charge (after release of 2016 margin build) relating to the change in Ogden discount rate in the UK. £20m related to our UK business and £3m to Northern Ireland. This also reflected the benefit of net settlement gains in H2 against H1 revised case reserves.

Our assessment of the margin in reserves for the Group (the difference between our actuarial indication and the booked reserves in the financial statements) returned to its target level of 5% of booked claims reserves.

Underwriting operating expenses

The Group underwriting expense ratio of 14.4% was 0.6 points better than a year ago at constant FX (2016: 15.0%²). Pleasingly, all regions contributed with improvements of 0.3 points in Scandinavia, 1.4 points in Canada and 0.4 points in UK & International.

Commissions

The Group commission ratio in 2017 of 13.7% was flat² at constant exchange.

¹ Proforma for share of aggregate reinsurance recoveries and excludes the impact of the Ogden rate change, with the corresponding adjustment in Central functions; ² Group excluding disposals for 2016

Investment result

The investment result was £284m (2016: £298m) with investment income of £331m (2016: £369m), investment expenses of £13m (2016: £12m) and the liability discount unwind of £34m (2016: £59m).

Investment income was down 10% on prior year, primarily reflecting the impact of the disposal of Latin America and the UK Legacy book, together with ongoing reinvestment at lower yields. The average book yield across our major bond portfolios was down slightly to 2.5% (2016: 2.6%).

Based on current forward bond yields and foreign exchange rates, it is estimated that investment income will be c.£285-310m for 2018, c.£275-300m for 2019 and c.£270-295m for 2020. The discount unwind is expected to be in the region of c.£30-35m per annum.

Total controllable costs

Our cost reduction programme has now delivered total gross cost reductions of £395m, compared to a 2018 target of more than £400m. We are raising our target for a fourth time to over £450m gross savings by the end of 2019.

Group written total controllable costs were down 6%¹ to £1,425m. This comprised 8% cost reductions, offset by 2% inflation. Canada delivered year-on-year 'real' cost reductions of 9%, Scandinavia delivered 5% and UK & International delivered 5%. The written controllable cost ratio was 21.3% (2016: 23.1%).

Group FTE² is down 23% (excluding disposals) since the start of 2014 to 12,636 at 31 December 2017. FTE decreased by 6% during the course of 2017.

The earned controllable expense ratio improved to 21.5% in 2017, with all regions contributing. It is now down 4.4 points since the start of 2014¹, making good progress towards our ambition of an earned controllable expense ratio of less than 20%.

Earned controllable expense ratio: ◇	Scandinavia %	Canada %	UK & International %	Total %
Year ended 31 December 2017	23.3	18.7	20.8	21.5
Year ended 31 December 2016 ¹	24.3	20.7	22.0	23.0

Non-operating items

Interest costs:

- Interest costs in 2017 were £43m (£54m including the new tier 1 issuance – see below), down from £99m in 2016. The reduction reflects debt restructuring actions over the past 12 months
- In 2017, the Group issued c.£300m of restricted tier 1 notes in Scandinavia and retired £636m of existing high coupon debt. These actions supplemented the £200m debt retirement completed in July 2016
- Coupon costs for the new Scandinavian issuance are reflected at the bottom of the management P&L as 'other equity costs', as per accounting rules. The cost for the year was £11m, with an annualised interest cost for this instrument of £14m.

¹ Group excluding disposals for 2016 (and prior years where relevant) and at constant FX

² Full time equivalent employees

Other non-operating charges:

£m	2017	2016
Net gains/ losses/ FX	47	(194)
Debt buyback premium	(59)	(39)
Restructuring costs	(155)	(168)
Amortisation	(15)	(16)
Pension net interest cost	(7)	(4)
Goodwill/ intangible asset write-backs/ (downs)	17	(30)
Other	-	(14)
Total ¹	(172)	(465)

- Net gains of £47m in 2017 include a £66m gain relating to the UK Legacy disposal (mainly mark-to-market of the assets transferred to the buyer); a £22m charge relating to the commutation of the Group's adverse development reinsurance cover, both as previously noted in 2016; and a £23m software impairment charge relating to the UK, Scandinavia and Ireland
- 2017 included a charge of £59m relating to the premium paid on the debt buybacks completed during the first half of the year
- Restructuring costs were £155m in 2017. These costs are c.£50m higher than originally planned; however, they have enabled a fourth increase in our cost savings target to over £450m by the end of 2019. It remains our ambition that 2017 will be the last year of 'below the line' restructuring charges. Total 'cost to achieve' these savings will have been c.1.3x the annual savings target, improved from the 1.5x originally expected
- The goodwill write-back of £17m in 2017 reflects the re-measurement of the fair value of the Oman business following its IPO process during the year.

Tax

The Group reported a tax charge of £126m for 2017, giving an effective tax rate (ETR) of 28% (2016: 78%). The Group underlying tax rate was 22.1% (2016: 24%).

The tax charge of £126m largely comprises tax payable on Scandinavian and Canadian profits as well as Canadian dividend withholding tax of £28m. The Canadian dividend withholding tax includes £23m attributable to a one-off dividend in connection with an internal debt reorganisation. Excluding this one-off dividend withholding tax the group ETR would be 23%.

The carrying value of the Group's net deferred tax asset at 31 December 2017 was £220m (2016: £216m), of which £217m (2016: £212m) is in the UK. At current tax rates, a further c.£229m (2016: £183m) of deferred tax assets remain available for use but not recognised on balance sheet; these are predominantly in the UK and Ireland.

In 2018, we would expect the Group's ETR and underlying tax rate to continue to trend towards 20% given the scale of the unrecognised UK tax assets.

Dividend

We are pleased to declare a final dividend of 13.0p per ordinary share (2016: 11.0p). Together with the interim dividend of 6.6p, this brings the total dividend for the year to 19.6p (up 23%), representing a 45% payout of underlying EPS. Our medium term policy of ordinary dividend payouts of between 40-50% of earnings remains, with additional distributions where justified.

¹ Foreign currency translation reserve

BALANCE SHEET

Movement in Net Assets

	Share- holders' funds ¹ £m	Non- controlling interests £m	Tier 1 notes £m	Total equity £m	Loan capital £m	Equity & loan capital £m	TNAV [◇] £m
Balance at 1 January 2017	3,715	132	-	3,847	1,068	4,915	2,862
Profit after tax	289	33	-	322	-	322	385
Foreign exchange losses net of tax	(22)	(14)	-	(36)	-	(36)	(22)
Fair value losses net of tax	(194)	(1)	-	(195)	-	(195)	(194)
Pension fund gains net of tax	44	-	-	44	-	44	44
Repayment & amortisation of loan capital	-	-	-	-	(627)	(627)	-
Issue of tier 1 notes	-	-	297	297	-	297	-
Share issue	4	-	-	4	-	4	4
Share based payments	16	-	-	16	-	16	16
Prior year final dividend	(112)	(10)	-	(122)	-	(122)	(112)
Interim dividend	(68)	-	-	(68)	-	(68)	(68)
Other equity costs ²	(20)	-	-	(20)	-	(20)	(20)
Changes in interests in subsidiaries	1	12	-	13	-	13	1
Goodwill and intangible additions	-	-	-	-	-	-	(131)
Balance at 31 December 2017	3,653	152	297	4,102	441	4,543	2,765

Per share (pence) [◇]

At 1 January 2017	352	281
At 31 December 2017	345	270

Tangible net assets remained broadly constant at £2.8bn at 31 December 2017.

Profit after tax of £385m was offset by negative fair value mark-to-market movements of £194m, mainly reflecting a reduction in the bond unrealised gains reserve. This was driven by the bond pull-to-par effect and the realisation of gains on the transfer of the Legacy assets. Payment of the 2016 final and 2017 interim dividends (totalling £180m) also reduced tangible net assets, together with investment of £131m in intangible assets, primarily IT related (net investment of £37m after amortisation shown as part of profit).

The IAS 19 pension valuation generated a gain of £44m. The annual update to mortality tables more than offset negative movements, including narrower 'AA' corporate bond spreads (see page 24 for further detail).

¹ Ordinary shareholders' funds including preference share capital of £125m

² Includes preference dividends of £9m and coupons of £11m paid on 2017 issued restricted tier 1 securities

CAPITAL POSITION

Solvency II position ¹ :	Requirement (SCR) £bn	Eligible Own Funds £bn	Surplus £bn	Coverage %
31 December 2017	1.8	2.9	1.1	163%
31 December 2016	1.8	2.9	1.1	158%

The Solvency II coverage ratio¹ increased to 163% during 2017 (31 December 2016: 158%):

	%
At 1 January 2017	158
Recurring:	
Underlying capital generation	25
IAS 19 movements, including annual update to mortality tables	4
Market movements excluding IAS 19, partly due to a slight weakening of Sterling	2
Net capital investment after amortisation	(2)
Pull-to-par on unrealised bond gains	(9)
2017 dividends	(11)
Non-recurring:	
Disposal of UK Legacy liabilities	18
Ogden rate change	(3)
Debt restructuring actions	(10)
Restructuring costs and other non-operating items	(9)
At 31 December 2017	163

Please refer to Appendix (page 23) for further Solvency II details (including sensitivities).

OUTLOOK

RSA's goal for 2018 is to set new record levels of performance for shareholders and to serve customers well, whilst continuing to move business capabilities forward consistent with our best-in-class ambitions.

We expect markets to remain competitive, showing modest growth overall. Our priority is to maintain underwriting discipline and to improve areas of 2017 underwriting disappointment. Nevertheless, we target positive premium growth in aggregate.

We aim to make further gains in attritional loss ratios and in cost efficiency. Weather and large loss ratios are hard to predict, although bounded by reinsurance protection consistent with prior years. However, we do expect to see improved large loss performance compared with 2017.

Investment income (pre discount unwind) is expected to be c.£285-310m for 2018 subject to market movements. Interest costs should be c.£25m with a further c.£14m in coupons paid on restricted tier I securities which is recognised directly in equity. We target 2018 to be clear of 'below the line' restructuring costs.

¹ The Solvency II capital position at 31 December 2017 is estimated

REGIONAL REVIEW – SCANDINAVIA

Management basis

	Net written premiums		Change		Underwriting result			
	2017 £m	2016 £m	RFX %	CFX %	2017 £m	2016 £m		
Split by country								
Sweden	1,055	990	7	1	259	174		
Denmark	623	588	6	(1)	61	63		
Norway	155	143	8	2	(5)	2		
Total Scandinavia	1,833	1,721	7	-	315	239		
Split by class								
Household	362	336	8	1				
Personal Motor	353	332	6	1				
Personal Accident & Other	339	313	8	2				
Total Scandinavia Personal	1,054	981	7	1	240	175		
<i>Policy count change</i>			<i>1</i>	<i>1</i>				
Property	327	295	11	4				
Liability	147	151	(3)	(9)				
Commercial Motor	214	202	6	-				
Other	91	92	(1)	(6)				
Total Scandinavia Commercial	779	740	5	(1)	75	64		
<i>Volume change</i>			<i>(3)</i>	<i>(3)</i>				
Total Scandinavia	1,833	1,721	7	-	315	239		
Investment result					74	72		
Scandinavia operating result					389	311		
Operating ratios (%)	Claims		Commission		Expenses		Combined	
	2017	2016	2017	2016	2017	2016	2017	2016
Scandinavia Personal	61.2	66.9	3.1	2.9	12.7	12.2	77.0	82.0
Scandinavia Commercial	70.5	69.5	3.4	4.1	16.7	18.0	90.6	91.6
Total Scandinavia	65.2	68.0	3.2	3.4	14.5	14.8	82.9	86.2
<i>Earned controllable expense ratio</i>					23.3	24.2		
<i>Claims ratio:</i>				<i>5 year average</i>				
<i>Weather loss ratio</i>	0.1	0.4		1.0				
<i>Large loss ratio</i>	5.7	5.0		5.7				
<i>Current year attritional loss ratio</i>	62.6	64.2						
<i>Prior year effect on loss ratio</i>	(3.2)	(1.6)						

SCANDINAVIA

Scandinavia delivered operating profit of £389m, up 25%. Driving this was an excellent underwriting profit performance of £315m in 2017, up 24% (at constant FX). The combined ratio (82.9%) was within our < 85% best-in-class ambition for the first time on record. Current and prior year profitability were strong, at £255m and £60m respectively.

Net written premiums of £1,833m were up 7% at reported FX and up 0.3% at constant FX (2016: £1,721m). A number of premium related key performance indicators are showing positive signs. In Sweden, Personal Lines policies-in-force ('PIFs') grew steadily in 2017, with Q4 1.5% higher than Q4 in 2016. Commercial Lines new business in Q4 was 22% higher than the same quarter last year. While Denmark Personal Lines PIFs contracted between 2012 and 2016, this trend flattened in 2017. Commercial Lines returned to growth this year excepting the more volatile Construction, Power & Engineering business.

We continue to make good progress with our customer agenda. Improvement initiatives included the launch of a 'chat bot' service in Sweden and a new customer claims service portal in Denmark. Overall retention was in line with 2016 at 78%, Personal Lines retention improved but was offset by a decrease in Commercial Lines.

The current year attritional loss ratio of 62.6% was 1.6 points better than 2016 reflecting underwriting discipline, ongoing capability improvements and lower claims handling costs. Benign weather experience (0.3 points better than last year) was offset by adverse large loss experience (0.7 points higher than last year but in line with the 5 year average of 5.7%). The prior year effect on the loss ratio was particularly positive, producing a benefit of 3.2% (2016: 1.6%).

The Scandinavian performance improvement programme has continued to deliver well, with particular focus on operational efficiency; for example, process redesign, robotics and automation. We have also pursued further site consolidation and IT cost reduction, and we launched a BPO programme for certain operational and support activities in Q4 of 2017.

Total written controllable expenses were down 3% year-on-year¹, with 5% cost reductions absorbing 2% inflation. The earned controllable cost ratio of 23.3% showed a 0.9 point reduction year-on-year. Staff related costs reduced by 8%¹ in 2017 with headcount down 9% in the year and down 23% since the end of 2013.

Geographically, Sweden generated an underwriting profit of £259m (2016: £184m¹) and a combined ratio of 75.3% (2016: 82.2%¹). While the current year combined ratio improved by 2.2 points (3%), favourable prior year development contributed 4.7 points year-on-year, partly reflecting more benign Motor account development. Denmark produced a combined ratio of 90.3%; while this was 0.6 points higher than 2016, the current year combined ratio improved by 1.7 points.

Inclusive of an investment result of £74m (2016: £72m), the region's total operating profit of £389m (2016: £311m) was up by a pleasing 25%.

Scandinavia – Outlook

We continue to expect Scandinavian P&C markets to grow in line with local GDP and we target medium-term growth broadly in line with the market, subject to maintaining underwriting discipline.

Our focus remains on continued sustainable improvement in the underlying performance of the business, particularly relating to customer volumes, attritional loss ratios and costs. While our 2017 result is within the target combined ratio of < 85%, we see scope for further progress in the sustainability and composition of the result.

¹ At constant FX

REGIONAL REVIEW – CANADA

Management basis

	Net written premiums		Change		Underwriting result	
	2017 £m	2016 £m	RFX %	CFX %	2017 £m	2016 £m
Household	498	445	12	4		
Personal Motor	622	549	13	6		
Total Canada Personal	1,120	994	13	5	75	91
<i>Policy count change</i>			3	3		
Property	218	194	12	5		
Liability	109	102	7	-		
Commercial Motor	119	102	17	9		
Marine & Other	53	51	4	(2)		
Total Canada Commercial	499	449	11	4	23	(17)
<i>Volume change</i>			1	1		
Total Canada	1,619	1,443	12	5	98	74
Investment result					61	66
Canada operating result					159	140

Operating ratios (%)	Claims		Commission		Expenses		Combined	
	2017	2016	2017	2016	2017	2016	2017	2016
Canada Personal	67.1	64.0	11.2	11.0	14.9	16.0	93.2	91.0
Canada Commercial	61.3	67.9	18.3	18.0	15.8	17.9	95.4	103.8
Total Canada	65.3	65.2	13.4	13.1	15.2	16.6	93.9	94.9

Earned controllable expense ratio

18.7 20.7

Claims ratio:

Weather loss ratio

3.7

5.7

5 year
average

5.0

Large loss ratio

7.7

6.4

5.1

Current year attritional loss ratio

56.8

57.8

Prior year effect on loss ratio

(2.9)

(4.7)

CANADA

In 2017, Canada increased operating profit by 14% to £159m (2016: £140m). Underwriting profit also rose 32% (to £98m), despite higher large losses and lower prior year releases than a year ago. The combined ratio improved to within our best-in-class ambition of < 94% and seems likely to compare favourably with local competitors.

Net written premiums of £1,619m were up 12% at reported FX and 5% at constant FX (2016: £1,443m as reported). Growth was particularly strong in the broker channel, with Personal broker up 10% (policy count up 4%) and Commercial broker up 4%, both at constant FX. Johnson, our direct business, also returned to growth in the year (policy count up 2%).

We continue to work hard to enhance our customer offering. In Johnson, we have made strong progress in digital capabilities while customer NPS scores have continued to improve and outperform benchmarks. In our broker distributed businesses, faster response times and new digital tools enable brokers to service their clients anywhere, anytime, reducing the time to quote from hours to minutes. Customer retention has improved to 85.8% from 84.3% a year ago with Personal Lines up 1.7 points and Commercial Lines up 0.9 points.

The business generated an underwriting profit of £98m (2016: £74m), with a current year profit of £56m and a prior year profit of £42m. The current year attritional loss ratio of 56.8% was 1 point lower than a year ago, reflecting both rating action and our investments in pricing sophistication. Weather experience was 2 points favourable to 2016, noting that the prior year included 2.9 points for the Fort McMurray wildfire losses. Large loss experience was elevated at 7.7%, compared to 6.4% in 2016 and a five year average of 5.1%. Prior year reserve releases, while positive at 2.9%, were lower than last year (2016: 4.7%). Overall, the combined ratio was 93.9% (2016: 94.9%).

Our business improvement programme in Canada progressed well, delivering further enhancements to pricing sophistication, process simplification and site consolidation, while the implementation of the Guidewire claims system is proceeding as planned.

Total written controllable expenses were down 7% year-on-year, with 9% cost reductions offset by 2% inflation. The earned controllable cost ratio of 18.7% showed a creditable 2.0 point reduction during 2017. Headcount was down 5% in the year and is now down 21% since the end of 2013.

Canada – Outlook

We target a continuation of the positive premium and underwriting trends that we have seen in 2017. Sustaining a combined ratio of < 94% will remain a priority and we believe that there is scope for further performance improvements from here.

Risks to performance include volatility in weather and large losses. We are working hard to drive large loss ratios back towards long term averages, recognising trends early and taking any underwriting and/or pricing action required. The Canadian Motor market remains challenging and we continue to lobby through industry associations for product reform.

REGIONAL REVIEW – UK & INTERNATIONAL

Management basis

	Net written premiums		Change		Underwriting result			
	2017 £m	2016 £m	RFX %	CFX %	2017 £m	2016 £m		
Household	559	555	1	1				
Personal Motor	303	235	29	29				
Pet	282	278	1	1				
Total UK Personal	1,144	1,068	7	7	10	48		
<i>Policy count change</i>			2	2				
Property	676	642	5	4				
Liability	294	300	(2)	(2)				
Commercial Motor	226	262	(14)	(14)				
Marine & Other	348	316	10	6				
Total UK Commercial	1,544	1,520	2	-	(126)	75		
<i>Volume change</i>			1	1				
Total UK	2,688	2,588	4	3	(116)	123		
UK proforma¹					(53)			
Ireland	303	306	(1)	(7)	9	(49)		
Middle East	208	187	11	6	25	14		
Total UK & International	3,199	3,081	4	2	(82)	88		
UK & International proforma¹					(16)			
Investment result					149	149		
UK & International operating result					67	237		
UK & International proforma¹					133			
Operating ratios (%)	Claims		Commission		Expenses		Combined	
	2017	2016	2017	2016	2017	2016	2017	2016
Total UK Personal	62.7	57.8	20.3	21.2	16.2	16.7	99.2	95.7
Total UK Commercial	75.3	61.8	21.7	21.1	11.1	12.3	108.1	95.2
Total UK	70.0	60.2	21.1	21.2	13.2	14.0	104.3	95.4
UK proforma¹							102.0	
Ireland	71.8	91.6	11.7	12.2	13.5	12.4	97.0	116.2
Middle East	48.5	56.8	17.3	16.6	21.9	19.4	87.7	92.8
UK & International	68.8	63.0	20.0	20.0	13.8	14.2	102.6	97.2
UK & International proforma¹							100.5	
<i>Earned controllable expense ratio</i>					20.8	22.1		
<i>Claims ratio:</i>			<i>5 year average</i>					
<i>Weather loss ratio</i>	4.8	2.7	4.0					
<i>Large loss ratio</i>	15.5	12.1	12.4					
<i>Current year attritional loss ratio</i>	50.1	49.0						
<i>Prior year effect on loss ratio</i>	(1.6)	(0.8)						

¹ Proforma for net aggregate reinsurance recovery and excludes the impact of the Ogden rate change

UK & INTERNATIONAL

The UK & International business segment delivered operating profit of £133m¹, down 44%. Driving this result was a disappointing combined ratio of 100.5%¹ (2016: 97.2%).

