Liberty Mutual Insurance Europe Plc

Solvency and Financial Condition Report
As at 31st December 2017

Contents

SUMMARY

Introduction

This Solvency and Financial Condition Report (SFCR) has been prepared to satisfy the requirements of Article 292 of the Delegated Acts for the implementation of Solvency II, for Liberty Mutual Insurance Europe Plc (LMIE), or the 'Company' for the year ended 31 December 2017. This is the second such Report following the implementation of the Solvency II regime for 2016.

LMIE is part of a Sub-Group of companies consolidating into Liberty International European Holdings, S.L.U. (hereinafter referred to as LIEH or the holding Company) whose ultimate parent company is Liberty Mutual Holding Company Inc. (hereinafter referred to as Liberty Mutual, LMHC, or the ultimate parent Company). Boston based Liberty Mutual Holding Company, the parent corporation of the Liberty Mutual Insurance group of entities is a diversified global insurer and fourth largest property and casualty insurer in the U.S. based on 2016 direct written premium. The Liberty Mutual Insurance group employs more than 50,000 people in over 800 offices throughout the world and, through its subsidiaries and affiliated companies, offers a wide range of property and casualty insurance products and services to individuals and businesses alike.

LMIE operates within the Liberty Specialty Markets (LSM) organisation, representing Liberty Mutual Group's (LMG) Global Specialty business unit in the London Market, together with Liberty Syndicate 4472 at Lloyd's. Our policies and procedures are written at LSM level, this is because we manage our business and strategy at LSM level, whilst maintaining appropriate oversight over legal entities.

LMIE was re-registered as a UK public company in March 2018. During 2018 it is intended that LMIE will convert to a UK societas europaea. Thereafter LMIE may transfer its corporate seat from the UK to Luxembourg, while maintaining its UK presence as a branch. The timing of this latter step is at present uncertain.

As part of the Brexit strategy, LMIE has established and licensed an in-house coverholder in Luxemburg, Liberty Specialty Markets Europe Sarl (LSME). LSME acts as an intermediary company, acting on behalf of LMIE, and it began underwriting on behalf of LMIE from its branches throughout Europe on 1 November 2017.

The Brexit strategy has been designed to accommodate whichever circumstances pertain after March 2019, whether this is a full UK exit or interim transitional arrangements.

Business and performance

On a UK GAAP basis, the Company reported losses before tax of $125.6m (2016 profits: $44.4m), and after taking into account tax and gains on the investment portfolio, total comprehensive losses of $90.5m, compared to total income of $38.6m in 2016. This is due to the abnormally high catastrophe losses in the U.S. in the third quarter and adverse developments in the Property and General Liability book. This is after taking into account favourable reserve development from prior years.

System of governance

The Board of directors is responsible for the governance of the company and they have established a robust corporate governance framework as an effective means of meeting that responsibility. The board is headed by an independent non-executive chairman, who is responsible for leadership of the board and ensuring its effectiveness. The board gives the President and Managing Director the responsibility for the running of the company's business.

The Board delegates certain matters to the following Board Committees in accordance with the terms of reference of those committees:

- Audit Committee
- Board Executive Committee
- Investment Committee
- Nomination Committee
- Remuneration Committee
- Reserving Committee
- Risk Management Committee

The Board and Committees are supported by LMIE key control functions of Actuarial, Risk Management, Compliance and Internal Audit. Each function is headed by an individual who performs either a Senior Insurance Management Function or Significant Influence Function role.

The governance structure is reviewed on an annual basis by the Head of Governance in order to ensure that it is effective and appropriate to the organisation. There have been no material changes in the system of governance during the period.

LMIE requires all persons who perform key functions and are classified as Senior Insurance Managers, i.e. those persons who effectively run the business, to have adequate knowledge and experience to enable sound and prudent management of risks facing the company and to be of good repute and integrity.

The Company operates within a Risk Management and Internal Control Framework (RMF) which is designed to enable LSM's operations to engage with risk in a controlled fashion consistent with the Board's appetite and available capital capacity in order to generate risk adjusted returns to the Liberty Mutual Group.

Risk profile

In order for LMIE to be able to properly reflect its risk profile, all material risks affecting it are considered as part of LMIE's risk management framework, insofar they may adversely impact the achievement of its goals.

The aforementioned exercise covers both quantitative as well as qualitative risks (e.g. Group / Contagion / strategic etc.), and is undertaken both on ongoing conditions as well as part of stressed scenarios, informing LMIE ORSA policy, as well as its Capital management strategy, including capital needs, transferability and fungibility as appropriate.

The Company has undertaken stress testing as part of its annual Own Risk and Solvency Assessment (ORSA) process. The results of same provide assurance that LMIE can withstand both plausible and extreme shocks over its planning horizon.

The risk profile of the Company is described in Section C with regard to the following risk categories:

- Underwriting risk
- Market risk
- Credit risk
- Liquidity risk

- Operational risk
- Other material risks

The LSM Risk Universe Policy sets out how LSM undertakes the categorisation of exposed risks. The business objectives of the Risk Universe policy are to ensure that:

- All risks that could impact the on-going viability of the company are identified.
- Identified risks are measured and managed in the most appropriate method.
- All risks are owned by the most appropriate Executive and that each risk is reported through the correct committee or working group.

Risk Management is responsible for preparing the Own Risk and Solvency Assessment ("ORSA") report. The purpose of the ORSA process is to inform the Board of the ongoing assessment of the risk to LMIE both due to its current activities as well as those arising from its business strategy and future plans. It also informs all stakeholders concerned, on how LMIE plans to mitigate these risks and how much current and future capital is required to both maintain solvency and support the achievement of the business plan.