UK

The UK business result (includes European branches and 'London market' international business lines) suffered from a number of material market events in 2017. This was reflected in a combined ratio of 102.0%¹ (2016: 95.4%). Underwriting losses include the impact of adverse weather events (US/ Caribbean hurricanes and Mexico earthquakes) amounting to £72m (net of GVC recovery), adverse large loss volatility and higher Household claims inflation.

Despite this accumulation of adverse market conditions, the underlying UK business continues to make progress. Net written premiums increased by 3% at constant exchange. UK Personal growth of 7% (policy count up 2%) was underpinned by continued growth in our Motor telematics proposition. UK Commercial net written premiums were flat at constant FX in a competitive market. Targeted growth in our Marine and Property portfolios was offset by shrinkage in Commercial Motor resulting from strong underwriting actions.

In December, we successfully launched our new distribution partnership with Nationwide Building Society as well as signing/ renewing a number of other important long term distribution relationships. Our transformation agenda continues to deliver benefits with increased process simplification and enhanced data analytics capabilities. Intense pricing response and underwriting remediation of the issues that hit 2017 is already well advanced.

Total written controllable expenses were down 3% on a like-for-like basis. Real cost reductions of 6% were offset by 3% inflation. The earned controllable cost ratio of 20.3% improved 1.6 points year-on-year. Headcount was down 8% in the 2017 and is now down 24% since the end of 2013.

Ireland

Ireland returned to underwriting profit delivering a profit of £9.5m and combined ratio of 97.0% (or 96.2% excluding Ogden), underpinned by disciplined underwriting actions. The attritional loss ratio of 60.4% was 5.8 points better than prior year. The result also absorbed a £2.5m cost due to the Ogden discount rate change. Net written premiums of £303m were down 7% at constant FX versus 2016 following targeted remediation activity.

Middle East

The Middle East delivered an underwriting result of £25m (2016: £14m) and a record combined ratio of 87.7% (2016: 92.8%) driven by a 5.0 point improvement in the attritional loss ratio. Net written premiums of £208m were up 6% at constant FX despite challenging economic conditions.

UK & International – Outlook

We expect underlying premium trends to continue into 2018 and weather and large losses to return towards long term levels. Attritional loss ratio weakness of 2017 will not fully correct in 2018 as remedial pricing actions take time to earn through. Our plans target further underwriting improvements, cost reductions and capability uplifts.

In Ireland, we aim to improve profit levels through underwriting and cost actions. In the Middle East, the medium term outlook remains positive and work is underway to further develop capabilities, including underwriting and pricing sophistication. For the UK & International business as a whole, we retain the performance ambition of < 94% combined ratio, although we do not expect to reach this level in 2018.

¹ Proforma for net aggregate reinsurance recovery and excludes the impact of the Ogden rate change

INVESTMENT PERFORMANCE

Management basis

Investment result	2017 £m	2016 £m	Change %
Bonds	262	300	(13)
Equities	32	28	14
Cash and cash equivalents	5	10	(50)
Property	21	23	(9)
Other	11	8	38
Investment income	331	369	(10)
Investment expenses	(13)	(12)	(8)
Unwind of discount	(34)	(59)	42
Investment result	284	298	(5)

Balance sheet unrealised gains (pre-tax)	31 Dec 2017 (£m)	31 Dec 2016 (£m)	Change %
Bonds	397	619	(36)
Equities	30	8	275
Other	1	2	(50)
Total	428	629	(32)

Investment portfolio	Value 31 Dec 2016 £m	Foreign exchange £m	Mark to market £m	Other movements £m	Transfer from assets held for sale £m	Value 31 Dec 2017 £m
Government bonds	3,713	6	(76)	207	-	3,850
Non-Government bonds	7,832	14	(109)	(1,014)	87	6,810
Cash	985	(11)	-	76	(2)	1,048
Equities	170	7	8	57	-	242
Property	333	-	1	(26)	-	308
Prefs & CIVs	522	(5)	17	(12)	-	522
Other	88	(2)	4	129	-	219
Total	13,643	9	(155)	(583)	85	12,999

Split by currency:

Sterling	3,994	3,468
Danish Krone	1,081	1,096
Swedish Krona	2,565	2,588
Canadian Dollar	3,232	3,079
Euro	1,345	1,443
Other	1,426	1,325
Total	13,643	12,999

Credit quality – bond portfolio

	Non-government		Government	
	31 Dec 2017 %	31 Dec 2016 %	30 Dec 2017 %	31 Dec 2016 %
AAA	42	35	66	65
AA	15	22	30	30
A	30	30	4	4
BBB	11	11	-	1
< BBB	2	2	-	-
Non-rated	-	-	-	-
Total	100	100	100	100

INVESTMENT PERFORMANCE

Investment income of £331m (2016: £369m) was offset by investment expenses of £13m (2016: £12m) and the liability discount unwind of £34m (2016: £59m). Investment income was down 10% on prior year, primarily reflecting the impact of the UK Legacy business disposal, together with ongoing reinvestment at lower yields.

The average book yield for 2017 on the total portfolio was 2.5% (2016: 2.6%), with an average yield on the bond portfolios of 2.4% (2016: 2.5%). Reinvestment rates in the Group's major bond portfolios were approximately 1.4%.

At 31 December 2017, the average duration of the Group's bond portfolios of 3.8 years was marginally higher than at the prior year end (31 December 2016: 3.6 years).

The investment portfolio decreased by 5% during the year to £13.0bn. The movement was driven primarily by cash outflows for corporate debt restructuring and negative mark-to-market unwind on bond holdings.

At 31 December 2017, high quality widely diversified fixed income securities represented 82% of the portfolio (31 December 2016: 85%). Equities (largely REITs) represented 2% (31 December 2016: 1%) and cash was 8% of the total portfolio (31 December 2016: 7%).

The quality of the bond portfolio remains very high with 98% investment grade and 70% rated AA or above. We remain well diversified by sector and geography.

Unrealised bond gains and pull-to-par

At year-end, balance sheet unrealised gains of £428m (pre-tax) had reduced by £201m or 32% during 2017, driven by realised gains from the UK Legacy disposal, negative mark-to-market on bond holdings due to yield movements and bond pull-to-par.

Based on year-end forward yields, we anticipate that unrealised gains on the AFS bond portfolio should largely unwind over the next 3 years, with c.£150m expected to unwind in 2018. The capital impact of this amount is under £100m, the balance being projected yield change. The capital impact from pull-to-par is expected to fall sharply in 2019 and 2020 based on current market forward yield curves, which have improved further (risen) since year-end.

Outlook

Based on forward bond yields and foreign exchange rates, it is estimated that investment income will be higher than previously guided, namely c.£285-310m for 2018, c.£275-300m for 2019 and c.£270-295m for 2020. These projected income numbers are, however, sensitive to changes in market conditions. We continue to expect a discount unwind on long-tail liabilities of c.£30-35m per annum.

APPENDIX I
Further information

DISPOSALS

2016 net written premiums of £6,408m included £127m in respect of businesses now disposed (Latin America and Russia). The underwriting profit of £380m for the same period included a loss of £12m in respect of these disposed businesses. See page 26 for further detail.

CAPITAL

Solvency II sensitivities

2017 coverage ratio **163%**

Sensitivities (change in coverage ratio):	Including pensions	Excluding pensions
Interest rates: +1% non-parallel ¹ shift	+11%	+6%
Interest rates: -1% non-parallel ¹ shift	-10%	-7%
Equities: -15%	-8%	-2%
Property: -10%	-3%	-2%
Foreign exchange: GBP +10% vs all currencies	-3%	-4%
Cat loss of £75m net	-4%	-4%
Credit spreads: +0.25% ² parallel shift	+4%	-2%
Credit spreads: -0.25% parallel shift	-14%	+3%

The above sensitivities have been considered in isolation. The impact of a combination of sensitivities may be different to the individual outcomes stated above.

Reconciliation of IFRS total capital to Eligible Own Funds

	31 Dec 2017
	£bn
Shareholders' funds (including preference shares)	3.9
Loan capital	0.5
Non-controlling interests	0.1
Total IFRS capital	4.5
Less: goodwill & intangibles	(0.8)
Adjust technical provisions to Solvency II basis	(0.3)
Basic Own Funds	3.4
Tiering & availability restrictions	(0.4)
Foreseeable dividends	(0.1)
Eligible Own Funds	2.9

¹ The interest rate sensitivity assumes a non-parallel shift in the yield curve to reflect that the long end of the yield curve is typically more stable than the short end; ² The IAS 19 surplus cap will dampen upside credit spread sensitivities, so these should not be extrapolated

PENSIONS

The table below provides a reconciliation of the movement in the Group's pension fund position under IAS 19 (net of tax) from 1 January 2017 to 31 December 2017:

	UK £m	non-UK £m	Group £m
Net pension fund deficit at 1 January 2017	(113)	(84)	(197)
Actuarial gains ¹	66	10	76
Increase in tax charge on UK surplus	(32)	-	(32)
Deficit funding	55	4	59
Other movements ²	1	5	6
Pension fund surplus/(deficit) at 31 December 2017	(23)	(65)	(88)

At an aggregate level, the pension fund position under IAS 19 improved during the year from a £197m deficit at 1 January 2017 to a deficit of £88m at 31 December 2017 (net of tax).

The UK position improved by £90m during the year, driven by deficit funding contributions (£65m pre-tax) and actuarial gains (primarily due to updated views of life expectancy). Gains were partially offset by actual pension increases being higher than expected.

The UK defined benefit schemes closed to future accrual on 31 March 2017 and, where applicable, the stated accounting position of those schemes has been reduced for the tax cost of an authorised return of surplus.

The non-UK schemes' deficit improved by £19m during the year, due largely to a combination of favourable membership experience and positive asset performance.

IAS 19 sensitivities on UK schemes

	Assets	Liabilities
IAS 19 position at 31 December 2017 (£bn)	8.3	(8.3)
Sensitivities (£bn change in assets/ liabilities) ³ :		
Interest rates: -1% ⁴	+1.7	+1.7
Inflation: +1% ⁴	+1.0	+0.9
Equities: -15% ⁵	-0.1	-
'AA' credit spreads: -0.25%	+0.1	+0.4

¹ Actuarial gains/ (losses) include pension investment expenses, variance against expected returns, change in actuarial assumptions and experience losses

² Other movements include regular contributions, service/ administration costs, expected returns, interest costs and settlement gains/ (losses)

³ Sensitivities are rounded to the nearest £0.1 bn; for example, the net interest rate stress as modelled is circa £60m adverse

⁴ Actual net sensitivity to changes in interest rates and breakeven inflation will vary depending on size and direction of stress and is also highly dependent on the level of credit spreads at any point in time

⁵ Includes 15% reduction in equities and 10% reduction in all other 'growth' assets

REINSURANCE

Updates to our reinsurance programme for 2018 are outlined below.

The 3 year Group aggregate reinsurance cover that commenced in 2015 has been renewed until the end of 2020. The key terms of the new 3 year deal are as follows:

- Cover protects all of our short tail business including Property, Marine and Construction/ Engineering
- Events or individual net losses of £10m or greater are added together across our financial year. When a loss exceeds £10m it is included in full
- Cover attaches when the total of these retained losses is greater than £170m
- Limit of cover is £150m per year, with £300m maximum over the 3 year period
- Counterparties are high credit quality reinsurers (45% AA- or better, 46% A- or better, 9% collateralised).

Retentions for our UK and Ireland Motor programme have been reduced to £1m and €1m respectively (£3m and €3m respectively in 2017).

Outside of these, our key retentions remain unchanged at £75m for UK Cat; £50m for non-UK Cat (Canada/ US/ Caribbean C\$75m); maximum of £50m for Property Risk.

SEGMENTAL ANALYSIS

Management basis – 12 months ended 31 December 2016

	Scandinavia	Canada	UK & International	Central functions	Core Group	Disposals ¹	Group FY 2016
	£m	£m	£m	£m	£m	£m	£m
Net Written Premiums	1,721	1,443	3,081	36	6,281	127	6,408
Net Earned Premiums	1,735	1,454	3,173	(22)	6,340	188	6,528
Net Incurred Claims	(1,181)	(948)	(1,998)	18	(4,109)	(106)	(4,215)
Commissions	(60)	(191)	(636)	-	(887)	(54)	(941)
Operating expenses	(255)	(241)	(451)	(5)	(952)	(40)	(992)
Underwriting result ◇	239	74	88	(9)	392	(12)	380
Investment income	98	71	161	-	330	39	369
Investment expenses	(3)	(2)	(7)	-	(12)	-	(12)
Unwind of discount	(23)	(3)	(5)	-	(31)	(28)	(59)
Investment result ◇	72	66	149	-	287	11	298
Central expenses	-	-	-	(23)	(23)	-	(23)
Operating result ◇	311	140	237	(32)	656	(1)	655
Interest							(99)
Legacy sale							(204)
Other non-operating charges							(261)
Profit before tax							91
Tax							(71)
Profit after tax							20
Underlying profit before tax ◇							556
Loss ratio (%)	68.0	65.2	63.0	-	64.8	-	64.6
Weather loss ratio	0.4	5.7	2.7	-	2.6	-	2.5
Large loss ratio	5.0	6.4	12.1	-	9.2	-	8.9
Current year attritional loss ratio ◇	64.2	57.8	49.0	-	55.2	-	55.2
Prior year effect on loss ratio	(1.6)	(4.7)	(0.8)	-	(2.2)	-	(2.0)
Commission ratio (%)	3.4	13.1	20.0	-	14.0	-	14.4
Expense ratio (%)	14.8	16.6	14.2	-	15.0	-	15.2
Combined ratio (%) ◇	86.2	94.9	97.2	-	93.8	-	94.2
Earned controllable expense ratio (%) ◇	24.2	20.7	22.1	-	23.0		23.3

¹ Disposals comprise Latin America and Russia, both completed during 2016

COMBINED RATIO DETAIL

Group

£m unless stated		Current year	Prior year		2017 total	Current year	Prior year		2016 total
Net written premiums	1	6,659	7	19	13	6,678	6,438	(30)	6,408
Net earned premiums	2	6,590	8	15	14	6,605	6,542	(14)	6,528
Net incurred claims	3	(4,523)	9	173	15	(4,350)	(4,354)	139	(4,215)
Commissions	4	(883)	10	(28)	16	(911)	(929)	(12)	(941)
Operating expenses	5	(947)	11	(3)	17	(950)	(988)	(4)	(992)
Underwriting result ◇	6	237	12	157	18	394	271	109	380
CY attritional claims	19	(3,642)				(3,605)			
Weather claims	20	(168)				(166)			
Large losses	21	(713)				(583)			
Net incurred claims	22	(4,523)				(4,354)			
Loss ratio (%)		=15 / 14		23	65.9				64.6
Weather loss ratio		=20 / 2		24	2.6				2.5
Large loss ratio		=21 / 2		25	10.8				8.9
Current year attritional loss ratio ◇		=19 / 2		26	55.3				55.2
Prior year effect on loss ratio		=23 - 24 - 25 - 26		27	(2.8)				(2.0)
Commission ratio (%)		=16 / 14		28	13.7				14.4
Expense ratio (%)		=17 / 14		29	14.4				15.2
Combined ratio (%) ◇		=23 + 28 + 29		30	94.0				94.2

Scandinavia

£m unless stated		Current year	Prior year		2017 total	Current year	Prior year		2016 total
Net written premiums		1,837	(4)		1,833	1,721	-		1,721
Net earned premiums		1,837	(1)		1,836	1,735	-		1,735
Net incurred claims		(1,258)	61		(1,197)	(1,207)	26		(1,181)
Commissions		(59)	-		(59)	(60)	-		(60)
Operating expenses		(265)	-		(265)	(255)	-		(255)
Underwriting result		255	60		315	213	26		239
CY attritional claims		(1,151)				(1,114)			
Weather claims		(1)				(6)			
Large losses		(106)				(87)			
Net incurred claims		(1,258)				(1,207)			
Loss ratio (%)					65.2				68.0
Weather loss ratio					0.1				0.4
Large loss ratio					5.7				5.0
Current year attritional loss ratio					62.6				64.2
Prior year effect on loss ratio					(3.2)				(1.6)
Commission ratio (%)					3.2				3.4
Expense ratio (%)					14.5				14.8
Combined ratio (%)					82.9				86.2

COMBINED RATIO DETAIL

Canada

£m unless stated	Current Year	Prior year	2017 total	Current year	Prior year	2016 total
Net written premiums	1,619	-	1,619	1,447	(4)	1,443
Net earned premiums	1,591	-	1,591	1,458	(4)	1,454
Net incurred claims	(1,084)	45	(1,039)	(1,018)	70	(948)
Commissions	(212)	-	(212)	(196)	5	(191)
Operating expenses	(239)	(3)	(242)	(238)	(3)	(241)
Underwriting result	56	42	98	6	68	74
CY attritional claims	(904)			(842)		
Weather claims	(58)			(83)		
Large losses	(122)			(93)		
Net incurred claims	(1,084)			(1,018)		
Loss ratio (%)			65.3			65.2
Weather loss ratio			3.7			5.7
Large loss ratio			7.7			6.4
Current year attritional loss ratio			56.8			57.8
Prior year effect on loss ratio			(2.9)			(4.7)
Commission ratio (%)			13.4			13.1
Expense ratio (%)			15.2			16.6
Combined ratio (%)			93.9			94.9

Total UK&I

£m unless stated	Current year	Prior year	2017 total	Current year	Prior year	2016 total
Net written premiums	3,175	24	3,199	3,072	9	3,081
Net earned premiums	3,179	17	3,196	3,176	(3)	3,173
Net incurred claims	(2,238)	39	(2,199)	(2,026)	28	(1,998)
Commissions	(610)	(28)	(638)	(618)	(18)	(636)
Operating expenses	(441)	-	(441)	(450)	(1)	(451)
Underwriting result	(110)	28	(82)	82	6	88
UK & International proforma¹			(16)			
CY attritional claims	(1,593)			(1,554)		
Weather claims	(153)			(87)		
Large losses	(492)			(385)		
Net incurred claims	(2,238)			(2,026)		
Loss ratio (%)			68.8			63.0
Weather loss ratio			4.8			2.7
Large loss ratio			15.5			12.1
Current year attritional loss ratio			50.1			49.0
Prior year effect on loss ratio			(1.6)			(0.8)
Commission ratio (%)			20.0			20.0
Expense ratio (%)			13.8			14.2
Combined ratio (%)			102.6			97.2
UK & International proforma¹			100.5			

¹ Proforma for net aggregate reinsurance recovery and excludes the impact of the Ogden rate change

APPENDIX II
Alternative Performance Measures

JARGON BUSTER & ALTERNATIVE PERFORMANCE MEASURES

Set out below are explanations of the key technical terms and alternative performance measures (APMs) used within this report. APMs are complementary to measures defined within International Financial Reporting Standards (IFRS) and are used by management to explain the Group's business performance and financial position. They include common insurance industry metrics, as well as measures management and the Board consider are more representative of its underlying trading performance and that provide more meaningful comparisons between periods and business segments. APMs are identifiable within Group tables by the symbol \diamond , and those used to determine management and executive remuneration are identified below with \diamond^* . A reconciliation of APMs to their nearest IFRS Income Statement equivalents, detailing the adjustments made, can be found below.

Term	Definition	APM	Reconciliation	
Affinity	Selling insurance through a partner's distribution network, usually to a group of similar customers, e.g. store-card holders, alumni groups, unions and utility company customers.			
Attritional Loss Ratio	This is the underlying loss ratio (net incurred claims and claims handling expense as a proportion of net earned premium) of our business prior to volatile impacts from weather, large losses and prior-year reserve developments.	\diamond	I	R
Claims Frequency	Average number of claims per policy over the year.			
Claims Handling Expenses	The administrative cost of processing a claim (such as salary costs, costs of running claims centres, allocated share of the costs of head office units) which are separate to the cost of settling the claim itself with the policyholder.			
Claims Ratio (Loss Ratio)	Percentage of net earned premiums that is paid out in claims and claims handling expenses.	\diamond	I	V
Claims Reserve (Provision for Losses and Loss Adjustment Expenses)	A provision established to cover the estimated cost of claims payments and claims handling expenses that are still to be settled and incurred in respect of insurance cover provided to policyholders up to the reporting date.			
Claims Severity	Average cost of claims incurred over the period.			
Combined Operating Ratio (COR)	A measure of underwriting performance calculated on an 'earned' basis as follows: COR = loss ratio + commission ratio + expense ratio, where Loss ratio = net incurred claims / net earned premiums Commission ratio = commissions / net earned premiums Expense ratio = operating expenses / net earned premiums	\diamond^*	I	Y
Commission	An amount paid to an intermediary such as a broker for introducing business to the Group.			
Constant Exchange (CFX)	Prior period comparative retranslated at current period exchange rates.	\diamond	4	N/a
Controllable Costs / Expenses	A measure of operating expenses incurred by the Group in undertaking business activities, predominantly underwriting and policy acquisition costs, excluding commission and premium related costs such as levies. They are adjusted to include claims handling costs that are reported within net claims incurred.	\diamond^*	5	N/a
Current Year Underwriting Result	The profit or loss earned from business for which insurance cover has been provided during the current financial period.	\diamond	I	Q
Expense Ratio	Underwriting and policy expenses expressed as a percentage of net earned premium.	\diamond	I	X
Exposure	A measurement of risk we are exposed to through the premiums we have written. For example, in motor insurance one vehicle insured for one year is one unit of exposure.			
Financial Conduct Authority (FCA)	The regulatory authority with responsibility for the conduct of the UK financial services industry.			
Gross Written Premium (GWP)	Total revenue generated through sale of insurance products. This is before taking into account reinsurance and is stated irrespective of whether payment has been received.			
IBNR (Incurred But Not Yet Reported)	An estimated reserve for amounts owed to all valid claimants who have had a covered loss but have not yet reported it and for claims that have been reported but the cost is not yet known.			

Term	Definition	APM	Reconciliation		
Interest Costs	Interest costs represent the cost of Group debt excluding any debt buy back costs.	◇	I	O	
Investment Result	Investment result is the money we make from our investments on a management basis. It comprises the major component of net investment return, investment income, in addition to unwind of discount and investment expenses.	◇	I	AA	
Large Losses	Single claim or all claims arising from a single loss event with a net cost of £500k or higher.				
Large Loss Ratio	The large loss ratio is an expression of claims incurred in the period with a net cost of £500k or higher as a percentage of net earned premium over the same period.	◇	I	T	
Net Asset Value (NAV) per Share	Net asset value per share is calculated as closing shareholders' funds, less preference share capital, divided by the number of shares in issue at the end of the period.	◇	3	E	
Net Earned Premium (NEP)	The proportion of premium written, net of the cost of associated reinsurance, which represents the consideration charged to policyholders for providing insurance cover during the reporting period.				
Net Incurred Claims (NIC)	The total claims cost incurred in the period less any share that is borne by reinsurers. It includes both claims payments and movements in claims reserves and claims handling expenses in the period.				
Net Written Premium (NWP)	Premium written or processed in the period, irrespective of whether it has been paid, less the amount shared with reinsurers.				
Non-Operating Charges	Non-operating charges represent items that are excluded to arrive at the underlying profit after tax measure.	◇	I	AD	
	Item	Reason for classification			
	Gains and losses arising from the disposal of businesses	To allow assessment of the performance of ongoing business activities			
	Amortisation of intangible assets	To allow meaningful assessment of segmental performance where similar internally generated assets are not capitalised			
	Impairment of intangible assets	Where the impairment arises from restructuring activities			
	Reorganisation costs	To allow assessment of the performance of ongoing business activities	◇	I	AD
	Pension administration and net interest costs	Costs that are dependent on the level of defined benefit pension scheme plan funding and arise from servicing past pension commitments			
	Realised and unrealised gains and losses on investments / foreign exchange gains and losses	To remove the impact of market volatility and investment rebalancing activity			
Debt buy back costs	To allow meaningful assessment of ongoing finance costs				
Operating Profit	Operating profit is profit before tax less non-operating charges.	◇	I	AC	
Payout Ratio	Ordinary dividends expressed as a percentage of underlying profit after tax attributable to ordinary shareholders.				
Policies in Force	The number of active insurance policies for which Group is providing cover				
Prior Year Underwriting Result	Updates to premium, claims, commission and expense estimates relating to prior years.	◇	I	P	
Property and Casualty (P&C) (Non-Life Insurance or General Insurance)	Property insurance covers loss or damage through fire, theft, floods, storms and other specified risks. Casualty insurance primarily covers losses arising from accidents that cause injury to other people or damage to the property of others.				
Prudential Regulation Authority (PRA)	The regulatory authority with responsibility for the prudential regulation and supervision of the UK financial services industry.				

Term	Definition	APM	Reconciliation	
Pull to par	The movement of a bond's price toward its face value as it approaches its maturity date			
Rate	The price of a unit of insurance based on a standard risk for one year. Actual premium charged to the policyholder may differ from the rate due to individual risk characteristics and marketing discounts.			
Reinsurance	The practice whereby part or all of the risk accepted is transferred to another insurer (the reinsurer).			
Reported Exchange (RFX)	Prior period comparative translated at exchange rates applicable at that time.			
Return on Equity	Profit attributable to ordinary shareholders (profit after tax excluding non-controlling interests, coupon on tier 1 notes and preference dividend) expressed in relation to opening ordinary shareholders' funds (opening ordinary shareholders funds less preference share capital).	◇	2	F
Return on Tangible Equity	Profit attributable to ordinary shareholders (profit after tax excluding non-controlling interests, coupon on tier 1 notes and preference dividend) expressed in relation to opening tangible net asset value.	◇	2	H
Solvency II	Capital adequacy regime for the European insurance industry which commenced in 2016 and is based on a set of EU wide capital requirements and risk management standards.			
Scrip Dividend	Where shareholders choose to receive the dividend in the form of additional shares rather than cash. The Group would issue new shares to meet the scrip demand.			
Tangible Net Asset Value (TNAV)	Tangible net asset value comprises shareholders' equity, less preference share capital and goodwill and intangible assets.	◇*	3	C
Tangible Net Asset Value (TNAV) per Share	Tangible net asset value, divided by the number of shares in issue at the end of the period.	◇	3	F
Underlying Profit after Tax	This provides a key measure of shareholder value and one that informs overall valuation in the insurance sector. It takes profit after tax, excluding the proportion that is attributable to non-controlling interests, preference shareholders and Tier 1 note holders and adds back the after tax impact of non-operating charges.	◇*	2	B
Underlying Return on Equity	Underlying profit after tax expressed in relation to opening shareholders' funds excluding preference share capital.	◇	2	G
Underlying Return on Tangible Equity	A key measure of shareholder value and one that informs overall valuation in the insurance sector. Underlying profit after tax expressed in relation to opening tangible net asset value.	◇*	2	I
Underlying Tax Rate	The underlying Core Group tax rate mainly comprising the local statutory tax rates in the Group's territories applied to underlying regional profits (operating profits less interest costs).	◇	6	A
Underlying Earnings per Share (EPS)	A key measure of the underlying earnings power of the group as it excludes shorter-term and temporary changes, such as restructuring costs. Underlying earnings per share is calculated as underlying profit after tax divided by the weighted average number of shares in issue during the period.	◇	2	K
Underwriting Result	A measure of underwriting performance calculated as net earned premium less net claims and underwriting and policy acquisition costs.	◇	I	Z
Unearned Premium	The portion of a premium that relates to future periods, for which protection has not yet been provided, irrespective of whether the premium has been paid or not.			
Weather Losses	Weather claims incurred with a net cost of £500k or higher.			
Weather Loss Ratio	The weather loss ratio is an expression of weather losses in the period with a net cost of £500k or higher as a percentage of earned premium.	◇	I	S
Yield	Rate of return on an investment in percentage terms. The dividend payable on a share expressed as a percentage of the market price.			

I. IFRS reconciliation to management P&L for the 12 months ended 31 December 2017

£'m	IFRS			Management					Profit before tax
	Continuing	Discontinued	Total	Underwriting result	Investment result	Central costs	Operating result	Non-operating charges	
Income									
Gross written premiums	7,599	-	7,599	7,599					
Less: reinsurance premiums	(921)	-	(921)	(921)					
Net written premiums	6,678	-	6,678	6,678					
Change in the gross provision for unearned premiums	(16)	-	(16)	(16)					
Less: change in provision for unearned reinsurance premiums	(57)	-	(57)	(57)					
Change in provision for unearned premiums	(73)	-	(73)	(73)					
Net earned premiums, analysed as	6,605	-	6,605	A 6,605					
Current year				B 6,590					
Prior year				C 15					
Investment income	331	-	331	D 6,605	331				
Realised gains on investments	19	-	19					19	
Gains / (losses) on forex derivatives	(5)	-	(5)					(5)	
Unrealised gains / (losses)	1	-	1					1	
Impairments	4	-	4					4	
Net investment return	350	-	350						
Other insurance income	146	-	146	E 146					
Other non-insurance income	4	-	4			4			
Foreign exchange gain	-	-	-					-	
Other operating income	150	-	150						
Total income	7,105	-	7,105						
Expenses									
Gross claims incurred	(5,136)	-	(5,136)	(5,136)					
Less: claims recoveries from reinsurers	786	-	786	786					
Net claims, analysed as	(4,350)	-	(4,350)	F (4,350)					
Attritional				G (3,642)					
Weather				H (168)					
Large				I (713)					
Prior year				J 173					
Earned CY commission	(883)	-	(883)	K (883)					
Earned PY commission	(28)	-	(28)	L (28)					
Earned CY operating expenses	(1,093)	-	(1,093)	M (1,093)					
Earned PY operating expenses	(3)	-	(3)	N (3)					
Underwriting and policy acquisition costs	(2,007)	-	(2,007)	(2,007)					
Unwind of discount	(34)	-	(34)		(34)				
Investment expenses	(13)	-	(13)		(13)				
Non-insurance expenses	(3)	-	(3)			(3)			
Central expenses	(17)	-	(17)			(17)			
Amortisation of intangible assets	(15)	-	(15)					(15)	
Pension net interest and administration costs	(7)	-	(7)					(7)	
Reorganisation costs	(155)	-	(155)					(155)	
Foreign exchange losses	(1)	-	(1)					(1)	
Impairment of intangibles	(23)	-	(23)					(23)	
Other operating expenses	(234)	-	(234)						
	(6,625)	-	(6,625)						
Interest costs	(43)	-	(43)					(43)	
Debt buy back costs	(59)	-	(59)					(59)	
Finance costs	(102)	-	(102)					(102)	
Acquisitions and disposals	69	-	69					69	
Net share of profit after tax of associates	1	-	1						
Profit / (Loss) before tax	448	-	448	394	284	(15)	663	(215)	448
Income tax expense	(126)	-	(126)	Z	AA	AB	AC	AD	
Profit / (Loss) for the year	322	-	322						
			C+J+L+N	P 157	PY Underwriting				
			Z - P	Q 237	CY Underwriting				
				394					
Attritional loss ratio		G / B	R	55.3%					
Weather loss ratio		H / B	S	2.6%					
Large loss ratio		I / B	T	10.8%					
Prior year loss ratio		V-R-S-T	U	(2.8%)					
Loss ratio		F/A	V	65.9%					
Commission ratio		(K+L) / A	W	13.7%					
Expense ratio		(E+M+N) / A	X	14.4%					
Combined operating ratio		V + W + X	Y	94.0%					

I. IFRS reconciliation to management P&L for the 12 months ended 31 December 2016

£'m	IFRS			Management					
	Continuing	Discontinued	Total	Underwriting result	Investment result	Central costs	Operating result	Non-operating charges	Profit before tax
Income									
Gross written premiums	7,220	256	7,476	7,476					
Less: reinsurance premiums	(981)	(87)	(1,068)	(1,068)					
Net written premiums	6,239	169	6,408	6,408					
Change in the gross provision for unearned premiums	109	38	147	147					
Less: change in provision for unearned reinsurance premiums	(8)	(19)	(27)	(27)					
Change in provision for unearned premiums	101	19	120	120					
Net earned premiums, analysed as	6,340	188	6,528	6,528					
Current year				6,542					
Prior year				(14)					
				6,528					
Investment income	355	14	369		369				
Realised gains on investments	28	2	30					30	
Gains / (losses) on forex derivatives	(41)		(41)					(41)	
Unrealised gains / (losses)	(3)		(3)					(3)	
Impairments	8		8					8	
Net investment return	347	16	363						
Other insurance income	133		133						
Other non-insurance income	5		5						
Foreign exchange gain	32		32			5			32
Other operating income	170	-	170						
Total income	6,857	204	7,061						
Expenses									
Gross claims incurred	(4,826)	(304)	(5,130)	(5,130)					
Less: claims recoveries from reinsurers	707	208	915	915					
Net claims, analysed as	(4,119)	(96)	(4,215)	(4,215)					
Attritional				(3,605)					
Weather				(166)					
Large				(583)					
Prior year				139					
				(4,215)					
Earned CY commission	(873)	(56)	(929)	(929)					
Earned PY commission	(12)		(12)	(12)					
Earned CY operating expenses	(1,088)	(33)	(1,121)	(1,121)					
Earned PY operating expenses	(4)		(4)	(4)					
Underwriting and policy acquisition costs	(1,977)	(89)	(2,066)	(2,066)					
Unwind of discount	(59)	(5)	(64)		(59)			(5)*	
Investment expenses	(12)		(12)		(12)				
Non-insurance expenses	(5)		(5)			(5)			
Central expenses	(23)		(23)			(23)			
Amortisation of intangible assets	(16)		(16)					(16)	
Pension net interest and administration costs	(4)		(4)					(4)	
Reorganisation costs	(161)	(7)	(168)					(168)	
Solvency II costs	(7)		(7)					(7)	
Impairment of intangibles	(1)		(1)					(1)*	
Other operating expenses	(229)	(7)	(236)						
	(6,384)	(197)	(6,581)						
Interest costs	(99)		(99)					(99)	
Debt buy back costs	(39)		(39)					(39)	
Finance costs	(138)	-	(138)					(138)	
Acquisitions and disposals	(234)	(17)	(251)					(251)	
Net share of profit after tax of associates	-	-	-						
Profit / (Loss) before tax	101	(10)	91	380	298	(23)	655	(564)	91
Income tax expense	(54)	(17)	(71)	Z	AA	AB	AC	AD	
Profit / (Loss) for the year	47	(27)	20						
			C+J+L+N	P	109				
			Z - P	Q	271				
					380				
Attritional loss ratio		G / B	R	55.2%					
Weather loss ratio		H / B	S	2.5%					
Large loss ratio		I / B	T	8.9%					
Prior year loss ratio		V-R-S-T	U	(2.0%)					
Loss ratio		F/A	V	64.6%					
Commission ratio		(K+L) / A	W	14.4%					
Expense ratio		(E+M+N) / A	X	15.2%					
Combined operating ratio		V + W + X	Y	94.2%					

* £5m of discount unwind reported as economic assumption changes

2. Metric calculations		2017	2016
		£m	£m
	Profit after tax	322	20
	Less: non-controlling interest	(33)	7
	Less: coupon on 2017 issued restricted tier 1 instrument	(11)	-
	Less: preference dividend	(9)	(9)
	A Profit attributable to ordinary shareholders	269	18
APM Rec 1	Add: non-operating charges	215	564
	Add: non-controlling interest share of non-operating charges	13	(19)
APM Rec 1	Less: interest costs	(43)	(99)
APM Rec 6	Less: underlying tax differential	(10)	(62)
	B Underlying profit after tax attributable to ordinary shareholders	444	402
	Opening shareholders' funds	3,715	3,642
	Less: preference share capital	(125)	(125)
	C Opening ordinary shareholders' funds	3,590	3,517
Note 11	Less: opening goodwill and intangibles	(728)	(679)
	D Opening tangible ordinary shareholders' funds	2,862	2,838
	E Weighted average no. share issue during the period (un-diluted)	1,021	1,018
	Return on equity		
A/C	F Reported	7.5%	0.5%
B/C	G Underlying	12.4%	11.4%
	Return on tangible equity		
A/D	H Reported	9.4%	0.6%
B/D	I Underlying	15.5%	14.2%
	Earnings per share		
A/E	J Basic earnings per share	26.3	1.8
B/E	K Underlying earnings per share	43.5	39.5
3. Balance sheet reconciliations		2017	2016
		£m	£m
	A Closing shareholders' funds	3,653	3,715
	Less: preference share capital	(125)	(125)
	B Ordinary shareholders funds	3,528	3,590
Note 23	Less: closing goodwill and intangibles	(763)	(728)
	C Tangible net asset value	2,765	2,862
	D Shares in issue at the period end	1,023	1,019
B/D	E Net asset value per share	345	352
C/D	F Tangible net asset value per share	270	281
4. Net written premium movement and constant exchange		2017	2016
		£m	£m
	Total net written premium	6,678	6,408
	Discontinued net written premium	-	(169)
	Continuing net written premium	6,678	6,239
	Disposals of continuing operations	-	42
Note 9	A Core net written premiums	6,678	6,281
	YOY movement	397	378
	Comprised of:		
	Volume change including portfolio actions and reinsurance	(25)	(137)
	Rate increases	163	141
	B Movement at constant exchange	138	4
	Foreign exchange	259	374
	Total movement	397	378
B/A	C % movement at constant exchange	2%	0%

5. Controllable expenses		2017	2016
		£m	£m
	Underwriting and policy admin costs	(2,007)	(2,066)
APM Rec I	Less: commission	911	941
	Less: non controllable premium related costs e.g. levies	130	112
	Add: claims expenses within net claims	(406)	(424)
APM Rec I	Add: investment expenses	(13)	(12)
APM Rec I	Add: central expenses	(17)	(23)
	Add: other	(23)	(43)
A	Written controllable expense base	(1,425)	(1,515)
	Less: controllable deferred acquisition costs	8	(6)
B	Earned controllable expense base	(1,417)	(1,521)
C	Net written premiums	6,678	6,408
D	Net earned premiums	6,605	6,528
A/C	E Written controllable expense ratio	21.3%	23.7%
B/D	F Earned controllable expense ratio	21.5%	23.3%

6. Underlying tax rate		2017	2016
		%	%
	Effective tax rate (ETR)	28	78
	Less tax effect of:		
	Withholding tax on intercompany dividend	(5)	-
	Unrecognised tax losses	(1)	(11)
	Underlying versus IFRS regional profit mix	(1)	(27)
	Tax on disposals	0	(13)
	Other	1	(3)
A	Underlying tax rate	22	24
		£m	£m
APM Rec I	Operating profit	663	655
APM Rec I	Less interest costs	(43)	(99)
	B Underlying profit before tax	620	556
AxB	C Underlying tax	(136)	(133)
	Tax	(126)	(71)
D	Underlying tax differential	(10)	(62)

7. COR proforma		Reported	Ogden	GVC	Proforma
UK & International					
A	Net earned premium £m	3,196		(23)	3,173
B	Underwriting result £m	(82)	23	43	(16)
1-(B/A)	C COR %	102.6			100.5
UK					
A	Net earned premium £m	2,684		(23)	2,661
B	Underwriting result £m	(116)	20	43	(53)
1-(B/A)	C COR %	104.3			102.0

REPORTING AND DIVIDEND TIMETABLE

Reporting:

Q1 2018 trading update 10 May 2018

Dividend:

Final ordinary dividend for the period ended 31 December 2017

Announcement date	22 February 2018
Ex-dividend date	1 March 2018
Record date	2 March 2018
Dividend payment date	18 May 2018

1st preference dividend

Announcement date	22 February 2018
Ex-dividend date	1 March 2018
Record date	2 March 2018
Dividend payment date	3 April 2018

Note: The final ordinary dividend is conditional upon the directors being satisfied, in their absolute discretion, that the payment of the interim ordinary dividend would not breach any legal or regulatory requirements, including Solvency II regulatory capital requirements.

PREFERENCE SHARE DIVIDEND

In accordance with the original subscription terms, qualifying registered holders of the 7 3/8 percent cumulative irredeemable preference shares of £1 each will receive the first preference dividend at a rate of 3.6875p per share.

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Further information

A live webcast of the analyst presentation, including the question and answer session, will be broadcast on the website at 09:00am on 22 February 2018. A webcast and transcript of the presentation will be available via the company website (www.rsagroup.com).

Important disclaimer

This press release and the associated conference call may contain ‘forward-looking statements’ with respect to certain of the Group’s plans and its current goals and expectations relating to its future financial condition, performance, results, strategic initiatives and objectives. Generally, words such as “may”, “could”, “will”, “expect”, “intend”, “estimate”, “anticipate”, “aim”, “outlook”, “believe”, “plan”, “seek”, “continue” or similar expressions identify forward-looking statements. These forward-looking statements are not guarantees of future performance. By their nature, all forward-looking statements are inherently predictive and speculative and involve risk and uncertainty because they relate to future events and circumstances which are beyond the Group’s control, including amongst other things, UK domestic and global economic business conditions, market-related risks such as fluctuations in interest rates and exchange rates, the policies and actions of regulatory authorities, the impact of competition, inflation, deflation, the timing impact and other uncertainties of future acquisitions or combinations within relevant industries, as well as the impact of tax and other legislation or regulations in the jurisdictions in which the Group and its affiliates operate. As a result, the Group’s actual future financial condition, performance and results may differ materially from the plans, goals and expectations set forth in the Group’s forward-looking statements. Forward-looking statements in this press release are current only as of the date on which such statements are made. The Group undertakes no obligation to update any forward-looking statements, save in respect of any requirement under applicable law or regulation. Nothing in this press release shall be construed as a profit forecast.

CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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CONDENSED CONSOLIDATED INCOME STATEMENT
STATUTORY BASIS
for the year ended 31 December 2017

	Note	2017 £m	2016 £m
Income			
Gross written premiums		7,599	7,220
Less: reinsurance premiums		(921)	(981)
Net written premiums	7	6,678	6,239
Change in gross provision for unearned premiums		(16)	109
Less: change in provision for unearned reinsurance premiums		(57)	(8)
Change in provision for unearned premiums		(73)	101
Net earned premiums		6,605	6,340
Net investment return		350	347
Other operating income		150	170
Total income		7,105	6,857
Expenses			
Gross claims incurred		(5,136)	(4,826)
Less: claims recoveries from reinsurers		786	707
Net claims		(4,350)	(4,119)
Underwriting and policy acquisition costs		(2,007)	(1,977)
Unwind of discount		(34)	(59)
Other operating expenses, reorganisation costs and impairments		(234)	(229)
		(6,625)	(6,384)
Finance costs		(102)	(138)
Profit on disposal of business and realised gains on held for sale assets	5(c)	69	-
Remeasurement of disposal groups	5(d)	-	(234)
Net share of profit after tax of associates		1	-
Profit before tax	7	448	101
Income tax expense	8	(126)	(54)
Profit after tax from continuing operations		322	47
(Loss) from discontinued operations, net of tax	5(a)	-	(27)
Profit for the year		322	20
Attributable to:			
Equity holders of the Parent Company		289	27
Non-controlling interests		33	(7)
		322	20
Earnings per share on profit attributable to the ordinary shareholders of the Parent Company:			
Basic			
From continuing operations	9	26.3p	4.4p
From discontinued operations	9	-	(2.6)p
		26.3p	1.8p
Diluted			
From continuing operations	9	26.1p	4.4p
From discontinued operations	9	-	(2.6)p
		26.1p	1.8p
Ordinary dividends paid and proposed for the year			
Interim dividend paid	10	6.6p	5.0p
Final dividend proposed	10	13.0p	11.0p

The attached notes on pages 45 to 85 form an integral part of these consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
STATUTORY BASIS
for the year ended 31 December 2017

	Note	2017 £m	2016 £m
Profit for the year		322	20
Items from continuing operations that may be reclassified to the income statement:			
Exchange (losses)/gains net of tax on translation of foreign operations		(36)	228
Fair value (losses)/gains on available for sale financial assets net of tax		(197)	151
		(233)	379
Items from continuing operations that will not be reclassified to the income statement:			
Pension - remeasurement of net defined benefit asset/liability net of tax		44	(316)
Movement in property revaluation surplus net of tax		2	1
		46	(315)
Other comprehensive (expense)/income for the year from continuing operations		(187)	64
Other comprehensive income for the year from discontinued operations	5(a)	-	120
Total other comprehensive (expense)/income for the year		(187)	184
Total comprehensive income for the year from continuing operations		135	111
Total comprehensive income for the year from discontinued operations	5(a)	-	93
Total comprehensive income for the year		135	204
Attributable to:			
Equity holders of the Parent Company			
from continuing operations		117	98
from discontinued operations		-	94
		117	192
Non-controlling interests			
from continuing operations		18	13
from discontinued operations		-	(1)
		18	12
		135	204

The attached notes on pages 45 to 85 form an integral part of these consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY STATUTORY BASIS

for the year ended 31 December 2017

	Ordinary share capital	Ordinary share premium	Own shares	Preference shares	Revaluation reserves	Capital redemption reserve	Foreign currency translation reserve	Retained earnings	Share- holders' equity	Tier I notes	Non- controlling interests	Total equity
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Balance at 1 January 2016	1,017	1,077	(1)	125	293	389	(221)	963	3,642	-	129	3,771
Total comprehensive income												
Profit for the year	-	-	-	-	-	-	-	27	27	-	(7)	20
Other comprehensive income/(expense)	-	-	-	-	181	-	299	(315)	165	-	19	184
	-	-	-	-	181	-	299	(288)	192	-	12	204
Transactions with owners of the Group												
Contribution and distribution												
Dividends (note 10)	-	-	-	-	-	-	-	(131)	(131)	-	(3)	(134)
Shares issued for cash (note 17)	2	3	-	-	-	-	-	-	5	-	-	5
Share based payments (note 17)	1	-	-	-	-	-	-	15	16	-	-	16
Other reserve transfer	-	-	-	-	28	-	-	(28)	-	-	-	-
	3	3	-	-	28	-	-	(144)	(110)	-	(3)	(113)
Changes in shareholders' interests in subsidiaries	-	-	-	-	(6)	-	-	(3)	(9)	-	(6)	(15)
Total transactions with owners of the Group	3	3	-	-	22	-	-	(147)	(119)	-	(9)	(128)
Balance at 1 January 2017	1,020	1,080	(1)	125	496	389	78	528	3,715	-	132	3,847
Total comprehensive income												
Profit for the year	-	-	-	-	-	-	-	289	289	-	33	322
Other comprehensive income/(expense)	-	-	-	-	(192)	-	(24)	44	(172)	-	(15)	(187)
	-	-	-	-	(192)	-	(24)	333	117	-	18	135
Transactions with owners of the Group												
Contribution and distribution												
Dividends (note 10)	-	-	-	-	-	-	-	(200)	(200)	-	(10)	(210)
Shares issued for cash (note 17)	1	3	-	-	-	-	-	-	4	-	-	4
Share based payments (note 17)	2	-	-	-	-	-	-	14	16	-	-	16
Issue of Tier I notes (note 18)	-	-	-	-	-	-	-	-	-	297	-	297
Other reserve transfer	-	-	-	-	(7)	-	-	7	-	-	-	-
	3	3	-	-	(7)	-	-	(179)	(180)	297	(10)	107
Changes in shareholders' interests in subsidiaries	-	-	-	-	-	-	-	1	1	-	12	13
Total transactions with owners of the Group	3	3	-	-	(7)	-	-	(178)	(179)	297	2	120
Balance at 31 December 2017	1,023	1,083	(1)	125	297	389	54	683	3,653	297	152	4,102

The attached notes on pages 45 to 85 form an integral part of these consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION
STATUTORY BASIS
as at 31 December 2017

	Note	2017 £m	2016 £m
Assets			
Goodwill and other intangible assets	11	763	728
Property and equipment		104	109
Investment property		308	333
Investments in associates		13	12
Financial assets	12	11,643	12,325
Total investments		11,964	12,670
Reinsurers' share of insurance contract liabilities	14	2,252	2,252
Insurance and reinsurance debtors		2,923	2,823
Deferred tax assets	15	276	270
Current tax assets	15	43	65
Other debtors and other assets		559	430
Other assets		878	765
Cash and cash equivalents	16	1,048	985
		19,932	20,332
Assets of operations classified as held for sale	5(b)	668	807
Total assets		20,600	21,139
Equity and liabilities			
Equity			
Shareholders' equity		3,653	3,715
Tier 1 notes	18	297	-
Non-controlling interests		152	132
Total equity		4,102	3,847
Liabilities			
Loan capital	19	441	1,068
Insurance contract liabilities	20	12,793	12,676
Insurance and reinsurance liabilities	20	934	954
Borrowings		123	251
Deferred tax liabilities	15	56	54
Current tax liabilities	15	24	32
Provisions		407	420
Other liabilities		1,052	1,087
Provisions and other liabilities		1,539	1,593
		15,830	16,542
Liabilities of operations classified as held for sale	5(b)	668	750
Total liabilities		16,498	17,292
Total equity and liabilities		20,600	21,139

The attached notes on pages 45 to 85 form an integral part of these consolidated financial statements.

The financial statements were approved on 21 February 2018 by the Board of Directors and are signed on its behalf by:

Scott Egan
Group Chief Financial Officer

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
STATUTORY BASIS
for the year ended 31 December 2017

	Note	2017 £m	Re-presented ¹ 2016 £m
Cash flows from operating activities			
Cash generated from operating activities	22	469	71
Tax paid		(104)	(88)
Net cash flows from operating activities - continuing operations		365	(17)
Net cash flows from operating activities - discontinued operations		-	(18)
Cash flows from investing activities			
Proceeds from sales or maturities of:			
Financial assets		3,030	3,747
Investment property		28	28
Property and equipment		-	10
Sale of subsidiaries (net of cash disposed of)		15	-
Purchase of:			
Financial assets		(2,406)	(3,589)
Property and equipment		(18)	(25)
Intangible assets		(131)	(139)
Cash element of reinsurance premium on UK Legacy assets	5(b)	(96)	-
Net cash flows from investing activities - continuing operations		422	32
Net cash flows from investing activities - discontinued operations		-	333
Cash flows from financing activities			
Proceeds from issue of share capital		4	5
Proceeds from issue of Tier 1 notes	18	297	-
Dividends paid to ordinary shareholders		(180)	(122)
Coupon payment on Tier 1 notes		(11)	-
Dividends paid to preference shareholders		(9)	(9)
Dividends paid to non-controlling interests		(10)	(3)
Redemption of debt instruments	19	(636)	(200)
Net movement in other borrowings		(136)	242
Interest paid		(133)	(150)
Net cash flows from financing activities - continuing operations		(814)	(237)
Net cash flows from financing activities - discontinued operations		-	-
Net (decrease)/increase in cash and cash equivalents		(27)	93
Cash and cash equivalents at the beginning of the year		1,087	902
Effect of changes in foreign exchange on cash and cash equivalents		(11)	92
Cash and cash equivalents at the end of the year	16	1,049	1,087

¹ A reconciliation of net profit before tax to cash flow from operating activities is now shown as a separate note.

The attached notes on pages 45 to 85 form an integral part of these consolidated financial statements.

BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

RSA Insurance Group Plc (the 'Company') is a public limited company incorporated and domiciled in England and Wales. The Company through its subsidiaries and associates (together the 'Group' or 'RSA') provides personal and commercial insurance products to its global customer base, principally in the UK, Ireland, Middle East (together 'UK & International'), Scandinavia and Canada.

1. BASIS OF PREPARATION

The consolidated financial statements within the full Annual Report and Accounts, from which the financial information within this preliminary announcement has been extracted, have been prepared on a going concern basis and in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union (EU) and the Companies Act 2006 where applicable. The consolidated financial statements are prepared on a historical cost basis. Where other bases are applied these are identified in the relevant accounting policy. The condensed consolidated financial information in this report has been prepared by applying the accounting policies used in the 2017 Annual Report and Accounts (see note 22).

In line with industry practice, the Group's statement of financial position is not presented using current and non-current classifications, but broadly in increasing order of liquidity.

The assets and liabilities considered as non-current include: investments in associates, deferred tax assets, property and equipment, intangible assets, goodwill, deferred tax liabilities, outstanding debt including loan capital and elements of financial investments, insurance contract liabilities and reinsurers' share of insurance contract liabilities.

The assets and liabilities considered as current include cash and cash equivalents, and insurance and reinsurance debtors.

The remaining balances are of a mixed nature. The current and non-current portions of such balances are set out in the respective notes or in the Risk Management note (note 4).

Except where otherwise stated, all figures included in the consolidated financial statements are presented in millions of pounds sterling (£m).

Estimation techniques and assumptions are presented in the relevant note in order to provide context to the figures presented. The most significant estimates and judgements are those used in determining insurance contract liabilities (note 20), deferred tax (note 15) and defined benefit pension scheme liabilities (note 21).

2. ADOPTION OF NEW AND REVISED STANDARDS

There are a small number of narrow scope amendments arising from annual improvements to standards that are applicable to the Group for the first time in 2017, none of which have had a significant impact on the consolidated financial statements.

3. NEW ACCOUNTING STANDARDS, INTERPRETATIONS AND AMENDMENTS

IFRS 17 'Insurance Contracts'

The International Accounting Standards Board (IASB) issued IFRS 17 'Insurance Contracts' in May 2017, which it is expected will replace IFRS 4 'Insurance Contracts' at the latest for annual reporting periods beginning on or after 1 January 2021. A Transitional Resource Group has been set up by the IASB to support implementation of the new standard. The European Financial Reporting Advisory Group (EFRAG) have been requested by the European Commission to provide their advice by the end of 2018 which should lead to endorsement some time in 2019. There is currently no certainty at the moment of what the endorsement process will be if this has not happened by the time the UK leaves the EU and RSA will continue to monitor this.

The Group has completed its initial impact assessment and is using these results to inform a detailed planning phase which is underway. During this phase decisions will be made on appropriate policies to adopt and the required change to Finance systems and processes. The Group intends to start implementation activities in 2018 and intends to parallel run systems and reporting during 2020 to assure reporting compliance by 1 January 2021.

IFRS 9 'Financial Instruments'

IFRS 9 'Financial Instruments' has been issued to replace IAS 39 'Financial Instruments: Recognition and Measurement' and primarily changes the classification and measurement of financial assets, depending on the business model under which they are held, as well as hedge accounting requirements and recognising expected credit losses.

The Group, in line with peers, will take advantage of the exemption available to entities whose activities are predominantly insurance related to defer applying IFRS 9 'Financial Instruments' (which would otherwise be applicable for annual reporting periods beginning on or after 1 January 2018) until 1 January 2021 which will coincide with the expected implementation of IFRS 17. This will enable accounting policy choices to consider the interrelationships of IFRS 17 and 9 particularly with regards to asset and liability management. Assessment and implementation of IFRS 9 will therefore run alongside IFRS 17 activity.

IFRS 15 'Revenue Recognition'

IFRS 15 'Revenue Recognition' is effective from 1 January 2018 and does not apply to insurance and financial instrument income. The impact of IFRS 15 on the recognition of relevant revenue has been evaluated during the year with no significant changes identified.

IFRS 16 'Leases'

IFRS 16 'Leases' replaces the existing standard IAS 17 'Leases' and standardises lessee treatment of leases and becomes effective at the latest for periods beginning on or after 1 January 2019. The standard requires a lessee to recognise a right-of-use asset representing its right to use the underlying asset and a lease liability representing the corresponding obligation to make lease payment. In addition, the nature of expenses related to those leases will now change as IFRS 16 replaces the straight line operating lease expense with a depreciation charge for the right-of-use assets and interest expense on the lease liabilities.

The Group has completed an initial assessment of the potential impact of adopting the standard but has still to complete its detailed assessment or to incorporate into its financial reporting systems and processes, which will take place during 2018. The actual impact of implementing IFRS 16 on the Group's financial statements will depend on future economic conditions, including the Group's borrowing rate at 1 January 2019, the composition of the Group's lease portfolio at that date, the Group's latest assessment of whether it will exercise any lease renewal options and the extent to which the group chooses to use practical expedients and recognition exemptions.

Other standards

The following amended standards and interpretations are not expected to have a significant impact on the Group's consolidated financial statements:

- Annual improvement to IFRSs 2014-2016 Cycle –Amendments to IFRS 1 and IAS 28
- Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2)
- Transfers of Investment Property (Amendments to IAS 40)
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28)
- IFRIC 22 Foreign Currency Transactions and Advance Consideration
- IFRIC 23 Uncertainty over Income Tax Treatments

RISK MANAGEMENT

4. RISK MANAGEMENT

Insurance Risk

The Group is exposed to risks arising from insurance contracts as set out below:

- A) Underwriting risk
- B) Reserving risk

A) Underwriting risk

Underwriting risk refers to the risk that claims arising are higher (or lower) than assumed in pricing due to bad experience including catastrophes, weakness in controls over underwriting or portfolio management, or claims management issues.

The majority of underwriting risk to which the Group is exposed is of a short-term nature, and generally does not exceed 12 months. The Group's underwriting strategy aims to ensure that the underwritten risks are well diversified in terms of the type, amount of risk, and geography in order to ensure that the Group minimises the volatility of its insurance result.

Underwriting limits are in place to enforce appropriate risk selection criteria and pricing with all of the Group's underwriters having specific licences that set clear parameters for the business they can underwrite, based on their expertise.

The Group has developed enhanced methods of recording exposures and concentrations of risk and has a centrally managed forum looking at Group underwriting issues, reviewing and agreeing underwriting direction and setting policy and directives where appropriate. The Group has a quarterly portfolio management process across all its business units where key risk indicators are tracked to monitor emerging trends, opportunities and risks. This provides greater control of exposures in high risk areas as well as enabling a prompt response to adverse claims development.

Pricing for the Group's products is generally based upon historical claims frequencies and claims severity averages, adjusted for inflation and modelled catastrophes, trended forward to recognise anticipated changes in claims patterns after making allowance for other costs incurred by the Group, conditions in the insurance market and a profit loading that adequately covers the cost of capital.

Decisions on how much insurance risk to pass on to other insurers through the use of reinsurance is another key strategy employed in managing the Group's exposure to insurance risk. The Group Board determines a maximum and the Group Corporate Centre determines a minimum level of risk to be retained by the Group as a whole and, therefore, the amount of central reinsurance cover purchased. This is then distributed across the Group in accordance with deemed risk appetite. Local operations may also purchase additional reinsurance within agreed local reinsurance appetite parameters.

Reinsurance arrangements in place include proportional, excess of loss, stop loss, catastrophe and adverse development coverage. These arrangements aim to prevent the Group suffering total net insurance losses beyond the Group's risk appetite in any one year.

The Group remains primarily liable as the direct insurer on all risks reinsured, although the reinsurer is liable to the Group to the extent of the insurance risk it has contractually accepted responsibility for.

B) Reserving risk

Reserving risk refers to the risk that the Group's estimates of future claims payments will be insufficient.

The Group establishes a provision for losses and loss adjustment expenses for the anticipated costs of all losses that have already occurred but have not yet been paid. Such estimates are made for losses already reported to the Group as well as for the losses that have already occurred but are not yet reported losses together with a provision for the future costs of handling and settling the outstanding claims.

There is a risk to the Group from the inherent uncertainty in estimating provisions at the end of the reporting period for the eventual outcome of outstanding notified claims as well as estimating the number and value of claims that are still to be notified.

4. RISK MANAGEMENT (CONTINUED)

The Group seeks to reduce its reserving risk through the use of experienced regional actuaries who estimate the actuarial indication of the required reserves based on claims experience, business volume, anticipated change in the claims environment and claims cost. This information is used by local reserving committees to recommend to the Group Reserving Committee the appropriate level of reserves for each region. This will include adding a margin onto the actuarial indication as a provision for unforeseen developments such as future claims patterns differing from historical experience, future legislative changes and the emergence of latent exposures. The Group Reserving Committee review these local submissions and recommend the final level of reserves to be held by the Group. The Group has a Group Reserving Committee which is chaired by the Group Chief Financial Officer and includes the Group Chief Executive, Group Underwriting Director, Group Chief Actuary and Group Chief Risk Officer. A similar committee has been established in each of the Group's primary operating segments. The Group Reserving Committee monitors the decisions and judgements made by the business units as to the level of reserves to be held. It then recommends to the Group Board via the Group Audit Committee the final decision on the level of reserves to be included within the consolidated financial statements. In forming its collective judgement, the Committee considers the following information:

- The actuarial indication of ultimate losses together with an assessment of risks and possible favourable or adverse developments that may not have been fully reflected in calculating these indications. At the end of 2017, these risks and developments include: the possibility of future legislative change having retrospective effect on open claims; changes in claims settlement procedures potentially leading to future claims payment patterns differing from historical experience; the possibility of new types of claim, such as disease claims, emerging from business written several years ago; general uncertainty in the claims environment; the emergence of latent exposures; the outcome of litigation on claims received; failure to recover reinsurance and unanticipated changes in claims inflation;
- The views of internal peer reviewers of the reserves and of other parties including actuaries, legal counsel, risk directors, underwriters and claims managers;
- The outcome from independent assurance reviews performed by the Group actuarial function to assess the reasonableness of regional actuarial indication estimates;
- How previous actuarial indications have developed.

Financial risk

Financial risk refers to the risk of financial loss predominantly arising from investment transactions entered into by the Group, and also to a lesser extent arising from insurance contracts, and includes the following risks:

- Credit risk;
- Market risk including price, interest rate and currency rate risks;
- Liquidity risk.

The Group undertakes a number of strategies to manage these risks including the use of derivative financial instruments for the purpose of reducing its exposure to adverse fluctuations in interest rates, foreign exchange rates and long term inflation. The Group does not use derivatives to leverage its exposure to markets and does not hold or issue derivative financial instruments for speculative purposes. The policy on use of derivatives is approved by the Board Risk Committee ('BRC').