LSM has two approaches to risk management defined by how the risk is categorised in the Risk Universe Policy. Intrinsic risks, which we actively seek, are managed through the use of risk appetites that are cascaded. Operational risks and other risks (strategic and group risk) for which LSM has limited appetite are managed through the Operational Risk & Internal Controls Policy and associated procedures.

Valuation for solvency purposes

LMIE prepares its annual financial statements under UK GAAP, and in particular under FRS 102 and 103. Its financial statements are presented in US dollars, the functional currency of LMIE.

As at 31 December 2017, LMIE total assets and liabilities under Solvency II valuation rules are $3,641.2 and $2,684.9m respectively (2016: $3,336.1m and $2,328.8m.). The Solvency II values are derived on a fair value basis under the EIOPA guidelines on valuation. In addition, Solvency II reporting formats require some reclassification of assets and liabilities from the categories reported in the financial statements.

The valuation and reclassification differences are extensively described in Section D of this report. The key valuation differences relate to the treatment of technical provisions.

Capital management

The purpose of own funds management is to maintain, at all times, sufficient own funds to cover the Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR) with an appropriate prudence margin as approved by the LMIE Board. The Company holds quarterly board meetings, in which the proportion of own funds over SCR and MCR are monitored and managed.

As part of own funds management, LMIE prepares ongoing annual projections and reviews the structure of own funds and future requirements. The business plan, which forms the base of the ORSA, contains a two-year projection of funding requirements and this helps focus actions for future funding.

LMIE currently uses the standard formula (SF) as defined by EIOPA to assess LMIE's ability to meet all of its regulatory capital obligations under normal and stressed conditions. However, the internal model is used alongside the SF to help LMIE understand and manage risks to its business, and challenge SF outputs where appropriate.

The capital of LMIE comprises share capital, share premium and reconciliation reserves, categorised as Tier One.

As at 31st December 2017 the SCR was $749.2m (2016: $710m) and LMIE had own funds in support of this of $956.2m (2016: $1,007m). LMIE complied with its capital management policy throughout the period.

DIRECTORS STATEMENT

Approval by the Liberty Mutual Insurance Europe Plc (LMIE) Board of Directors

of the Solvency and Financial Condition Report

For the financial year ended 31st December 2017

The Directors are responsible for preparing the SFCR in accordance with the Prudential Regulatory Authority (PRA) rules and SII Regulations.

The PRA Rulebook for SII firms in Rule 6.1(2) and Rule 6.2(1) of the Reporting Part requires that the Company must have in place a written policy ensuring the ongoing appropriateness of any information disclosed and that the Company must ensure that its SFCR is subject to approval by the Directors.

Each of the Directors, whose names and functions are listed in Directors' Report of the UK GAAP financial statements, confirm that, to the best of their knowledge:

(a) Throughout the financial year in question, the Company has complied in all material respects with the requirements of the PRA rules and SII Regulations as applicable; and

(b) It is reasonable to believe that, at the date of the publication of the SFCR, the Company continues to comply, and will continue to comply in future.

On behalf of the board.

J A R Dunn

Group Finance Director

M Moore

President and Managing Director

4th May 2018

AUDIT REPORT

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Report of the external independent auditor to the Directors of Liberty Mutual Insurance Europe Limited ('the Company') pursuant to Rule 4.1(2) of the External Audit Part of the PRA Rulebook applicable to Solvency II firms

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

Opinion

Except as stated below, we have audited the following documents prepared by the Company as at 31 December 2017:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Company as at 31 December 2017 ('the Narrative Disclosures subject to audit'); and
- Company templates S.02.01.02, S.17.01.02, S.23.01.01, S.25.01.21 and S28.01.01 ('the Templates subject to audit').

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

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

- The 'Business and performance', 'System of governance' and 'Risk profile' elements of the Solvency and Financial Condition Report;
- Company templates S05.01.02, S05.02.01 and S.19.01.21; and
- the written acknowledgement by management of their responsibilities, including for the preparation of the Solvency and Financial Condition Report ('the Responsibility Statement').

To the extent the information subject to audit in the relevant elements of the Solvency and Financial Condition Report includes amounts that are totals, sub-totals or calculations derived from the Other Information, we have relied without verification on the Other Information.

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

Basis for opinion

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

Conclusions relating to going concern

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

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

Emphasis of Matter – Basis of Accounting & Restriction on Use

We draw attention to the 'Valuation for solvency purposes', 'Capital Management' and other relevant disclosures sections of the Solvency and Financial Condition Report, which describe the basis of accounting. The Solvency and Financial Condition Report is prepared in compliance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based, and therefore in accordance with a special purpose financial reporting framework. As a result, the Solvency and Financial Condition Report may not be suitable for another purpose. The Solvency and Financial Condition Report is required to be published, and intended users include but are not limited to the Prudential Regulation Authority.

This report is made solely to the Directors of the Company in accordance with Rule 2.1 of the External Audit Part of the PRA Rulebook for Solvency II firms. Our work has been undertaken so that we might report to the Directors those matters that we have agreed to state to them in this report and for no other purpose.

Our opinion is not modified in respect of these matters.