Credit risk

Credit risk is the risk of loss resulting from the failure of a counterparty to honour its financial or contractual obligations to the Group. The Group's credit risk exposure is largely concentrated in its fixed income investment portfolio and to a lesser extent, its premium receivables, and reinsurance assets.

Credit risk is managed at both a Group level and at a local level. Local operations are responsible for assessing and monitoring the creditworthiness of their counterparties (e.g. brokers and policyholders). Local credit committees are responsible for ensuring these exposures are within the risk appetite of the local operations. Exposure monitoring and reporting for fixed income investments and premium receivables is embedded throughout the organisation with aggregate credit positions reported and monitored at Group level.

The Group's credit risk strategy appetite and credit risk policy are developed by the BRC and are reviewed and approved by the Board on an annual basis. This is done through the setting of Group policies, procedures and limits.

In defining its appetite for credit risk the Group looks at exposures at both an aggregate and business unit level distinguishing between credit risks incurred as a result of offsetting insurance risks or operating in the insurance market (e.g. reinsurance credit risks and risks to receiving premiums due from policyholders and intermediaries) and credit risks incurred for the purposes of generating a return (e.g. invested assets credit risk).

Limits are set at both a portfolio and counterparty level based on likelihood of default, derived from the rating of the counterparty, to ensure that the Group's overall credit profile and specific concentrations are managed and controlled within risk appetite.

The Group's investment management strategy primarily focuses on debt instruments of high credit quality issuers and seeks to limit the overall credit exposure with respect to any one issuer by ensuring limits have been based upon credit quality. Restrictions are placed on each of the Group's investment managers as to the level of exposure to various rating categories including unrated securities.

4. RISK MANAGEMENT (CONTINUED)

The Group is also exposed to credit risk from the use of reinsurance in the event that a reinsurer fails to settle its liability to the Group.

The Group Reinsurance Credit Committee oversees the management of credit risk arising from the reinsurer failing to settle its liability to the Group. Group standards are set such that reinsurers that have a financial strength rating of less than 'A-' with Standard & Poor's, or a comparable rating, are removed from the Group's authorised list of approved reinsurers unless the Group's internal review discovers exceptional circumstances in favour of the reinsurer. Collateral is taken, where appropriate, to mitigate exposures to acceptable levels. At 31 December 2017 the extent of collateral held by the Group against reinsurers' share of insurance contract liabilities was **£585m** (2016: £159m), which in the event of a default would be called and recognised on the balance sheet. The increase reflects the UK Legacy reinsurance arrangement announced on 7 February 2017 which is fully collateralised.

The Group's use of reinsurance is sufficiently diversified that it is not concentrated on a single reinsurer, or any single reinsurance contract. The Group regularly monitors its aggregate exposures by reinsurer group against predetermined reinsurer group limits, in accordance with the methodology agreed by the BRC. The Group's largest reinsurance exposures to active reinsurance groups are Berkshire Hathaway, Lloyd's of London and Talanx. At 31 December 2017 the reinsurance asset recoverable from these groups does not exceed **3.9%** (2016: 2.4%) of the Group's total financial assets. Stress tests are performed by reinsurer counterparty and the limits are set such that in a catastrophic event, the exposure to a single reinsurer is estimated not to exceed **6.4%** (2016: 6.1%) of the Group's total financial assets.

The credit profile of the Group's assets exposed to credit risk is shown below. The credit rating bands are provided by independent rating agencies. The table below sets out the Group's aggregated credit risk exposure for its financial and insurance assets.

As at 31 December 2017

	Credit rating relating to financial assets that are neither past due nor impaired						Value including held for sale £m	Less: Amounts classified as held for sale £m	Total of financial assets that are neither past due nor impaired £m
	AAA £m	AA £m	A £m	BBB £m	<BBB £m	Not rated £m			
Debt securities	5,358	2,170	2,305	655	171	1	10,660	-	10,660
Loans and receivables	81	-	5	104	4	25	219	-	219
Reinsurers' share of insurance contract liabilities ¹	-	617	1,574	605	45	41	2,882	636	2,246
Insurance and reinsurance debtors ²	75	32	971	74	53	1,622	2,827	16	2,811
Derivative assets	-	6	16	38	-	10	70	-	70
Other debtors	-	-	-	-	-	189	189	11	178
Cash and cash equivalents	317	315	378	14	8	21	1,053	5	1,048

¹ The increase in BBB reinsurers' share of insurance contract liabilities reflects the UK Legacy reinsurance arrangement announced in 2017 which is fully collateralised.

² The insurance and reinsurance debtors classified as not rated comprise personal policyholders and small corporate customers that do not have individual credit ratings. The overall credit risk to the Group is deemed to be low as the cover could be cancelled if payment were not received on a timely basis.

As at 31 December 2016

	Credit rating relating to financial assets that are neither past due nor impaired						Value including held for sale £m	Less: Amounts classified as held for sale £m	Total of financial assets that are neither past due nor impaired £m
	AAA £m	AA £m	A £m	BBB £m	<BBB £m	Not rated £m			
Debt securities	5,216	3,327	2,733	875	108	62	12,321	776	11,545
Loans and receivables	67	-	1	-	4	16	88	-	88
Reinsurers' share of insurance contract liabilities	-	605	1,577	90	20	51	2,343	96	2,247
Insurance and reinsurance debtors ¹	129	30	834	96	103	1,518	2,710	15	2,695
Derivative assets	-	2	8	37	-	9	56	-	56
Other debtors	-	-	-	-	-	127	127	1	126
Cash and cash equivalents	402	202	442	27	-	16	1,089	104	985

¹ The insurance and reinsurance debtors classified as not rated comprise personal policyholders and small corporate customers that do not have individual credit ratings. The overall credit risk to the Group is deemed to be low as the cover could be cancelled if payment were not received on a timely basis.

With the exception of government debt securities, the largest single aggregate credit exposure does not exceed **3%** (2016: 3%) of the Group's total financial assets.

4. RISK MANAGEMENT (CONTINUED)

Ageing of financial assets that are past due but not impaired

The following table provides information regarding the carrying value of financial assets that have been impaired and the ageing of financial assets that are past due but not impaired as at 2017, excluding those assets that have been classified as held for sale.

As at 31 December 2017

	Neither past due nor impaired	Financial assets that are past due but not impaired				Financial assets that have been impaired	Carrying value in the statement of financial position	Impairment losses charged/(reversed) to the income statement
		Up to three months	Three to six months	Six months to one year	Greater than one year			
		£m	£m	£m	£m			
Debt securities	10,660	-	-	-	-	10,660	-	
Loans and receivables	219	-	-	-	-	219	(4)	
Reinsurers' share of insurance contract liabilities	2,246	-	-	-	-	2,252	-	
Insurance and reinsurance debtors	2,811	51	22	24	13	2,923	4	
Derivative assets	70	-	-	-	-	70	-	
Other debtors	178	11	1	-	1	191	-	
Cash and cash equivalents	1,048	-	-	-	-	1,048	-	

As at 31 December 2016

	Neither past due nor impaired	Financial assets that are past due but not impaired				Financial assets that have been impaired	Carrying value in the statement of financial position	Impairment losses charged/(reversed) to the income statement
		Up to three months	Three to six months	Six months to one year	Greater than one year			
		£m	£m	£m	£m			
Debt securities	11,545	-	-	-	-	11,545	-	
Loans and receivables	88	-	-	-	-	88	(10)	
Reinsurers' share of insurance contract liabilities	2,247	-	-	-	-	2,252	-	
Insurance and reinsurance debtors	2,695	79	22	17	7	2,823	1	
Derivative assets	56	-	-	-	-	56	-	
Other debtors	126	-	-	-	3	129	-	
Cash and cash equivalents	985	-	-	-	-	985	-	

Market risk

Market risk is the risk of adverse financial impact resulting, directly or indirectly from fluctuations from equity and property prices, interest rates and foreign currency exchange rates. Market risk arises in our operations due to the possibility that fluctuations in the value of liabilities are not offset by fluctuations in the value of investments held. At Group level, it also arises in relation to the overall portfolio of international businesses. Market risk is subject to the Board Risk Committee risk management framework, which is subject to review and approval by the Board.

Market risk can be further broken down into three key components:

i. Equity and property risk

The Group classifies its investment portfolio in debt securities and equity securities in accordance with the accounting definitions under IFRS.

At 31 December 2017 the Group held investments classified as equity securities of **£764m** (2016: £692m). These include interests in structured entities and other investments where the price risk arises from interest rate risk rather than from equity market price risk. The Group considers that within equity securities, investments with a fair value of **£242m** (2016: £170m) may be more affected by equity index market price risk than by interest rate risk. On this basis a 15% fall in the value of equity index prices would result in the recognition of losses of **£36m** (2016: £26m) in other comprehensive income.

4. RISK MANAGEMENT (CONTINUED)

In addition the Group holds investments in properties and in group occupied properties which are subject to property price risk. A decrease of 15% in property prices would result in the recognition of losses of **£46m** (2016: £50m) in the income statement and **£5m** (2016: £5m) in other comprehensive income.

This analysis assumes that there is no correlation between interest rate and property market rate risks. It also assumes that all other assets and liabilities remain unchanged and that no management action is taken. This analysis does not represent management's view of future market change, but reflects management's view of key sensitivities.

This analysis is presented gross of the corresponding tax credits/(charges).

ii. Interest rate risk

Interest rate risk arises primarily from the Group's investments in long-term debt and fixed income securities and their movement relative to the value placed on insurance liabilities. This impacts both the fair value and amount of variable returns on existing assets as well as the cost of acquiring new fixed maturity investments.

Given the composition of the Group's investments as at 31 December 2017, the table below illustrates the impact to the income statement and other comprehensive income of a hypothetical 100bps change in interest rates on fixed income securities and cash that are subject to interest rate risk.

Changes in the income statement and other comprehensive income (OCI):

	Increase in income statement		Decrease in other comprehensive income	
	2017 £m	2016 £m	2017 £m	2016 £m
Increase in interest rate markets:				
Impact on fixed income securities and cash of an increase in interest rates of 100bps	18	20	(412)	(452)

The Group manages interest rate risk by holding investment assets (predominantly fixed income) that generate cash flows which broadly match the duration of expected claim settlements and other associated costs.

The sensitivity of the fixed interest securities of the Group has been modelled by reference to a reasonable approximation of the average interest rate sensitivity of the investments held within each of the portfolios. The effect of movement in interest rates is reflected as a one time rise of 100bps on 1 January 2018 and 1 January 2017 on the following year's income statement and other comprehensive income. The impact of an increase in interest rates on the fair value of fixed income securities that would be initially recognised in OCI will reduce over time as the maturity date approaches.

iii. Currency risk

The Group incurs exposure to currency risk in two ways:

- Operational currency risk – by holding investments and other assets and by underwriting and incurring liabilities in currencies other than the currency of the primary environment in which the business units operate, the Group is exposed to fluctuations in foreign exchange rates that can impact both its profitability and the reported value of such assets and liabilities;
- Structural currency risk – by investing in overseas subsidiaries the Group is exposed to the risk that fluctuations in foreign exchange rates impact the reported profitability of foreign operations to the Group, and the value of its net investment in foreign operations.

Operational currency risk is principally managed within the Group's individual operations by broadly matching assets and liabilities by currency and liquidity. Operational currency risk is not significant.

Structural currency risk is managed at a Group level through currency forward contracts and foreign exchange options within predetermined limits set by the Group Investment Committee. In managing structural currency risk the needs of the Group's subsidiaries to maintain net assets in local currencies to satisfy local regulatory solvency and internal risk based capital requirements are taken into account. These assets should prove adequate to support local insurance activities irrespective of exchange rate movements but may affect the value of the consolidated shareholders' equity expressed in sterling.

At 31 December 2017, the Group's total shareholders' equity deployed by currency was:

	Pounds Sterling £m	Danish Krone/Euro £m	Canadian Dollar £m	Swedish Krona £m	Other £m	Total £m
Shareholders' equity at 31 December 2017	2,607	414	506	201	222	3,950
Shareholders' equity at 31 December 2016	2,516	284	477	236	202	3,715

4. RISK MANAGEMENT (CONTINUED)

Shareholders' equity is stated after taking account of the effect of currency forward contracts and foreign exchange options. The analysis aggregates the Danish Krone exposure and the Euro exposure as the Danish Krone continues to be pegged closely to the Euro. The Group considers this aggregate exposure when reviewing its hedging strategy.

The table below illustrates the impact of a hypothetical 10% change in Danish Krone/Euro, Canadian Dollar or Swedish Krona exchange rates on shareholders' equity when retranslating into sterling:

	10% strengthening in Pounds Sterling against Danish Krone/Euro £m	10% weakening in Pounds Sterling against Danish Krone/Euro £m	10% strengthening in Pounds Sterling against Canadian Dollar £m	10% weakening in Pounds Sterling against Canadian Dollar £m	10% strengthening in Pounds Sterling against Swedish Krona £m	10% weakening in Pounds Sterling against Swedish Krona £m
Movement in shareholders' equity at 31 December 2017	(38)	46	(46)	56	(18)	22
Movement in shareholders' equity at 31 December 2016	(25)	31	(43)	53	(21)	26

Changes arising from the retranslation of foreign subsidiaries' net asset positions from their primary currencies into Sterling are taken through the foreign currency translation reserve and so consequently these movements in exchange rates have no impact on profit.

Liquidity risk

Liquidity risk refers to the risk of loss to the Group as a result of assets not being available in a form that can immediately be converted into cash, and therefore the consequence of not being able to pay its obligations when due. To help mitigate this risk, the BRC sets limits on assets held by the Group designed to match the maturities of its assets to that of its liabilities.

A large proportion of investments are maintained in short-term (less than one year) highly liquid securities, which are used to manage the Group's operational requirements based on actuarial assessment and allowing for contingencies.

The following table summarises the contractual repricing or maturity dates, whichever is earlier. Provision for losses and loss adjustment expenses are presented and are analysed by remaining estimated duration until settlement.

As at 31 December 2017

	Less than one year £m	One to two years £m	Two to three years £m	Three to four years £m	Four to five years £m	Five to ten years £m	Greater than ten years £m	Total £m	Carrying value in the statement of financial position £m
Subordinated guaranteed US\$ bonds	-	-	-	-	-	-	7	7	6
Guaranteed subordinated notes due 2045	-	-	-	-	-	400	-	400	396
Guaranteed subordinated step-up notes due 2039	-	39	-	-	-	-	-	39	39
Provisions for losses and loss adjustment expenses	3,913	1,645	1,110	799	584	1,379	1,872	11,302	9,477
Direct insurance creditors	111	2	-	-	-	-	-	113	113
Reinsurance creditors	506	239	76	-	-	-	-	821	821
Borrowings	123	-	-	-	-	-	-	123	123
Deposits received from reinsurers	35	-	-	-	-	-	-	35	35
Derivative liabilities	7	27	-	11	-	5	38	88	88
Total	4,695	1,952	1,186	810	584	1,784	1,917	12,928	11,098
Interest on perpetual bonds and notes	25	23	21	21	21	60	1	172	

4. RISK MANAGEMENT (CONTINUED)

As at 31 December 2016

	Less than one year	One to two years	Two to three years	Three to four years	Four to five years	Five to ten years	Greater than ten years	Total	Carrying value in the statement of financial position
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Subordinated guaranteed US\$ bonds	-	-	-	-	-	-	7	7	6
Perpetual guaranteed subordinated capital securities	375	-	-	-	-	-	-	375	369
Guaranteed subordinated notes due 2045	-	-	-	-	-	400	-	400	395
Guaranteed subordinated step-up notes due 2039	-	-	300	-	-	-	-	300	298
Provisions for losses and loss adjustment expenses	3,583	1,728	1,150	805	556	1,300	1,887	11,009	9,365
Direct insurance creditors	108	-	-	-	-	-	-	108	108
Reinsurance creditors	559	201	86	-	-	-	-	846	846
Borrowings	251	-	-	-	-	-	-	251	251
Deposits received from reinsurers	67	-	-	-	-	-	-	67	67
Derivative liabilities	28	1	49	-	19	35	35	167	167
Total	4,971	1,930	1,585	805	575	1,735	1,929	13,530	11,872
Interest on perpetual bonds and notes	63	49	32	21	21	81	2	269	

The maturity analysis above is presented on an undiscounted basis. The carrying values in the statement of financial position are discounted where appropriate in accordance with Group accounting policy.

The capital and interest payable on the bonds and notes have been included until the dates on which the Group has the option to call the instruments and the interest rates are reset. For further information on terms of the bonds and notes, see note 19.

Pension risk

The Group is exposed to risks through its obligation to fund a number of schemes. These risks include market risk (assets not performing as well as expected), inflation risk and mortality risk over the lives of the members. The Group and trustees of the schemes work together to reduce these risks through agreement of investment policy including the use of interest rate, inflation rate and mortality swaps.

SIGNIFICANT TRANSACTIONS AND EVENTS

5. DISCONTINUED OPERATIONS AND DISPOSALS

a) Discontinued operations and disposals

The Group classified the following operations as discontinued because they have been sold and represent a separate geographical area of operation.

<u>Operation</u>	<u>Date of disposal</u>	<u>Acquirer</u>
Russia	29 January 2016	Joint Stock Insurance Company Blagostoyanie
Brazil	29 February 2016	Suramericana S.A.
Colombia	31 March 2016	Suramericana S.A.
Chile	30 April 2016	Suramericana S.A.
Argentina	30 April 2016	Suramericana S.A.
Mexico	31 May 2016	Suramericana S.A.
Uruguay	30 June 2016	Suramericana S.A.

The revenue, expenses and related income tax expense in 2016 relating to these discontinued operations is set out below.

The total loss on the sale of discontinued operations disposed of during 2016 after tax was £29m.

DISCONTINUED INCOME STATEMENT for the year ended 31 December 2017

	Note	2017 £m	2016 £m
Income			
Gross written premiums		-	256
Less: reinsurance premiums		-	(87)
Net written premiums	7	-	169
Change in the gross provision for unearned premiums		-	38
Less: change in provision for unearned reinsurance premiums		-	(19)
Change in provision for unearned premiums		-	19
Net earned premiums		-	188
Net investment return		-	16
Total income		-	204
Expenses			
Gross claims incurred		-	(304)
Less: claims recoveries from reinsurers		-	208
Net claims		-	(96)
Underwriting and policy acquisition costs		-	(89)
Unwind of discount		-	(5)
Other operating expenses		-	(7)
		-	(197)
(Loss) on disposal		-	(29)
(Loss) before tax		-	(22)
Income tax expense	8	-	(5)
(Loss) after tax		-	(27)

5. DISCONTINUED OPERATIONS AND DISPOSALS (CONTINUED)

DISCONTINUED STATEMENT OF COMPREHENSIVE INCOME for the year ended 31 December 2017

	2017 £m	2016 £m
Loss for the year from discontinued operations	-	(27)
Items from discontinued operations that may be reclassified to the income statement:		
Exchange losses recycled on disposal of discontinued operations net of tax	-	111
Exchange gains net of tax	-	3
	-	114
Fair value gains recycled on disposal of discontinued operations net of tax	-	1
Fair value gains on available for sale financial assets net of tax	-	3
	-	4
Items from discontinued operations that will not be reclassified to the income statement:		
Movement in property revaluation, net of tax	-	2
Other comprehensive income for the year from discontinued operations	-	120
Total comprehensive income for the year from discontinued operations	-	93

Discontinued operations disposed of during the year

There were no discontinued operations disposed of during 2017.

As at 31 December 2016

	Latin America £m	Russia £m	Total £m
Consideration received	434	5	439
Transaction costs	(20)	(1)	(21)
Net proceeds from sales	414	4	418
Carrying value of net assets disposed of	(321)	(3)	(324)
Gains on sale before recycling of items from other comprehensive income	93	1	94
Reclassification of items from other comprehensive income on disposals:			
Foreign currency translation reserve	(99)	(11)	(110)
Unrealised gains on available for sale investments	(1)	-	(1)
Losses on disposal of discontinued operations before tax on disposal	(7)	(10)	(17)
Tax on disposal	(12)	-	(12)
Losses on disposal of discontinued operations after tax	(19)	(10)	(29)

5. DISCONTINUED OPERATIONS AND DISPOSALS (CONTINUED)

b) Held for sale disposal groups

The assets (including any goodwill allocated to the business) and the liabilities of the businesses held for sale are shown below.