Other Information

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

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

Responsibilities of Directors for the Solvency and Financial Condition Report

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

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

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

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

Our objectives are to obtain reasonable assurance about whether the relevant elements of the Solvency and Financial Condition Report are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decision making or the judgement of the users taken on the basis of the Solvency and Financial Condition Report.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: https://www.frc.org.uk/Our-Work/Audit-and-Actuarial-Regulation/Audit-and-assurance/Standards-and-guidance/Standards-and-guidance-for-auditors/Auditors-responsibilities-for-audit/Description-of-auditors-responsibilities-for-audit.aspx. The same responsibilities apply to the audit of the Solvency and Financial Condition Report.

Report on Other Legal and Regulatory Requirements.

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

Ernst & Young LLP

Ernst & Young LLP
London
04 May 2018

The maintenance and integrity of the Company's web site is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Solvency and Financial Condition Report since it was initially presented on the web site.

SECTION A - BUSINESS AND PERFORMANCE

SECTION A. 1 – Business

Name and legal form of the undertaking

Liberty Mutual Insurance Europe Limited (LMIE) is a regulated insurance company incorporated in the United Kingdom (Registration number 1088268). The Company was re-registered under the Companies Act 2006 as a public company under the name of Liberty Mutual Insurance Europe Plc on 1 March 2018.

The immediate parent Company is Liberty Specialty Markets Holdco SL. The immediate parent was transferred from Liberty UK and Europe Holdings Limited in December 2017.

The ultimate parent Company is Liberty Mutual Holding Company Inc.(LMHC) of Boston, 175 Berkeley Street, Boston, Massachusetts 02117, U.S.A. a Company incorporated in the United States of America.

The smallest higher group of companies for which group accounts are drawn up and of which this Company is a member is Liberty International European Holdings S.L (Spain).

Boston based Liberty Mutual Holding Company, the parent corporation of the Liberty Mutual Insurance group of entities is a diversified global insurer and fourth largest property and casualty insurer in the U.S. based on 2016 direct written premium. The Company also ranks 75th on the Fortune 100 list of largest corporations in the U.S. based on 2016 revenue. As of December 31, 2017, LMHC had $142.502 billion in consolidated assets, $121.814 billion in consolidated liabilities, and $39.409 billion in annual consolidated revenue. The Liberty Mutual Insurance group employs more than 50,000 people in over 800 offices throughout the world.

LMHC, through its subsidiaries and affiliated companies, offers a wide range of property, casualty and life insurance products and services to individuals and businesses alike.

In early 2018, Liberty Mutual announced the realignment of its businesses to enhance the company's ability to meet the changing needs of consumer and business customers. Liberty Mutual's realignment features the following:

• Global Retail Markets (GRM) combining Global Consumer Markets with Business Insurance and Accident and Health organizations formerly in Commercial insurance.

• Global Risk Solutions (GRS) which brings together Liberty's Global Specialty, Ironshore, National Insurance and the Global Reinsurance Strategy Group into a single business.

These actions will allow the organization to focus on property and casualty insurance, and to take full advantage of the Company's scale, products, and capabilities globally.

LMIE forms part of Global Risk Solutions (GRS).

Name of the supervisory authority responsible for the financial supervision of the undertaking and external auditor

The Prudential Regulatory Authority (PRA) is responsible for the prudential supervision of the Company. Prudential Regulatory Authority, Bank of England, Threadneedle St, London, EC2R 8AH.

LMIE consolidates into the Spanish Entity Liberty International European Holding S.L. for Solvency II purposes and therefore is subject to Group Solvency II reporting via Liberty International European Holding S.L. The Group supervisor is “Direccion General de Seguros” (DGS, Spanish supervisor), which is located in Paseo de la Castellana, 44, Madrid, Spain. Furthermore, the consolidation is under the supervision of The Colleges of Supervisors which includes the PRA, DGS CBI (Ireland supervisor) and ASF (Portuguese supervisor).

At the global level the Group supervision is undertaken by the Division of Insurance of the Commonwealth of Massachusetts, located in 1000 Washington Street, 8th Floor, Boston, MA 02118, US.

Name of the external auditor

The Company’s external auditors are Ernst & Young LLP, 25 Churchill Place, London E14 SEY.

Holders of qualifying holdings

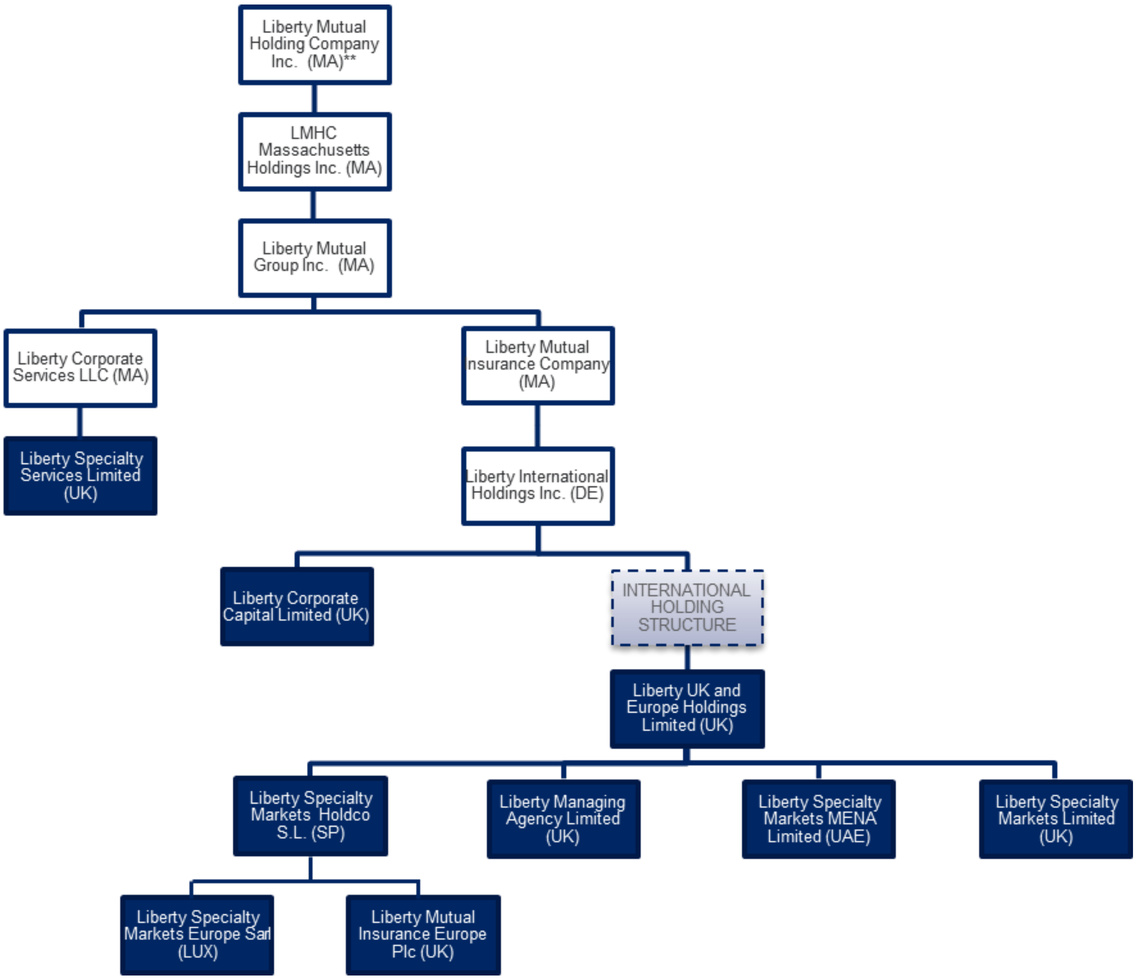
LMIE is wholly owned by the immediate parent company, Liberty Specialty Markets Holdco SL . The ultimate parent is Liberty Mutual Holding Company

The members of Liberty Mutual Holding Company are persons or organizations appearing as the primary insured in an in-force policy, or as the principal in the case of a surety bond, issued by only the following stock insurance companies:

1. Liberty Mutual Insurance Company
2. Liberty Mutual Fire Insurance Company
3. Employers Insurance of Wausau and
4. Liberty Mutual Personal Insurance Company

Details of the undertaking's position within the legal structure of the group

The following is a summarised organisation structure showing LMIE’s positioning within the overall Liberty group structure.



Unless otherwise stated ownership is 100%.

LMIE sits within the international holding structure of Liberty Mutual Holding Company Inc. The organisation chart shown is a summarised view of the overall Liberty structure and there are a number of companies within the hierarchy.

The undertaking's material lines of business and material geographical areas where it carries out business

LMIE is one of the key legal entities that makes up Liberty Specialty Markets (LSM) operating unit which is part of Global Risk Solutions business unit within Liberty Mutual Group (LMG). LSM manages its business through three key management Pillars which consist of a number of divisions made up of a number of lines of business. These lines differ from the Solvency II lines of business which mainly comprise, General Liability, Fire and other damage to Property and Credit and Suretyship. The lines managed by LSM have been mapped to the appropriate Solvency II lines of business in this report.

The Company predominantly operates from the United Kingdom and through a branch structure in mainland Europe, consisting of: Spain, France, Switzerland, Germany, Netherlands, Ireland and Italy

The Company took the decision to cease its branch activities in Asia, resulting in the exit from the Hong Kong and Labuan branches in August 2017.

Significant business or other events that have occurred over the reporting period and up to the date of the report

Through its European branch structure, the Company has significant operations and employees in the EU and enjoys a number of benefits from the UK being a member of the EU.

On 23 June 2016, through a referendum, the UK voted to leave the EU and on 29 March 2017, Article 50 of the Lisbon Treaty was triggered by the UK Government commencing the process of formal negotiation between the UK and the EU on the UK's exit which is expected to occur during a two-year period. A high degree of uncertainty exists around what the terms of the UK's relationship with the EU will be and whether any benefits of the current four freedoms of the EU will remain.

LMIE was re-registered as a UK public company in March 2018. During 2018 it is intended that LMIE will convert to a UK societas europaea. Thereafter LMIE may transfer its corporate seat from the UK to Luxembourg, while maintaining its UK presence as a branch. The timing of this latter step is at present uncertain.

As part of the Brexit strategy, LMIE has established and licensed an in-house coverholder in Luxemburg, Liberty Specialty Markets Europe Sarl (LSME). LSME acts as an intermediary company, acting on behalf of LMIE, and it began underwriting on behalf of LMIE from its branches throughout Europe on 1 November 2017.

The Brexit strategy has been designed to accommodate whichever circumstances pertain after March 2019, whether this is a full UK exit or interim transitional arrangements.

With effect from 20 December the immediate parent undertaking of the Company, Liberty UK and Europe Holdings Limited (LUEH), an English company (company number 7062171), whose registered office is at 20 Fenchurch Street, London EC3M 3AW, transferred its entire interest in the Company to Liberty Specialty Markets Holdco S.L., a Spanish sociedad limitada, whose registered office is at Paseo de las Doce Estrellas n. 4, 28042 Madrid (the "Transferee").