UK Legacy	2016 £m	Reinsurance and other movements £m	2017 £m
Assets classified as held for sale:			
Investments	689	(689)	-
Reinsurers' share of insurance contract liabilities	90	546	636
Insurance and reinsurance debtors	-	16	16
Other debtors and other assets	9	2	11
Cash and cash equivalents	101	(96)	5
Total assets of disposal groups	889	(221)	668
Remeasurement of disposal groups to fair value less costs to sell	(204)	204	-
Assets of operations classified as held for sale	685	(17)	668
Liabilities directly associated with assets classified as held for sale:			
Insurance contract liabilities	685	(49)	636
Insurance and reinsurance liabilities	-	2	2
Provisions and other liabilities	-	30	30
Liabilities of operations classified as held for sale	889	(221)	668
Net assets of operations classified as held for sale	-	-	-

The value of insurance contract liabilities, net of reinsurance (£90m), of £595m as at 31 December 2016 was £834m on an undiscounted basis (excludes claims handling provision and margin). The value of insurance contract liabilities, net of reinsurance (£90m), of £595m as at 31 December 2016 was £834m on an undiscounted basis (excludes claims handling provision and margin).

As at 31 December 2016

	UK Legacy £m	Oman ¹ £m	UK Other £m	Total £m
Assets classified as held for sale:				
Property and equipment	-	-	4	4
Investments	689	87	-	776
Reinsurers' share of insurance contract liabilities	90	6	-	96
Insurance and reinsurance debtors	-	15	-	15
Other debtors and other assets	9	6	1	16
Cash and cash equivalents	101	3	-	104
Total assets of disposal groups	889	117	5	1,011
Remeasurement of disposal groups to fair value less costs to sell	(204)	-	-	(204)
Assets of operations classified as held for sale	685	117	5	807
Liabilities directly associated with assets classified as held for sale:				
Insurance contract liabilities	685	50	-	735
Insurance and reinsurance liabilities	-	5	-	5
Provisions and other liabilities	-	10	-	10
Liabilities of operations classified as held for sale	685	65	-	750
Net assets of operations classified as held for sale	-	52	5	57

¹ At 31 December 2016 it was probable that the Group would lose control over its Oman business as a result of a government required public offering of 40% of the group holding. In 2017, the actual required sale was only 25% meaning control was maintained and as a result it is no longer held for sale.

5. DISCONTINUED OPERATIONS AND DISPOSALS (CONTINUED)

c) Profit on disposal of business and realised gains on held for sale assets

The net gain of £69m includes £66m relating to the realised gain on the investments transferred as part of the UK Legacy reinsurance transaction, offset by a charge of £22m on the commutation of the Group's Adverse Development Cover reinsurance protection bought partly to protect the UK Legacy book.

The reversal of part of the valuation adjustment on the Group's Oman business has resulted in a gain of £17m and the Group recognised a gain of £7m on the disposal of the Accident and Repairs business in the UK.

d) Remeasurement of disposal groups

In 2016, the assets and liabilities of the Oman and UK Legacy businesses were classified as held for sale. Upon classification as held for sale, the net assets were measured at the lower of carrying amount and fair value less costs to sell. This valuation adjustment resulted in a £234m loss which was recognised in the continuing income statement.

6. REORGANISATION COSTS

In 2017, the reorganisation costs of **£155m** (note 7) are directly associated with continuing operations (2016: £160m). The amounts are directly attributable to redundancy **£68m** (2016: £49m) and other restructuring activity of **£87m** (2016: £111m). Restructuring costs in 2017 relate to amounts incurred across the Group for activities such as process re-engineering and other cost reduction initiatives such as office footprint consolidation and reduction, reducing spans of control, and outsourcing.

NOTES TO THE CONDENSED CONSOLIDATED INCOME STATEMENT AND CONDENSED CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

7. SEGMENTAL INFORMATION

Group excluding disposals

The Group's primary operating segments comprise Scandinavia, Canada, UK & International and Central Functions which is consistent with how the Group is managed. The primary operating segments are based on geography and are all engaged in providing personal and commercial general insurance services. Central Functions include the Group's internal reinsurance function and Group Corporate Centre.

Each operating segment is managed by a member of the Group Executive Committee who is directly accountable to the Group Chief Executive and Board of Directors, who together form the central decision making function in respect of the operating activities of the Group. The UK is the Group's country of domicile and one of its principal markets.

Disposals

Disposals are categorised between disposals of continuing operations and discontinued operations:

Disposals of continuing operations

On 7 February 2017, the Group's UK Legacy liabilities were disposed of to Enstar Group Limited. The transaction initially takes the form of a reinsurance agreement, effective from 31 December 2016, which substantially effects economic transfer, to be followed by completion of a subsequent legal transfer of the business. The Group's UK Legacy business is managed as part of the UK operations. It is not presented as a discontinued operation as it is neither a separate geographical area nor a major line of business.

Discontinued operations

During 2015, the Group classified the Latin American and Russian operations as discontinued as they were held for sale at 31 December 2015 and represented a separate geographical area of operation. The sale of these operations completed in the first six months of 2016 and they were therefore classified as discontinued at 31 December 2016 (see note 5(a) for further details).

During 2017, no further operations have been classified as discontinued and as such, the 2016 comparatives do not require re-presentation.

Assessing segment performance

The Group uses the following key measures to assess the performance of its operating segments:

- Net written premiums;
- Underwriting result;
- Combined operating ratio (COR);
- Operating result.

Net written premiums is the key measure of revenue used in internal reporting.

Underwriting result, COR and operating result are Alternative Performance Measures (APMs), the key internal measures of profitability of the operating segments. The COR reflects the ratio of claims costs and expenses (including commission) to earned premiums, expressed as a percentage.

Transfers or transactions between segments are entered into under normal commercial terms and conditions that would also be available to unrelated third parties.

7. SEGMENTAL INFORMATION (CONTINUED)

Year ended 31 December 2017

	Scandinavia	Canada	UK & International	Central Functions	Total Group
	£m	£m	£m	£m	£m
Net written premiums	1,833	1,619	3,199	27	6,678
Underwriting result	315	98	(82)	63	394
Investment result	74	61	149	-	284
Central costs and other activities	-	-	-	(15)	(15)
Operating result (management basis)	389	159	67	48	663
Realised gains					19
Unrealised losses, impairments and foreign exchange					(1)
Interest costs					(102)
Amortisation of intangible assets					(15)
Pension net interest and administration costs					(7)
Reorganisation costs					(155)
Impairment of intangible assets and similar charges					(23)
Profit on disposal of business and realised gains on held for sale assets					69
Profit before tax					448
Tax on operations					(126)
Profit after tax					322
Combined operating ratio (%)	82.9%	93.9%	102.6%		94.0%

7. SEGMENTAL INFORMATION (CONTINUED)

Year ended 31 December 2016

	Scandinavia	Canada	UK & International	Central Functions	Group excluding disposals	Disposals of continuing operations	Continuing operations per income statement	Discontinued operations (note 5)	Total Group
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Net written premiums	1,721	1,443	3,081	36	6,281	(42)	6,239	169	6,408
Underwriting result	239	74	88	(9)	392	(16)	376	4	380
Investment result	72	66	149	-	287	2	289	9	298
Central costs and other activities	-	-	-	(23)	(23)	-	(23)	-	(23)
Operating result (management basis)	311	140	237	(32)	656	(14)	642	13	655
Realised gains							28	2	30
Unrealised losses, impairments and foreign exchange							(4)	-	(4)
Interest costs							(138)	-	(138)
Amortisation of intangible assets							(16)	-	(16)
Pension net interest and administration costs							(4)	-	(4)
Solvency II costs							(7)	-	(7)
Reorganisation costs							(160)	(8)	(168)
Economic assumption changes							(6)	-	(6)
Remeasurement of disposal groups							(234)	(17)	(251)
Profit/(loss) before tax							101	(10)	91
Tax on continuing operations							(54)	(5)	(59)
Tax on disposals of discontinued operations							-	(12)	(12)
Profit after tax							47	(27)	20
Combined operating ratio (%)	86.2%	94.9%	97.2%		93.8%				94.2%

8. INCOME TAX

The tax amounts charged/(credited) in the income statement are as follows:

	2017 £m	2016 £m
Current tax	136	90
Deferred tax	(10)	(36)
Total taxation attributable to continuing operations	126	54
Tax on disposal of discontinued operations	-	12
Tax on profits of discontinued operations	-	5
Taxation attributable to the Group	126	71

Reconciliation of the income tax expense

	2017 £m	2016 £m
Profit before tax	448	101
Tax at the UK rate of 19.2% (2016: 20.0%)	86	20
Tax effect of:		
Income/gains not taxable	(8)	(3)
Expenses not deductible for tax purposes	6	7
Impairment and amortisation of goodwill	(2)	6
Movement in deferred tax assets not recognised	4	(17)
Increase of tax provided in respect of prior periods	-	2
Different tax rates of subsidiaries operating in other jurisdictions	11	17
Withholding tax on dividends from subsidiaries	29	5
Effect of change in tax rates	2	16
Deductible Restricted Tier 1 coupon in equity	(2)	-
Other	-	1
Total income tax expense attributable to continuing operations	126	54
Total income tax expense attributable to discontinued operations	-	17
Income tax expense	126	71

The current tax and deferred income tax credited/(charged) to each component of other comprehensive income is as follows:

	Current Tax		Deferred Tax		Total	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Fair value gains and losses	20	5	(18)	(24)	2	(19)
Remeasurement of net defined benefit pension liability	-	-	15	64	15	64
Total credited/(charged) to other comprehensive income	20	5	(3)	40	17	45

Foreign exchange arising on the revaluation of current and deferred tax balances is reported through other comprehensive income within the foreign currency translation reserve.

The net current tax and deferred tax charged directly to equity is **£nil** (2016: £nil).

8. INCOME TAX (CONTINUED)

Tax rates

The table below provides a summary of the current tax and deferred tax rates for the year in respect of the core tax jurisdictions in which the Group operates.

	2017		2016	
	Current Tax	Deferred Tax	Current Tax	Deferred Tax
UK	19.2 %	17.0 %	20.0 %	17.0 %
Canada	27.2 %	27.2 %	27.5 %	27.5 %
Denmark	22.0 %	22.0 %	22.0 %	22.0 %
Ireland	12.5 %	12.5 %	12.5 %	12.5 %
Sweden	22.0 %	22.0 %	22.0 %	22.0 %

9. EARNINGS PER SHARE (EPS)

The earnings per ordinary share are calculated by reference to the profit attributable to the ordinary shareholders and the weighted average number of shares in issue during the year. These were **1,021,417,775** for basic EPS and **1,028,498,695** for diluted EPS (excluding those held in Employee Stock Ownership Plan (ESOP) and Share Incentive Plan (SIP) trusts). The number of shares in issue at 31 December 2017 was **1,022,677,174** (excluding those held in ESOP and SIP trusts).

Basic EPS

	2017		2016	
	Continuing	Discontinued	Continuing	Discontinued
Profit/(loss) attributable to the shareholders of the Parent Company (£m)	289	-	54	(27)
Less: cumulative preference dividends (£m)	(9)	-	(9)	-
Less: Tier 1 notes coupon payment (£m)	(11)	-	-	-
Profit/(loss) for the calculation of earnings per share	269	-	45	(27)
Weighted average number of ordinary shares in issue (thousands)	1,021,418	-	1,018,174	1,018,174
Basic earnings/(loss) per share (p)	26.3	-	4.4	(2.6)

Diluted EPS

	2017	2016
	£m	£m
Weighted average number of ordinary shares in issue (thousands)	1,021,418	1,018,174
Adjustments for share options and contingently issuable shares (thousands)	7,081	6,275
Total weighted average number of ordinary shares for diluted earnings per share (thousands)	1,028,499	1,024,449
Diluted earnings per share (p) relating to continuing operations	26.1	4.4
Diluted (loss) per share (p) relating to discontinued operations	-	(2.6)

Note 17 includes further information of the outstanding share options and unvested share awards to Group employees that could potentially dilute basic earnings per share in the future.

10. DIVIDENDS PAID AND PROPOSED

The final dividend to equity holders is recognised as a liability when approved at the Annual General Meeting (AGM). The Company and its subsidiaries may be subject to restrictions on the amount of dividends they can pay to shareholders as a result of regulatory requirements. However, based on the information currently available, the Group does not believe that such restrictions materially limit the ability to meet obligations or pay dividends. At the AGM on 5 May 2018, a final dividend in respect of the year ended 31 December 2017 of **13.0p** per ordinary share amounting to a total dividend of **£133m** is to be proposed. The proposed dividend will be paid and accounted for in shareholders' equity as an appropriation of retained earnings in the year ending 31 December 2018.

	2017	2016	2017	2016
	p	p	£m	£m
Ordinary dividend:				
Final paid in respect of prior year	11.0	7.0	112	71
Interim paid in respect of current year	6.6	5.0	68	51
	17.6	12.0	180	122
Preference dividend			9	9
Tier 1 notes coupon payment			11	-
			200	131

The Tier 1 notes coupon payment relates to the two floating rate notes issued on 27 March 2017 (note 18).

NOTES TO THE CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

II. GOODWILL AND INTANGIBLE ASSETS

	Goodwill	Intangible assets arising from acquired claims provisions	Externally acquired software	Internally generated software	Other	Total
	£m	£m	£m	£m	£m	£m
Cost						
At 1 January 2017	440	128	82	753	259	1,662
Additions	-	-	-	131	-	131
Disposals	-	-	-	(28)	-	(28)
Exchange adjustment	1	4	-	3	(3)	5
At 31 December 2017	441	132	82	859	256	1,770
Accumulated amortisation						
At 1 January 2017	-	128	68	418	172	786
Amortisation charge	-	-	9	66	19	94
Amortisation on disposals	-	-	-	(28)	-	(28)
Exchange adjustment	-	4	-	-	(2)	2
At 31 December 2017	-	132	77	456	189	854
Accumulated impairment						
At 1 January 2017	95	-	-	48	5	148
Impairment charge	-	-	-	20	-	20
Reversal of held for sale valuation adjustment	(17)	-	-	-	-	(17)
Exchange adjustment	1	-	-	1	-	2
At 31 December 2017	79	-	-	69	5	153
Carrying amount at 31 December 2017	362	-	5	334	62	763

11. GOODWILL AND INTANGIBLE ASSETS (CONTINUED)

	Goodwill	Intangible assets arising from acquired claims provisions	Externally acquired software	Internally generated software	Other	Total
	£m	£m	£m	£m	£m	£m
Cost						
At 1 January 2016	514	109	86	614	245	1,568
Additions and transfers	-	-	1	131	9	141
Disposals	(144)	-	(6)	(47)	(39)	(236)
Exchange adjustment	70	19	1	55	44	189
At 31 December 2016	440	128	82	753	259	1,662
Accumulated amortisation						
At 1 January 2016	-	108	64	355	151	678
Amortisation charge	-	1	8	61	18	88
Amortisation on disposals	-	-	(5)	(25)	(25)	(55)
Exchange adjustment	-	19	1	27	28	75
At 31 December 2016	-	128	68	418	172	786
Accumulated impairment						
At 1 January 2016	151	-	-	55	5	211
Held for sale valuation adjustment	30	-	-	1	-	31
Impairment on disposals	(86)	-	-	(16)	-	(102)
Exchange adjustment	-	-	-	8	-	8
At 31 December 2016	95	-	-	48	5	148
Carrying amount at 31 December 2016	345	-	14	287	82	728

Amortisation

Amortisation expense of **£79m** (2016: £72m) has been charged to underwriting and policy acquisition costs with the remainder recognised in other operating expenses.

Impairments

During 2017 the software impairment charge was **£20m** (2016: £1m), none of which was charged to underwriting and policy acquisition costs (2016: £nil). The impairment relates to software in the UK where business volumes have been lower than anticipated £11m and a Scandinavian IT system where certain older elements have been rendered obsolete £9m.

When testing for goodwill impairment, the carrying value of the Cash Generating Unit (CGU) to which goodwill has been allocated is compared to the recoverable amount as determined by a value in use calculation. These calculations use cash flow projections based on operating plans approved by management covering a three year period and using the best estimates of future premiums, operating expenses and taxes using historical trends, general geographical market conditions, industry trends and forecasts and other available information as discussed in more detail in the strategic report section. Cash flows beyond this period are extrapolated using the estimated growth rates which management deem appropriate for the CGU. The cash flow forecasts are adjusted by appropriate discount rates. Where a sales price has been agreed for a CGU, the sales proceeds less costs to sell are considered the best estimate of the value in use.

Where the value in use is less than the current carrying value of the CGU in the statement of financial position, the goodwill is impaired in order to ensure that the CGU carrying value is not greater than its future value to the Group.

II. GOODWILL AND INTANGIBLE ASSETS (CONTINUED)

Goodwill is allocated to the Group's CGUs, which are contained within the following operating segments:

	2017 £m	2016 £m
Scandinavia (Sweden, Norway, Denmark)	155	152
Canada (Commercial, Johnson, Personal, Travel)	157	160
UK and International (Ireland, Oman)	50	33
Total Goodwill	362	345

In 2016, legislation was issued by the Oman Government requiring a proportion of the company to be offered to the public. This was expected to result in the Group losing control and therefore the Oman business was classified as held for sale. Consequently the business was measured at fair value less costs to sell resulting in a revaluation adjustment in 2016 of £30m.

The proportion of business sold in 2017 was lower than expected resulting in control being retained by the Group. Goodwill of £17m has been reinstated in 2017 as a consequence.

Impairment Sensitivity

Following completion of the Group impairment testing, it was identified that the Norway CGU was sensitive to changes in key assumptions.

The sensitivities are listed below:

	Norway Potential impairment £m
Change to each year of the planning period (2018 to 2020)	
6% decrease in earned premium	(3)
6% increase in COR%	(3)

The range of pre-tax discount rates used for goodwill impairment testing, which reflect specific risks relating to the CGU at the date of evaluation and weighted average growth rates used in 2017 for the CGUs within each operating segment are shown below. The growth rates include improvements in trade performance, where these are forecast in the three year operational plan for the CGU.

	Pre-tax discount rate		Weighted average growth rate	
	2017	2016	2017	2016
Scandinavia	10%-11%	9%-10%	1%-3%	2%-3%
Canada	11%-13%	11%-12%	2%-4%	2%-4%
UK & International	9%-11%	9%-11%	2%	2%

12. FINANCIAL ASSETS

The following table analyses the Group's financial assets by classification as at 31 December 2017 and 31 December 2016.

As at 31 December 2017

	At fair value through profit and loss (FVTPL)	Available for sale	Loans and receivables	Total
	£m	£m	£m	£m
Equity securities	-	764	-	764
Debt securities	18	10,642	-	10,660
Financial assets measured at fair value	18	11,406	-	11,424
Loans and receivables	-	-	219	219
Total financial assets	18	11,406	219	11,643

As at 31 December 2016

	At fair value through profit and loss (FVTPL)	Available for sale	Loans and receivables	Total
	£m	£m	£m	£m
Equity securities	6	686	-	692
Debt securities	19	12,302	-	12,321
Financial assets measured at fair value	25	12,988	-	13,013
Loans and receivables	-	-	88	88
Total financial assets	25	12,988	88	13,101
Less: Assets classified as held for sale				
Debt securities	-	776	-	776
Total financial assets net of held for sale	25	12,212	88	12,325

The following table analyses the cost/amortised cost, gross unrealised gains and losses, and fair value of financial assets.

	2017				2016
	Cost / amortised cost £m	Unrealised gains £m	Unrealised losses and impairments £m	Fair value £m	Fair value £m
Equity securities	740	52	(28)	764	692
Debt securities	10,356	431	(127)	10,660	12,321
Financial assets measured at fair value	11,096	483	(155)	11,424	13,013
Loans and receivables	219	-	-	219	88
Total financial assets	11,315	483	(155)	11,643	13,101
Less: Assets classified as held for sale					
Debt securities	-	-	-	-	776
Total financial assets net of held for sale	11,315	483	(155)	11,643	12,325

Collateral

At 31 December 2017, the Group had pledged **£514m** (2016: £763m) of financial assets as collateral for liabilities or contingent liabilities. The assets pledged are included within the balance sheet as follows; government securities of **£461m** (2016: £636m), cash and cash equivalents of **£43m** (2016: £114m) and debt securities of **£10m** (2016: £13m). The terms and conditions of the collateral pledged are market standard in relation to letter of credit facilities.

At 31 December 2017, the Group has accepted **£31m** (2016: £101m) in collateral. The assets accepted are included within the balance sheet. The Group is permitted to sell or repledge collateral held in the event of default by the owner. The fair value of the collateral accepted is **£31m** (2016: £101m). The terms and conditions of the collateral held are market standard. The assets held as collateral are readily convertible into cash.

12. FINANCIAL ASSETS (CONTINUED)

Derivative financial instruments

The following table presents the fair value and notional amount of derivatives by term to maturity and nature of risk.

As at 31 December 2017

	Notional Amount			Total £m	Fair Value	
	Less than 1 year £m	From 1 to 5 years £m	Over 5 years £m		Asset £m	Liability £m
Designated as hedging instruments						
Currency risk (net investment in foreign operation)	1,253	-	-	1,253	21	(5)
Currency risk (cash flow)	1	5	-	6	1	-
Cross currency interest swaps (fair value/cash flow)	4	159	181	344	3	(44)
Total					25	(49)
At FVTPL						
Currency risk mitigation	223	-	-	223	2	-
Inflation risk mitigation	-	60	323	383	43	(39)
Total					45	(39)
Total derivatives					70	(88)

As at 31 December 2016

	Notional Amount			Total £m	Fair Value	
	Less than 1 year £m	From 1 to 5 years £m	Over 5 years £m		Asset £m	Liability £m
Designated as hedging instruments						
Currency risk (net investment in foreign operation)	1,271	-	-	1,271	7	(20)
Cross currency interest swaps (fair value/cash flow)	17	264	261	542	2	(109)
Total					9	(129)
At FVTPL						
Currency risk mitigation	317	-	-	317	6	(2)
Inflation risk mitigation	-	-	332	332	41	(36)
Total					47	(38)
Total derivatives					56	(167)

The use of derivatives can result in accounting mismatches when gains and losses arising on the derivatives are presented in the income statement in accordance with the Group's accounting policies, and corresponding losses and gains on the risks being mitigated are not included in the income statement. In such circumstances the Group may apply hedge accounting in accordance with IFRS and the Group accounting policy on hedging.

The Group applies hedge accounting to derivatives acquired to reduce foreign exchange risk in its net investment in certain major overseas subsidiaries. There was no ineffectiveness recognised in the income statement in respect of these hedges during 2017 or 2016.

The Group also applies hedge accounting to specified fixed interest assets in its investment portfolio. In order to remove exchange risk from these assets the Group may also acquire cross currency interest rate swaps to swap the cash flows from the portfolio into cash flows denominated in pounds sterling or the functional currency of the entity acquiring the asset. The Group applies fair value hedge accounting when using 'fixed to floating' interest rate swaps and cash flow hedge accounting when using 'fixed to fixed' interest rate swaps. The interest rate swaps exactly offset the timing and amounts expected to be received on the underlying investments. The investments have a remaining term of between four months and 38 years, with the substantial majority having a term of less than eight years. There have been no default and no defaults are expected on the hedged investments.

12. FINANCIAL ASSETS (CONTINUED)

The total gains on cash flow hedge instruments during 2017 were **£3m** (2016: £6m) in the consolidated statement of other comprehensive income, and the amount reclassified to the income statement was **£1m** (2016: £1m). The ineffectiveness recognised in the income statement was **£nil** (2016: £nil).

The total losses on the fair value hedge instruments recognised in the income statement were **£45m** (2016: £50m) and the offsetting gains related to the hedged risk were **£50m** (2016: £45m).

The Group enters into derivative transactions under International Swaps and Derivatives Association (ISDA) master netting arrangements. In general, under such agreements the amounts owed by each counterparty on a single day in respect of all transactions outstanding in the same currency are aggregated into a single net amount that is payable by one counterparty to the other. In certain circumstances, such as a credit default, all outstanding transactions under the agreement are terminated, the termination value is assessed and only a single net amount is payable in settlement of all transactions.

The ISDA agreements do not meet the criteria for offsetting in the statement of financial position. This is because the Group does not have any current legally enforceable right to offset recognised amounts, because the right to offset is enforceable only on the occurrence of future events. The tables below provide information on the impact of the netting arrangements.

In addition, during 2017, the Group took out borrowings from credit institutions under repurchase agreements of **£119m** (2016: £249m). The Group continues to recognise debt securities in the statement of financial position as the Group remains exposed to the risks and rewards of ownership.

Amounts subject to enforceable netting arrangements

As at 31 December 2017	Effect of offsetting in statement of financial position			Related items not offset		
	Gross amounts	Amounts offset	Net amounts reported	Financial instruments	Financial collateral	Net amount
	£m	£m	£m	£m	£m	£m
Derivative financial assets	70	-	70	(54)	(15)	1
Reverse repurchase arrangements and other similar secured lending	119	-	119	(119)	-	-
Total assets	189	-	189	(173)	(15)	1
Derivative financial liabilities	88	-	88	(54)	(31)	3
Repurchase arrangements and other similar secured borrowing	119	-	119	(119)	-	-
Total liabilities	207	-	207	(173)	(31)	3

Amounts subject to enforceable netting arrangements

As at 31 December 2016	Effect of offsetting in statement of financial position			Related items not offset		
	Gross amounts	Amounts offset	Net amounts reported	Financial instruments	Financial collateral	Net amount
	£m	£m	£m	£m	£m	£m
Derivative financial assets	56	-	56	(45)	(9)	2
Reverse repurchase arrangements and other similar secured lending	249	-	249	(249)	-	-
Total assets	305	-	305	(294)	(9)	2
Derivative financial liabilities	167	-	167	(45)	(113)	9
Repurchase arrangements and other similar secured borrowing	249	-	249	(249)	-	-
Total liabilities	416	-	416	(294)	(113)	9

13. FAIR VALUE MEASUREMENT

Fair value is used to value a number of assets within the statement of financial position and represents its market value at the reporting date.

Cash and cash equivalents, loans and receivables, other assets and other liabilities

For cash, loans and receivables, commercial paper, other assets, liabilities and accruals, their carrying amounts are considered to be as approximate fair values.

Group occupied property and investment property

Group occupied properties are valued on a vacant possession basis using third party valuers. Investment properties are valued, at least annually, at their highest and best use.

The fair value of property has been determined by external, independent valuers, having appropriate recognised professional qualifications and recent experience in the location and category of the property being valued.

The valuations of buildings with vacant possession are based on the comparative method of valuation with reference to sales of other vacant buildings. Fair value is then determined based on the locational qualities and physical building characteristics (principally condition, size, specification and layout) as appropriate.

Investment properties are valued using discounted cash flow models which take into account the net present value of cash flows to be generated from the properties. The cash flow streams reflect the current rent (the gross rent) payable to lease expiry, at which point it is assumed that each unit will be re-let at its estimated rental value. Allowances have been made for voids and rent free periods where applicable. The appropriate rent to be capitalised is selected on the basis of the location of the building, its quality, tenant credit quality and lease terms amongst other factors.

These cash flows are discounted at an appropriate rate of interest to determine their present value.

In both cases the estimated fair value would increase/(decrease) if:

- The estimated rental value is higher/(lower);
- Void periods were shorter/(longer);
- The occupancy rates were higher/(lower);
- Rent free periods were shorter/(longer);
- The discount rates were lower/(higher).

Derivative financial instruments

Derivative financial instruments are financial contracts whose fair value is determined on a market basis by reference to underlying interest rate, foreign exchange rate, equity or commodity instrument or indices.

Loan capital

The fair value measurement of the Group's loan capital instruments, with the exception of the subordinated guaranteed US\$ bonds, are based on pricing obtained from a range of financial intermediaries who base their valuations on recent transactions of the Group's loan capital instruments and other observable market inputs such as applicable risk free rate and appropriate credit risk spreads.

The fair value measurement of the subordinated guaranteed US\$ bonds is also obtained from an indicative valuation based on the applicable risk free rate and appropriate credit risk spread.

Fair value hierarchy

Fair value for all assets and liabilities which are either measured or disclosed is determined based on available information and categorised according to a three-level fair value hierarchy as detailed below.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from data other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3 fair value measurements are those derived from valuation techniques that include significant inputs for the asset or liability valuation that are not based on observable market data (unobservable inputs).

13. FAIR VALUE MEASUREMENT (CONTINUED)

A financial instrument is regarded as quoted in an active market (level 1) if quoted prices for that financial instrument are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

The Group uses prices received from external providers who calculate these prices from quotes available at the reporting date for the particular investment being valued. For investments that are actively traded the Group determines whether the prices meet the criteria for classification as a level 1 valuation. The price provided is classified as a level 1 valuation when it represents the price at which the investment traded at the reporting date taking into account the frequency and volume of trading of the individual investment together with the spread of prices that are quoted at the reporting date for such trades. Typically investments in frequently traded government debt would meet the criteria for classification in the level 1 category. Where the prices provided do not meet the criteria for classification in the level 1 category, the prices are classified in the level 2 category.

In limited circumstances, the Group does not receive pricing information from an external provider for its financial investments. In such circumstances the Group calculates fair value which may use input parameters that are not based on observable market data. Unobservable inputs are based on assumptions that are neither supported by prices from observable current market transactions for the same instrument nor based on available market data. In these cases, judgment is required to establish fair values. Valuations that require the significant use of unobservable data are classified as level 3 valuations. In addition, the valuations used for investment properties and for group occupied properties are classified in the level 3 category.

The following table provides an analysis of financial instruments and other items that are measured subsequent to initial recognition at fair value as well as financial liabilities not measured at fair value, grouped into levels 1 to 3. The table does not include financial assets and liabilities not measured at fair value if the carrying value is a reasonable approximation of fair value.

	Fair value hierarchy				Total £m
	Level 1 £m	Level 2 £m	Level 3 £m	Less: Assets of operations classified as held for sale £m	
Group occupied property - land and buildings	-	-	35	-	35
Investment properties	-	-	308	-	308
Available for sale financial assets:					
Equity securities	407	7	350	-	764
Debt securities	3,711	6,604	327	-	10,642
Financial assets at FVTPL:					
Equity securities	-	-	-	-	-
Debt securities	-	-	18	-	18
	4,118	6,611	1,038	-	11,767
Derivative assets:					
At FVTPL	-	45	-	-	45
Designated as hedging instruments	-	25	-	-	25
Total assets measured at fair value	4,118	6,681	1,038	-	11,837
Derivative liabilities:					
At FVTPL	-	39	-	-	39
Designated as hedging instruments	-	49	-	-	49
Total liabilities measured at fair value	-	88	-	-	88
Loan capital	-	507	-	-	507
Total value of liabilities not measured at fair value	-	507	-	-	507

13. FAIR VALUE MEASUREMENT (CONTINUED)

	Fair value hierarchy 2016				Total £m
	Level 1 £m	Level 2 £m	Level 3 £m	Less: Assets of operations classified as held for sale £m	
Group occupied property - land and buildings	-	-	38	4	34
Investment properties	-	-	333	-	333
Available for sale financial assets:					
Equity securities	323	-	363	-	686
Debt securities	4,256	7,756	290	776	11,526
Financial assets at FVTPL:					
Equity securities	-	-	6	-	6
Debt securities	-	-	19	-	19
	4,579	7,756	1,049	780	12,604
Derivative assets:					
At FVTPL	-	47	-	-	47
Designated as hedging instruments	-	9	-	-	9
Total assets measured at fair value	4,579	7,812	1,049	780	12,660
Derivative liabilities:					
At FVTPL	-	38	-	-	38
Designated as hedging instruments	-	129	-	-	129
Total liabilities measured at fair value	-	167	-	-	167
Loan capital	-	1,129	8	-	1,137
Total value of liabilities not measured at fair value	-	1,129	8	-	1,137

The movement in the fair value measurements of level 3 financial assets is shown in the table below:

	Available for sale investments		Investments at FVTPL		Total £m
	Equity securities £m	Debt securities £m	Equity securities £m	Debt securities £m	
At 1 January 2016	269	154	38	15	476
Total gains/(losses) recognised in:					
Income statement	1	-	1	(9)	(7)
Other comprehensive income	16	2	-	-	18
Purchases	49	118	5	28	200
Disposals	7	-	(38)	(15)	(46)
Exchange adjustment	21	16	-	-	37
At 1 January 2017	363	290	6	19	678
Total gains/(losses) recognised in:					
Income statement	2	-	-	(1)	1
Other comprehensive income	(12)	(6)	-	-	(18)
Purchases	22	59	-	-	81
Disposals	(31)	(16)	(6)	-	(53)
Exchange adjustment	6	-	-	-	6
Level 3 financial assets at 31 December 2017	350	327	-	18	695

13. FAIR VALUE MEASUREMENT (CONTINUED)

The following table shows the level 3 available for sale financial assets, investment properties and group occupied property carried at fair value as at the balance sheet date, the valuation basis, main assumptions used in the valuation of these instruments and reasonably possible decreases in fair value based on reasonably possible alternative assumptions.

		Reasonably possible alternative assumptions			
		2017		2016	
	Main assumptions	Current fair value £m	Decrease in fair value £m	Current fair value £m	Decrease in fair value £m
Available for sale financial assets and property					
Group occupied property - land and buildings ¹	Property valuation	35	(5)	38	(5)
Investment properties ¹	Cash flows; discount rate	308	(48)	333	(50)
Level 3 available for sale financial assets:					
Equity securities ²	Cash flows; discount rate	350	(10)	363	(14)
Debt securities ²	Cash flows; discount rate	327	(9)	290	(15)
Total		1,020	(72)	1,024	(84)

¹ The Group's property portfolio (including the Group occupied properties) is almost exclusively located in the UK. Reasonably possible alternative valuations have been determined using an increase of 100bps in the discount rate used in the valuation.

² The Groups investment in financial assets classified at level 3 in the hierarchy are primarily investments in various private fund structures investing in debt instruments where the valuation includes estimates of the credit spreads on the underlying holdings. The estimates of the credit spread are based upon market observable credit spreads for what are considered to be assets with similar credit risk. Reasonably possible alternative valuations have been determined using an increase of 100bps in the credit spread used in the valuation.

14. REINSURERS' SHARE OF INSURANCE CONTRACT LIABILITIES

	2017 £m	2016 £m
Reinsurers' share of provisions for unearned premiums	729	816
Reinsurers' share of provisions for losses and loss adjustment expenses	1,523	1,436
Total reinsurers' share of insurance contract liabilities net of held for sale	2,252	2,252
To be settled within 12 months	1,187	1,301
To be settled after 12 months	1,065	951

The following changes have occurred in the reinsurers' share of provision for unearned premiums during the year:

	2017 £m	2016 £m
Reinsurers' share of provision for unearned premiums at 1 January	818	961
Premiums ceded to reinsurers	920	1,068
Reinsurers' share of premiums earned	(977)	(1,096)
Changes in reinsurance asset	(57)	(28)
Reinsurers' share of portfolio transfers and disposals of subsidiaries	(27)	(137)
Exchange adjustment	(5)	22
Reinsurers' share of provision for unearned premiums at 31 December	729	818
Less: Assets classified as held for sale	-	2
Total reinsurers' share of provision for unearned premiums at 31 December net of held for sale	729	816

14. REINSURERS' SHARE OF INSURANCE CONTRACT LIABILITIES (CONTINUED)

The following changes have occurred in the reinsurers' share of provision for losses and loss adjustment expenses during the year:

	2017	2016
	£m	£m
Reinsurers' share of provisions for losses and loss adjustment expenses at 1 January	1,530	1,264
Reinsurers' share of total claims incurred	786	915
Total reinsurance recoveries received	(730)	(414)
Reinsurers' share of portfolio transfers and disposals of subsidiaries	-	(356)
Reinsurance of UK Legacy	568	-
Exchange adjustment	(23)	113
Other movements	28	8
Reinsurers' share of provisions for losses and loss adjustment expenses at 31 December	2,159	1,530
Less: Assets classified as held for sale	636	94
Total reinsurers' share of provisions for losses and loss adjustment expenses at 31 December net of held for sale	1,523	1,436

15. CURRENT AND DEFERRED TAX

Current Tax

	Asset		Liability	
	2017	2016	2017	2016
	£m	£m	£m	£m
To be settled within 12 months	40	60	13	25
To be settled after 12 months	3	5	11	11
Net current tax position at 31 December	43	65	24	36
Less: Classified as held for sale	-	-	-	4
Net current tax position at 31 December net of held for sale	43	65	24	32

Deferred Tax

	Asset		Liability	
	2017	2016	2017	2016
	£m	£m	£m	£m
Net deferred tax position at 31 December	276	270	56	54

The following are the major deferred tax assets/(liabilities) recognised by the Group:

	2017	2016
	£m	£m
Net unrealised gains on investments	(31)	(54)
Intangibles capitalised	(24)	(28)
Deferred acquisition costs	(8)	(7)
Tax losses and unused tax credits	97	190
Other deferred tax reliefs	87	10
Net insurance contract liabilities	(18)	(15)
Retirement benefit obligations	53	55
Capital allowances	55	56
Provisions and other temporary differences	9	9
Net deferred tax asset at 31 December	220	216

15. CURRENT AND DEFERRED TAX (CONTINUED)

The movement in the net deferred tax assets recognised by the continuing Group was as follows:

	2017	2016
	£m	£m
Net deferred tax asset at 1 January	216	123
Amounts credited to income statement	10	44
Amounts (charged)/credited to other comprehensive income	(3)	41
Net arising on acquisition/disposal of subsidiaries and other transfers	-	10
Exchange adjustments	(3)	7
Effect of change in tax rates	-	(8)
- income statement	-	(8)
- other comprehensive income	-	(1)
Net deferred tax asset at 31 December	220	216

At the end of the reporting period, the Group's continuing operations have unused tax losses of **£2,326m** (2016: £1,629m) for which no deferred tax asset is being recognised. This includes capital losses of **£1,189m** (2016: £1,194m) for which it is unlikely that a deferred tax asset would be recognised as most UK capital gains are exempt from tax. None of these losses are subject to expiry. In addition, the Group has deductible temporary differences of **£198m** (2016: £654m) for which no deferred tax has been recognised.

The Group has temporary differences in respect of the retained earnings of overseas subsidiaries not held for sale of **£509m** (2016: £1,006m) on which overseas taxes, including withholding taxes, might be incurred on the remittance of these earnings to the UK. This amount relates to the Group's subsidiaries in Canada. The Group is able to control the remittance of earnings to the UK and there is no intention to remit the retained earnings in the foreseeable future if the remittance would trigger a material incremental tax liability. As such the Group has not recognised any deferred tax in respect of the potential taxes on the temporary differences arising on unremitted earnings of continuing overseas subsidiaries and associates.

Of the **£220m** (2016: £216m) net deferred tax asset recognised by the Group's continuing operations, **£233m** (2016: £179m) relate to tax jurisdictions in which the Group has suffered a loss in either the current or preceding period. The assets have been recognised on the basis that future taxable profits will be available against which these deferred tax assets can be utilised. The evidence for the future taxable profits is a forecast consistent with the three year operational plans prepared by the relevant businesses, which are subject to internal review and challenge. Where relevant, the forecast includes extrapolations of the operational plans using assumptions consistent with those used in the plans.

16. CASH AND CASH EQUIVALENTS

	2017	2016
	£m	£m
Cash and cash equivalents and bank overdrafts (consolidated statement of cash flows)	1,049	1,087
Add: Overdrafts reported in other borrowings	4	2
Total cash and cash equivalents	1,053	1,089
Less: Assets classified as held for sale	5	104
Total cash and cash equivalents (consolidated statement of financial position)	1,048	985

17. SHARE CAPITAL

The issued share capital of the Parent Company is fully paid and consists of two classes; Ordinary Shares with a nominal value of £1 each and Preference Shares with a nominal value of £1 each. The issued share capital at 31 December 2017 is:

	2017	2016
	£m	£m
Issued and fully paid		
1,022,835,039 Ordinary Shares of £1 each (2016: 1,019,554,986 Ordinary Shares of £1 each)	1,023	1,020
125,000,000 Preference Shares of £1 each (2016: 125,000,000 Preference Shares of £1 each)	125	125
	1,148	1,145

17. SHARE CAPITAL (CONTINUED)

During 2017, the Company issued a total of 3,280,053 new Ordinary Shares of £1 each ranking pari passu with Ordinary Shares in issue (2016: 2,495,144 new Ordinary Shares of £1 each), on the exercise of employee share options and in respect of employee share awards. The number of Ordinary Shares in issue, their nominal value and the associated share premiums are as follows:

	Number of shares	Nominal value £m	Share premium £m
At 1 January 2016	1,017,059,842	1,017	1,077
Issued in respect of employee share options and employee share awards	2,495,144	3	3
At 1 January 2017	1,019,554,986	1,020	1,080
Issued in respect of employee share options and employee share awards	3,280,053	3	3
At 31 December 2017	1,022,835,039	1,023	1,083

Rights attaching to the shares

The rights attaching to each class of share may be varied with the consent of the holders of 75% of the issued shares of that class.

Ordinary Shares of £1 each

Each member holding an Ordinary Share shall be entitled to vote on all matters at a general meeting of the Company, be entitled to receive dividend payments declared in accordance with the Articles of Association, and have the right to participate in any distribution of capital of the Company including on a winding up of the Company.

Preference Shares of £1 each

The Preference Shares are not redeemable but the holders of the Preference Shares have preferential rights over the holders of Ordinary Shares in respect of dividends and of the return of capital in the event of the winding up of the Company.

Provided a resolution of the Board exists, holders of Preference Shares are entitled to a cumulative preferential dividend of 7.375% per annum, payable out of the profits available for distribution, to be distributed in half yearly instalments. Preference shareholders have no further right to participate in the profits of the Company.

Full information on the rights attaching to shares is in the RSA Insurance Group plc Articles of Association which are available on the Group's website.