SECTION A. 2 – Underwriting Performance

Underwriting performance by Solvency II Lines of Business

The following table outlines the Company's key financial performance indicators during the year ended 31 December 2017 by Solvency II lines of business. Note that the 2016 comparative amounts have been restated to conform with the 2017 presentation.

2017	Gross Written Premiums $(000)	Net Earned Premiums $(000)	Net Incurred Claims $(000)	Expenses $(000)	Underwriting Performance $(000)
Motor vehicle liability	(72)	6	(9,645)	(123)	9,773
Other motor	(9)	1	(1,192)	(15)	1,208
Marine, Aviation and transport	48,773	56,603	35,176	17,526	3,901
Fire and other damage to property	211,834	139,885	195,919	49,461	(105,496)
General Liability	603,723	364,854	282,949	141,473	(59,569)
Credit and Suretyship	201,089	82,334	34,619	38,077	9,638
Miscellaneous Financial loss	138,669	1,142	930	(6,244)	6,457
Non proportional reinsurance Casualty	2,147	(6,062)	426	(453)	(6,034)
Non proportional reinsurance Marine, Aviation and transport	2,284	(8,597)	213	1,317	(10,127)
Non proportional reinsurance Property	42,223	12,336	(5,492)	7,011	10,817
Other non-assigned				1,932	(1,932)
TOTAL	**1,250,662**	**642,502**	**533,904**	**249,962**	**(141,364)**

Investment Income	33,658
Other expenses reported in the Financial Statements	17,866
Total loss for the period as reported in the Financial Statements	**(125,572)**

2016 Restated	Gross Written Premiums $(000)	Net Earned Premiums $(000)	Net Incurred Claims $(000)	Expenses $(000)	Underwriting Performance $(000)
Motor vehicle liability	1,797	25,411	24,179	3,862	(2,629)
Other motor	222	3,141	2,988	476	(324)
Marine, Aviation and transport	38,853	31,911	41,840	16,905	(26,834)
Fire and other damage to property	204,082	143,536	122,619	61,696	(40,779)
General Liability	573,728	371,588	209,425	148,665	13,498
Credit and Suretyship	204,316	53,489	42,145	35,982	(24,638)
Miscellaneous Financial loss	138,713	(322)	1,749	(8,522)	6,451
Non proportional reinsurance Casualty	21,002	13,304	(3,501)	(769)	17,574
Non proportional reinsurance Marine, Aviation and transport	3,604	3,438	(8,474)	936	10,976
Non proportional reinsurance Property	15,295	9,782	3,339	1,483	4,959
Other non-assigned				846	(846)
TOTAL	**1,201,612**	**655,278**	**436,310**	**261,561**	**(42,593)**

Investment Income	73,400
Other expenses reported in the Financial Statements	(13,524)
Total profit for the period as reported in the Financial Statements	**44,331**

Overview and highlights

The Company made a loss before tax of $125.6m in 2017, compared to a profit of $44.3m in 2016.

Gross written premiums increased by $49m in 2017, up 4% when compared to 2016. The Company's strategy of identifying and investing in growth areas meant that, despite highly competitive market conditions, the Company's business expanded in its core areas in 2017.

The claims ratio increased to 83.1% in 2017 from 66.6% in 2016. This is due to the abnormally high catastrophe losses in the U.S. in the third quarter and adverse developments in our Commercial Property and Casualty book. This is after taking into account favourable reserve development from prior years.

The result for 2017 was also adversely impacted by foreign exchange losses of $17.9m (2016 gains of $13.5m). Investment return fell from $73.3m to $32.7m as bond yields fell, while operating expenses fell by $12m in the year.

Gross written premiums grew in a number of classes, reflecting rate increases (Aviation), growth in certain product lines (Property and Binders in Fire and other damage to property, Single Project business, multi-year Capital Products deals in General Liability), this was offset by decreases in certain areas (Offshore Energy in General Liability due to a lack of desirable opportunities), and as the company had exited Motor business, and sold the regional commercial casualty business in previous years.

Claims experience was slightly worse than just volume growth due to the 2017 hurricane losses (Fire and property) a number of large losses in the Onshore Heavy Industry and Oil and Gas portfolios, deteriorating experience in the UK commercial casualty book, and a number of large claims in the Energy Liability and Financial Lines' books.

Underwriting Result by material geographical area

The Company is managed by underwriting division as detailed above. The following table summarises the underwriting performance of the Company by its material geographic areas.

As at 31st December 2017	Gross Written Premiums $(000)	Net Earned Premiums $(000)	Net Incurred Claims $(000)	Expenses $(000)	Underwritting Performance $(000)
United Kingdom	648,458	299,616	234,417	123,786	(58,587)
France	101,646	48,135	34,202	19,402	(5,469)
Ireland	62,439	9,158	6,124	5,575	(2,541)
Spain	48,765	34,004	19,984	12,579	1,442
Italy	48,163	30,546	22,768	14,113	(6,334)
United States	90,672	46,961	66,959	16,537	(36,536)

As at 31st December 2016	Gross Written Premiums $(000)	Net Earned Premiums $(000)	Net Incurred Claims $(000)	Expenses $(000)	Underwritting Performance $(000)
United Kingdom	673,843	362,360	251,977	145,249	(34,865)
France	113,940	43,189	30,477	18,061	(5,348)
Spain	42,616	35,512	16,950	11,262	7,300
Italy	49,426	31,008	18,851	14,819	(2,662)
United States	65,350	24,427	2,553	8,450	13,424
Netherlands	36,343	26,733	16,451	9,625	657

LMIE's geographical footprint continues to focus on UK, Europe and the US markets.

The results by geographical location are largely due to the abnormally high catastrophe losses in the U.S. in the third quarter and adverse developments.

LMIE writes Structured Risks Solutions (SRS) policies that are typically more specialist or structured in nature and can vary year on year depending on specific business opportunities. This has led to an increase in GWP in Ireland and US.

The result for Netherland is consistent year on year, however, Netherlands is not reported in 2017 due to Ireland writing more business in 2017

SECTION A. 3 – Investment Performance

The investment portfolio is managed by Liberty Mutual Investments, the specialist investment management arm of LMG. In accordance with investment guidelines, the investment strategy is approved by the LMIE Investment Committee, then by the LMIE Board. There is a minimum credit rating requirement of investment grade and an average quality requirement of A. Limits are also established by issue, counterparty, asset type and rating. Securities must be readily marketable.

The Company's investment portfolio is made up predominantly of debt securities and other fixed income securities.

The following summarise the investment results for the year.

2017 $(000)	Net Investment Income Interest and Dividends	Realised Gains and Losses	Amortisation	Net Investment Income	Unrealised Gains and Losses	Forex gains and losses	Total Investment Return
Government bonds	18,291	1,442	(7,982)	11,750	4,723	0	16,473
Corporate bonds	42,033	2,944	(25,530)	19,448	14,966	0	34,414
Collateralised securities (interest)	253	0	(87)	166	50	0	216
Collective Investment Undertakings	124	1,813	0	1,936	0	0	1,936
Cash and deposits	358	0	0	358	0	0	358
Total Investment income	**61,059**	**6,199**	**(33,599)**	**33,658**	**19,739**	**0**	**53,397**

2016 $(000)	Net Investment Income Interest and Dividends	Realised Gains and Losses	Amortisation	Net Investment Income	Unrealised Gains and Losses	Forex gains and losses	Total Investment Return
Government bonds	21,779	2,297	0	24,076	3,181	0	27,257
Corporate bonds	38,315	9,348	0	47,663	5,376	0	53,038
Collateralised securities (interest)	302	0	0	302	13	0	316
Collective Investment Undertakings	56	748	0	804	43	0	847
Cash and deposits	554	0	0	554	0	0	554
Total Investment income	**61,006**	**12,394**	**0**	**73,400**	**8,612**	**0**	**82,012**

Investments in Securitisations

The Company's holdings in securitised assets is shown in the table following:

$(000)	2017	2016
RMBS	5,234	10,272
CMBS	3,816	3,885
ABS	197	1,114
Total	**9,247**	**15,271**

SECTION A. 4 – Performance of Other Activities

Administrative expenses are incurred in the day to day running of the Company, these include items such as staff and office costs, and bad debts, note this is not an exhaustive list.

Material Leasing arrangements for both finance and operating:

At 31 December 2017, the Company had future minimum rentals payable under operating leases rechargeable from its service company as follows.

Other obligations including Leases	2017 $(000)	2016 $(000)
Future minimum rentals payable under operating leases rechargeable from LSML to the Company are as follows:	7,062	7,078
Later than one year and not later than five years	23,110	22,572
Later than five years	46,281	47,118
Total	76,453	76,453

SECTION A. 5 – Any Other Information

Exchange losses of $17,866m (2016: exchange gains $13,524m) were reported in 2017.

No other material events have occurred during the year.

SECTION B - SYSTEM OF GOVERNANCE

SECTION B. 1 – General Information on the System of Governance

On the 19th of January 2018, Liberty Mutual restructured its operations and the new structure consolidates Liberty's underwriting into two new units, Global Risk Solutions (GRS) and Global Retail Markets (GRM).

Liberty Mutual also announced that its new global risks solutions business will be structured into four separate divisions as part of a reorganisation in the wake of the sale of its life business.

Liberty Specialty Markets (LSM) will operate the group's reinsurance and specialty insurance businesses based outside the US and Canada. This brings together, under a single management team in London, LSM's existing operations with Liberty Mutual and Ironshore's existing specialty operations in South America, Asia Pacific, Bermuda and Europe, including Pembroke, which will continue to operate independently from Liberty's syndicate business.