Employee share schemes

157,866 Ordinary Shares (2016: 414,049 Ordinary Shares) are held by the Share Incentive Plan Trust which may subsequently be transferred to employees (including Executive Directors) to satisfy Sharebuild Matching Share awards. These shares are presented as own shares. Own shares are deducted from equity. No gain or loss is recognised on the purchase, sale, issue or cancellation of the own shares. Any consideration paid or received is recognised directly in equity.

At 31 December 2017, the total number of options over Ordinary Shares outstanding under the Group employee share option plans is 4,996,149 (2016: 5,047,441) and the total number of potential shares outstanding under the long term incentive plan and under the Sharebuild is 11,940,129 Ordinary Shares (2016: 12,638,394 Ordinary Shares).

18. OTHER EQUITY INSTRUMENTS - TIER I NOTES

On 27 March 2017, the Company issued two floating rate Restricted Tier I (RTI) Notes totalling £297m in aggregate size and with a blended coupon of c.4.7%. The Notes are as follows:

Swedish Krona 2,500m at 3 month Stibor +525bps (equivalent to c.4.8% coupon on issue)
 Danish Krone 650m at 3 month Cibor +485bps (equivalent to c.4.6% coupon on issue)

Interest on the Notes is due and payable only at the sole and absolute discretion of the Company, subject to certain additional restrictions set out in the terms and conditions, and is non-cumulative. In addition the terms and conditions of the Notes will require the Company to cancel interest payments in certain circumstances. The Notes are redeemable (subject to certain conditions) at the option of the Company in whole but not in part on the first call date, being the fifth anniversary of the issue date, or any interest payment date thereafter or in the event of certain changes in the tax, regulatory or ratings treatment of the Notes. Any redemption is subject, inter alia, to the Company giving notice to the relevant regulator and the regulator granting permission to redeem. The Notes convert into ordinary shares of the Company, at a pre-determined price in the event that certain solvency capital requirements are breached, as more fully set out in the terms and conditions of the Notes. Accordingly, the Notes are treated as a separate category within Equity and coupon payments are recognised as distributions, similar to the treatment of preference share dividends.

19. LOAN CAPITAL

	2016	Cash movements	Non cash movements	2017
	£m	Settlement	Amortisation	£m
Subordinated guaranteed US\$ bonds	6	-	-	6
Guaranteed subordinated step-up notes due 2039	298	(261)	2	39
Guaranteed subordinated notes due 2045	395	-	1	396
Total dated loan capital	699	(261)	3	441
Perpetual guaranteed subordinated capital securities	369	(375)	6	-
Total loan capital	1,068	(636)	9	441

The subordinated guaranteed US\$ bonds were issued in 1999 and have a nominal value of \$9m and a redemption date of 15 October 2029. The rate of interest payable on the bonds is 8.95%.

The dated guaranteed subordinated step-up notes were issued on 20 May 2009 at a fixed rate of 9.375%. The nominal £500m bonds have a redemption date of 20 May 2039. On 12 July 2016, the Group bought back £200m in nominal value of these step-up notes, with a further £245m being bought back on 31 March 2017, £15m in Q2 2017 and £1m in Q3 and Q4 2017. The remaining £39m has a first call date of 20 May 2019.

The dated guaranteed subordinated notes were issued on 10 October 2014 at a fixed rate of 5.125%. The nominal £400m bonds have a redemption date of 10 October 2045. The Group has the right to repay the notes on specific dates from 10 October 2025. If the bonds are not repaid on that date, the applicable rate of interest would be reset at a rate of 3.852% plus the appropriate benchmark gilt for a further five year period.

The perpetual guaranteed subordinated capital securities issued on 12 May 2006 have a nominal value of £375m and the rate of interest payable is 6.701% of the nominal value. On 29 March 2017, the Group bought back £347m of the outstanding principal amount. The remaining £28m balance was settled in July 2017.

The bonds and the notes are contractually subordinated to all other creditors of the Group such that in the event of a winding up or of bankruptcy, they are able to be repaid only after the claims of all other creditors have been met.

There have been no defaults on any bonds or notes during the year. The Group has the option to defer interest payments on the bonds and notes, but has to date not exercised this right.

20. INSURANCE CONTRACT LIABILITIES

Estimation techniques and uncertainties

Provisions for losses and loss adjustment expenses are subject to a robust reserving process by each of the Group's business units and at Group Corporate Centre, as detailed in the Risk Management note.

There is also considerable uncertainty in regard to the eventual outcome of the claims that have occurred by the end of the reporting period but remain unsettled. This includes claims that may have occurred but have not yet been notified to the Group and those that are not yet apparent to the insured.

The provisions for losses and loss adjustment expenses are estimated using previous claims experience with similar cases, historical payment trends, the volume and nature of the insurance underwritten by the Group and current specific case reserves. Also considered are developing loss payment trends, the potential longer term significance of large events, and the levels of unpaid claims, legislative changes, judicial decisions and economic, political and regulatory conditions.

The Group uses a number of commonly accepted actuarial projection methodologies to determine the appropriate provision to recognise. These include methods based upon the following:

- The development of previously settled claims, where payments to date are extrapolated for each prior year;
- Estimates based upon a projection of claims numbers and average cost;
- Notified claims development, where notified claims to date for each year are extrapolated based upon observed development of earlier years ;
- Expected loss ratios;
- Bornhuetter- Ferguson method, which combines features of the above methods;
- Bespoke methods for specialist classes of business.

In selecting the method and estimate appropriate to any one class of insurance business, the Group considers the appropriateness of the methods and bases to the individual circumstances of the provision class and underwriting year.

Individually large and significant claims are generally assessed separately, being measured either at the face value of the loss adjusters' estimates or projected separately in order to allow for the future development of large claims.

The level of provision carried by the Group targets the inclusion of a margin of 5% for the core businesses on top of the actuarial indication outlined above. The appropriateness of the 5% target is subject to regular review as part of the Group reserving process at Group Corporate Centre.

Discount assumptions

The total value of provisions for losses and loss adjustment expenses less related reinsurance recoveries before discounting for continuing operations is **£8,520m** (2016: £8,784m).

Claims on certain classes of business (excluding annuities) have been discounted as follows:

	Category	Discount rate		Average number of years to settlement from reporting date	
		2017	2016	2017	2016
		%	%	Years	Years
UK	Asbestos and environmental	4.0	4.0	8	11
Scandinavia	Disability	1.3	1.3	8	7

In determining the average number of years to ultimate claims settlement, estimates have been made based on the underlying claims settlement patterns.

As at 31 December 2017, the value of the discount on net claims liability reserves is **£111m** (2016: £388m) excluding annuities and periodic payment orders. All other factors remaining constant, a decrease of 1% in the discount rates would reduce the value of the discount by approximately **£70m** (2016: £120m).

A decrease of 1% in the real discount rate for UK and Scandinavia annuities would reduce the value of the discount by approximately **£100m** (2016: £110m). The sensitivity calculation has taken into consideration the undiscounted provisions for each class of business and the respective average settlement period.

20. INSURANCE CONTRACT LIABILITIES (CONTINUED)

Gross insurance contract liabilities and the reinsurers' share of insurance contract liabilities

The gross insurance contract liabilities and the reinsurers' share of insurance contract liabilities presented in the statement of financial position are comprised as follows:

	Gross	RI	Net
	2017	2017	2017
	£m	£m	£m
Provision for unearned premiums	3,316	(729)	2,587
Provision for losses and loss adjustment expenses	10,113	(2,159)	7,954
Total insurance contract liabilities	13,429	(2,888)	10,541
Less: Held for sale provision for unearned premiums	-	-	-
Less: Held for sale provisions for losses and loss adjustment expenses	636	(636)	-
Less: Total liabilities held for sale	636	(636)	-
Provision for unearned premiums at 31 December net of held for sale	3,316	(729)	2,587
Provision for losses and loss adjustment expenses at 31 December net of held for sale	9,477	(1,523)	7,954
Total insurance contract liabilities excluding held for sale	12,793	(2,252)	10,541

	Gross	RI	Net
	2016	2016	2016
	£m	£m	£m
Provision for unearned premiums	3,328	(818)	2,510
Provision for losses and loss adjustment expenses	10,083	(1,530)	8,553
Total insurance contract liabilities	13,411	(2,348)	11,063
Less: Held for sale provision for unearned premiums	17	(2)	15
Less: Held for sale provisions for losses and loss adjustment expenses	718	(94)	624
Less: Total liabilities held for sale	735	(96)	639
Provision for unearned premiums at 31 December net of held for sale	3,311	(816)	2,495
Provision for losses and loss adjustment expenses at 31 December net of held for sale	9,365	(1,436)	7,929
Total insurance contract liabilities excluding held for sale	12,676	(2,252)	10,424

Provision for unearned premiums, gross of acquisition costs

	2017	2016
	£m	£m
Provision for unearned premiums (gross of acquisition costs) at 1 January	3,994	4,200
Premiums written	7,599	7,477
Less: Premiums earned	(7,583)	(7,624)
Changes in provision for unearned premiums	16	(147)
Gross portfolio transfers and disposals	-	(418)
Exchange adjustment	(24)	357
Other movements	-	2
Provision for unearned premiums (gross of acquisition costs) at 31 December	3,986	3,994
Less: Liabilities classified as held for sale	-	20
Provision for unearned premiums (gross of acquisition costs) at 31 December net of held for sale	3,986	3,974

20. INSURANCE CONTRACT LIABILITIES (CONTINUED)

The provision for unearned premiums is shown net of deferred acquisition costs of **£670m** (2016: £663m). The reasons for the movement in deferred acquisition costs during 2017 are as follows:

	2017	2016
	£m	£m
Acquisition costs deferred during the year	1,101	1,010
Amortisation charged during the year	(1,094)	(1,037)
Exchange (losses)/gains	(4)	56
Other movements	4	6
Assets transferred to held for sale	-	(3)
Movement in deferred acquisition costs	7	32

The reinsurers' share of deferred acquisition costs is included within accruals and deferred income.

Provisions for losses and loss adjustment expenses

The following changes have occurred in the provisions for losses and loss adjustment expenses during the year:

	2017	2016
	£m	£m
Provisions for losses and loss adjustment expenses at 1 January	10,083	9,457
Gross claims incurred and loss adjustment expenses	5,135	5,130
Total claims payments made in the year net of salvage and other recoveries	(5,093)	(5,001)
Gross portfolio transfers, acquisitions and disposals	(46)	(578)
Exchange adjustment	(27)	994
Other movements	61	81
Provisions for losses and loss adjustment expenses at 31 December	10,113	10,083
Less: Liabilities classified as held for sale	636	718
Provisions for losses and loss adjustment expenses at 31 December net of held for sale	9,477	9,365

Claims development tables

The tables below present changes in the historical provisions for losses and loss adjustment expenses that were established in 2007 and the provisions for losses and loss adjustment expenses arising in each subsequent accident year. The tables are presented at current year average exchange rates on an undiscounted basis and have been adjusted for operations that have been disposed of.

The top triangle of the tables presents the estimated provisions for ultimate incurred losses and loss adjustment expenses for each accident year as at the end of each reporting period.

The lower triangle of the tables presents the amounts paid against those provisions in each subsequent accounting period.

The estimated provisions for ultimate incurred losses change as more information becomes known about the actual losses for which the initial provisions were set up and as the rates of exchange change.

20. INSURANCE CONTRACT LIABILITIES (CONTINUED)

Consolidated claims development table gross of reinsurance

	2007 and prior	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Estimate of cumulative claims												
At end of accident year	9,388	2,623	2,524	2,802	2,999	2,854	3,181	2,857	2,850	2,844	3,088	
One year later	8,889	2,644	2,616	2,935	3,053	2,898	3,246	2,973	2,863	2,837		
Two years later	8,524	2,621	2,573	2,875	3,082	2,874	3,169	2,886	2,828			
Three years later	8,125	2,560	2,531	2,905	3,008	2,866	3,123	2,861				
Four years later	7,856	2,554	2,559	2,891	2,942	2,821	3,113					
Five years later	7,625	2,514	2,554	2,856	2,909	2,836						
Six years later	7,544	2,498	2,515	2,817	2,900							
Seven years later	7,499	2,485	2,526	2,803								
Eight years later	7,674	2,483	2,529									
Nine years later	7,910	2,485										
Ten years later	7,832											
2017 Movement	78	(2)	(3)	14	9	(15)	10	25	35	7		158
Claims paid												
One year later	2,352	1,257	1,209	1,533	1,378	1,342	1,491	1,351	1,338	1,440		
Two years later	1,205	401	425	418	499	503	558	429	545			
Three years later	947	252	271	286	334	291	275	292				
Four years later	604	186	200	212	193	190	206					
Five years later	443	123	149	116	108	145						
Six years later	438	72	73	65	77							
Seven years later	308	39	40	54								
Eight years later	155	37	32									
Nine years later	146	23										
Ten years later	227											
Cumulative claims paid	6,825	2,390	2,399	2,684	2,589	2,471	2,530	2,072	1,883	1,440		
Reconciliation to the statement of financial position												
Current year provision before discounting	1,007	95	130	119	311	365	583	789	945	1,397	3,088	8,829
Exchange adjustment to closing rates												(5)
Discounting												(105)
Annuities												758
Present value recognised in the consolidated statement of financial position												9,477
Held for sale												636
Total Group												10,113

20. INSURANCE CONTRACT LIABILITIES (CONTINUED)

Consolidated claims development table net of reinsurance

	2007 and prior	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Estimate of cumulative claims												
At end of accident year	8,017	2,388	2,287	2,455	2,625	2,584	2,776	2,531	2,403	2,263	2,319	
One year later	7,603	2,380	2,345	2,532	2,613	2,616	2,876	2,568	2,332	2,239		
Two years later	7,239	2,379	2,305	2,502	2,597	2,593	2,801	2,522	2,292			
Three years later	6,827	2,331	2,276	2,518	2,549	2,554	2,770	2,472				
Four years later	6,550	2,319	2,309	2,525	2,504	2,515	2,729					
Five years later	6,330	2,289	2,311	2,492	2,478	2,522						
Six years later	6,253	2,269	2,290	2,468	2,463							
Seven years later	6,244	2,256	2,285	2,458								
Eight years later	6,423	2,256	2,271									
Nine years later	6,664	2,246										
Ten years later	6,682											
2017 Movement	(18)	10	14	10	15	(7)	41	50	40	24		179
Claims paid												
One year later	1,974	1,118	1,109	1,282	1,184	1,208	1,328	1,182	1,132	1,071		
Two years later	993	349	363	386	414	407	436	371	317			
Three years later	770	239	238	256	269	248	244	217				
Four years later	498	176	190	196	176	195	188					
Five years later	394	106	130	100	107	122						
Six years later	381	70	70	61	64							
Seven years later	275	35	34	49								
Eight years later	117	30	28									
Nine years later	184	21										
Ten years later	207											
Cumulative claims paid	5,793	2,144	2,162	2,330	2,214	2,180	2,196	1,770	1,449	1,071		
Reconciliation to the statement of financial position												
Current year provision before discounting	889	102	109	128	249	342	533	702	843	1,168	2,319	7,384
Exchange adjustment to closing rates												(19)
Discounting												(99)
Annuities												688
Present value recognised in the consolidated statement of financial position												7,954
Held for sale												-
Total Group												7,954

Insurance and reinsurance liabilities

	2017	2016
	£m	£m
Direct insurance creditors	113	110
Reinsurance creditors	823	849
Total insurance and reinsurance liabilities	936	959
Less: Liabilities classified as held for sale	2	5
Total	934	954

21. POST-RETIREMENT BENEFITS AND OBLIGATIONS

Movement in surplus/(deficit) during the year:

	2017 £m	2016 £m
(Deficit)/surplus at 1 January	(252)	67
Current service costs	(11)	(23)
Past service costs	(1)	(5)
Pension net interest (charge)/credit	(6)	6
Administration costs	(7)	(9)
Gains/(losses) on settlements/curtailments	6	-
Total pension expense	(19)	(31)
Contributions by the Group	101	110
Return on scheme assets less amounts included in pension net interest credit	277	1,279
Effect of changes in financial assumptions	(309)	(1,770)
Effect of changes in demographic assumptions	166	1
Experience gains and losses	(34)	120
Investment expenses	(11)	(10)
Other net surplus remeasurements	(62)	-
Remeasurements of net defined benefit liability	27	(380)
Exchange adjustment	2	(18)
Pension and post-retirement deficit	(141)	(252)
Deferred tax in respect of net pension and post-retirement deficit	53	55
Net pension and post-retirement deficit at 31 December	(88)	(197)

The value of scheme assets and the scheme obligations are as follows:

	2017			2016
	UK £m	Other £m	Total £m	Total £m
Present value of funded obligations	(8,326)	(434)	(8,760)	(8,774)
Present value of unfunded obligations	(7)	(111)	(118)	(119)
Present value of obligations	(8,333)	(545)	(8,878)	(8,893)
Equities	591	161	752	764
Government debt	5,275	147	5,422	5,289
Non-Government debt	3,351	114	3,465	3,276
Derivatives	743	-	743	808
Other (including infrastructure, commodities, hedge funds, loans)	-	26	26	27
Securities at fair value	9,960	448	10,408	10,164
Property	189	-	189	164
Cash	63	7	70	61
Other (including infrastructure, commodities, hedge funds, loans)	519	-	519	484
Other investments	771	7	778	709
Value of asset and longevity swaps	(2,387)	-	(2,387)	(2,232)
Total assets in the schemes	8,344	455	8,799	8,641
Other net surplus remeasurements	(62)	-	(62)	-
Total deficit	(51)	(90)	(141)	(252)
Defined benefit pension schemes	(51)	(30)	(81)	(196)
Other post-retirement benefits	-	(60)	(60)	(56)
Schemes in surplus	119	22	141	70
Schemes in deficit	(170)	(112)	(282)	(322)

The UK defined benefit schemes closed to future accrual on 31 March 2017. UK schemes in surplus have been reduced for the tax cost of an authorised return of surplus, classified above as 'Other net surplus remeasurements'. Our judgement is that the authorised refund tax charge is not an income tax within the meaning of IAS12 and so the surplus is recognised net of this tax charge rather than the tax charge being included within deferred taxation.

NOTES TO THE CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

22. RECONCILIATION OF CASH FLOWS FROM OPERATING ACTIVITIES

The reconciliation of net profit before tax to cash flows from operating activities is as follows:

	Note	2017 £m	2016 £m
Cash flows from operating activities			
Profit for the year before tax from continuing operations		448	101
Adjustments for non-cash movements in net profit for the year			
Amortisation of available for sale assets		58	70
Depreciation		22	20
Amortisation and impairment of intangible assets	11	114	83
Fair value (gains)/losses on disposal of financial assets		(15)	15
Impairment on available for sale financial assets		(4)	(8)
Share of (profit) of associates		(1)	-
(Profit) on disposal of business and realised gains on held for sale assets		(69)	-
Remeasurement of disposal groups		-	234
Foreign exchange loss/(gain)		7	(87)
Other non-cash movements		24	17
Changes in operating assets/liabilities			
Loss and loss adjustment expenses		2	(308)
Unearned premiums		68	(76)
Movement in working capital		(253)	(69)
Reclassification of investment income and interest paid		(181)	(212)
Pension deficit funding		(65)	(65)
Cash generated from investment of insurance assets			
Dividend income		32	28
Interest and other investment income		282	328
Cash flows from operating activities		469	71

RESULTS FOR THE YEAR 2017

23. RESULTS FOR THE YEAR 2017

This financial information set out above does not constitute statutory accounts for the years ended 31 December 2017 or 31 December 2016 but is derived from those accounts. Statutory accounts for 2016 have been delivered to the Registrar of Companies, and those for 2017 will be delivered in due course. The auditors' have reported on those accounts; their reports were (i) unqualified (ii) did not include reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and (iii) did not include a statement under section 498(2) or (3) of the Companies Act 2006.

APPENDIX A: EXCHANGE RATES

Local currency/£	12 Months 2017		12 Months 2016	
	Average	Closing	Average	Closing
Canadian Dollar	1.67	1.70	1.79	1.66
Danish Krone	8.49	8.39	9.11	8.71
Swedish Krona	10.99	11.09	11.59	11.19
Euro	1.14	1.13	1.22	1.17

RESPONSIBILITY STATEMENT

We confirm that to the best of our knowledge:

- A) The financial statements within the full Annual Report and Accounts, from which the financial information within this preliminary announcement has been extracted, are prepared in accordance with International Financial Reporting Standards as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and result of the Group;
- B) The management report within this preliminary announcement includes a fair review of the development and performance of the business and the position of the Group; and
- C) The risk and capital management section within this preliminary announcement includes a description of the principal risks and uncertainties faced by the Group.

Signed on behalf of the Board

Stephen Hester
Group Chief Executive

Scott Egan
Group Chief Financial Officer

21 February 2018

21 February 2018