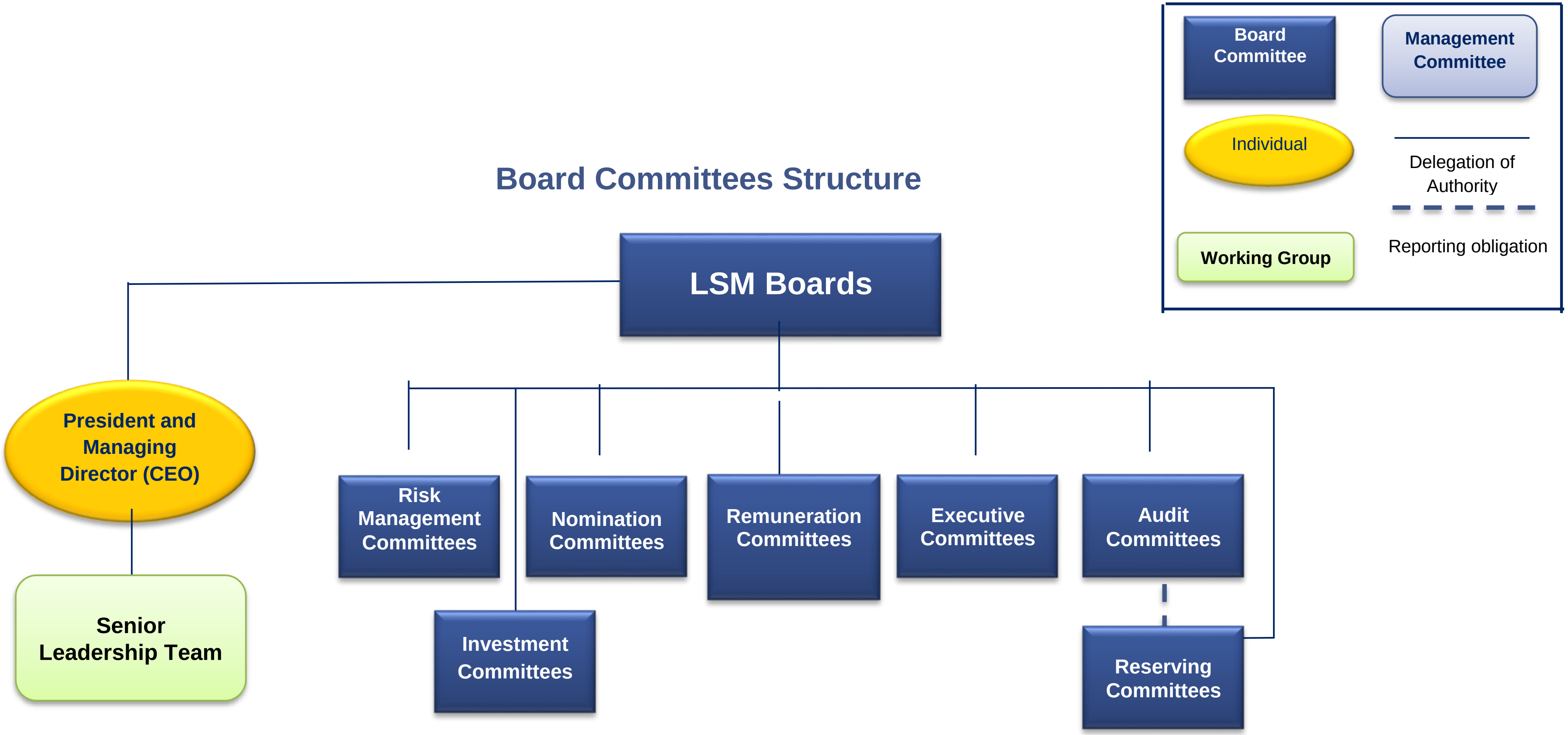
LMIE is one of the key legal entities that makes up LSM.

LMIE's corporate governance framework is the system by which the company is directed and controlled. The board of directors is responsible for the governance of the company and they have established a corporate governance framework as an effective means of meeting that responsibility. LMIE adheres to the provisions of its Articles of Association and the Companies Act and principles of good corporate governance.

Management and Governance Structure

The ultimate supervisory body of the company is the board of directors which has the responsibility of ensuring that the principles of good governance are observed at the board, sub-committees of the board and throughout the organisation. The board and sub-committees are set out below with a description for each of its main roles and responsibilities.

Board Committees Structure



Overview of the role of the Board

Segregation of Board Responsibilities

The board is headed by a non-executive chair, who is responsible for leadership of the board and ensuring its effectiveness. The board gives the chief executive officer (CEO) the responsibility for the running of the company's business. The role of the independent non-executive directors is to scrutinise and challenge the performance of management in meeting agreed goals and objectives and to monitor the reporting of performance. They satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and effective. The Board of Directors are supported by the Legal, Governance and Company Secretarial teams.

Overview of the Board Committees

The Board delegates certain matters to the following Board Committees in accordance with the terms of reference of those committees:

- Audit Committee
- Board Executive Committee
- Investment Committee
- Nomination Committee
- Remuneration Committee
- Reserving Committee
- Risk Management Committee

Audit Committee

The Audit Committee is responsible for assisting the Board in assessing the financial reporting processes, internal controls, performance of the internal and external audit processes and any other matters that may impact the financial results of the Company.

The Committee membership consists of the Chair of the Board and two highly skilled and experienced independent Non-Executive Directors. The Committee is attended by senior management including the Head of Internal Audit and lead partner of the external auditors.

The Chair of the Committee reports to the Board on the activities of the Committee. The Committee meets with the external auditors and Head of Internal Audit without members of management present. The responsibilities of the Audit Committee include:

- Monitoring the financial statements and making recommendations to the board.
- Reviewing the consistency of, and any changes to accounting and reserving policies.
- Reviewing the appropriateness of management's tax strategy and controls.
- Keep under review the operating effectiveness of the Company's internal controls, including the adequacy of policies and procedures related to financial crime.
- Review the procedures for handling allegations from whistle-blowers their subsequent investigation and appropriate follow up.
- Consider and approve the remit of the Internal Audit function, monitoring its resources, reviewing its effectiveness and approval of the annual Internal Audit plan.
- Receive all significant reports relevant to internal controls and review and monitor management's responsiveness to the report.

Board Executive Committee

The Board Executive Committee (BEC) is responsible for dealing with certain matters delegated to it by the Board relating to the day-to-day management of the business. The Committee membership is comprised of the Executive Directors.

The Chair reports to the Board on its proceedings. The BEC considers and, if thought fit, approves and authorises executive management to carry out a range of duties subject to amounts within any requisite LSM protocols. These duties include approval and authority to execute regulatory returns not specifically reserved to the board.

Investment Committee

The Investment Committee is responsible for assisting the Board in overseeing the Company's Investment and Market Risk policies and procedures. The Committee ensures that the Company has sufficient assets to cover claims as they fall due and seeks to optimise investment income and achieve a return based on an acceptable level of active risk. The Committee also has oversight for the management of treasury issues.

The Committee membership comprises two Executive Directors and an experienced independent Non-Executive Director.

The Chair of the Committee is the Group Finance Director who reports to the Board on the activities of the Committee. The responsibilities of the Investment Committee include:

- Make recommendations to the Board regarding; the long-term framework and strategy for the investment of assets and the appointment of Investment Manager(s).
- Approve the investment management policy covering market risk; liquidity risk; asset liability management; asset concentration and credit risk and investment strategy.
- Approve the translation of these policies into Investment Guidelines and ensure that they are incorporated into an Investment Management Agreement, setting out the scope of Investment Managers authority as approved by the Committee.
- Review investments held and performance against stated investment objectives.
- Oversee the Investment Manager(s) operational performance and compliance with Investment Guidelines and Investment Management Agreement.
- In conjunction with the Investment Manager(s), set minimum liquidity levels for the Company to meet any cash requirements as they fall due.

Nomination Committee

The Nomination Committee for ensuring that the Board remains balanced both in terms of skill and experience and between executive and non-executive directors; leads the process for appointments to the Board and makes recommendations to the Board ensuring there is a formal, rigorous and transparent procedure.

The Chair of the board chairs the Nomination Committee and membership consists of a minimum of one Executive Director and one non-executive director.

The responsibilities of the Committee include:

- Regularly review the structure, size, diversity (in skill and person) and composition (including the skills, knowledge and experience) of the board and make recommendations to the Board with regard to any changes.
- Consider succession planning for senior executives in the course of its work, taking into account the challenges and opportunities facing the Company.
- Be responsible for identifying and nominating for the approval of the Board, candidates to fill board vacancies as and when they arise.
- Keep under review the time required from non-executive directors and assess whether the non-executive directors are spending enough time to fulfil their duties.
- Make recommendations to the board concerning the membership of the board committees and any matters relating to the continuation in office of any director at any time.

Reserving Committee

The Reserving Committee is responsible for overseeing the operational and functional integrity of the reserving process and monitoring conformity to the Reserving Risk Appetite specified by the Board. The committee is responsible for making proposals to the Board regarding reserves for the purposes of financial reporting bringing together underwriting, claims, actuarial and finance professional knowledge and judgement.

The Committee membership includes the CEO and Group Finance Director.

The Chair of the Committee is the Group Finance Director who reports to the Board on the activities of the Committee. The main responsibilities of the Committee include:

- Review quarterly reports from the Actuarial Function (Head of Reserving) setting out its professional views on the level of reserves, together with the key uncertainties affecting the reserves and their potential financial impact.
- Oversee the actuarial reserving process and the Technical Provisions Policy.
- Review quarterly reserves booked by Finance on an accident year basis, taking into consideration the views of the Head of Reserving and the Chief Actuary.
- Review the booked reserves and verify that they are within the bounds specified in the Reserving Risk Appetite set out by the Board.
- Review the Reserving Risk Policy and Procedures, Key Risk Indicators and Key Control Indicators in conjunction with the Risk Management Function.
- Brief the Audit Committee on key judgements and uncertainties to inform its recommendation to the Board regarding the level of reserves for the purposes of the financial statements.

Remuneration Committee

The Remuneration Committee is responsible for setting the remuneration policy across the Company; and determining the total individual remuneration package of in scope executives including basic salary and short- and long-term incentive awards. The Chair of the Board is the Committee Chair who with one independent non-executive director comprises the committee.

The main responsibilities of the Committee include:

- Determine the remuneration policy and review its on-going appropriateness.
- Within the terms of the agreed policy determine the total individual remuneration package of each executive director and other designated senior executives as determined by the Committee from time to time as being in scope.
- When setting remuneration policy for directors, review and have regard to pay and employment conditions across the Company.
- Oversee any major changes in core employee benefit structures.
- Agree the policy for authorising claims for expenses from the directors.
- Ensure that all provisions regarding disclosure of remuneration are fulfilled.
- Ensure compliance with gender pay gap requirements and all legal and regulatory requirements relating to remuneration applicable to the Company.

Risk Management Committee

The Risk Management Committee is responsible for assisting the Board in providing independent oversight of the Company's risk management framework, including risk appetite, regulatory capital and the risk function and to make appropriate recommendations as appropriate to the Board.

The Committee membership consists of three Independent Non-Executive Directors and the CEO. The Chair of the Committee is an independent Non-Executive Director who reports to the Board meeting on the activities of the Committee. The main responsibilities of the Committee include:

- Making recommendations to the board on risk appetite in the context of business strategy taking account of the economic and financial environment.
- Reviewing the Company's current and forecast performance against risk appetite
- Advising the Board on risk aspects of proposed strategic transactions and make recommendations regarding the Own Risk and Solvency Assessment (ORSA).
- Review the risk management framework and approving significant risk policies.
- Consider, assess and approve the annual Risk Management and Compliance plans.
- Monitor and review the effectiveness of the Risk Management functions.
- Receive reports on the performance of first line management in mitigating risks and adhering to company policies.
- Oversee the internal model including methodology, assumptions, validation (internal and independent) and governance. Reviewing output of the internal model including the SCR and the Standard Formula SCR calculations.
- Review the adequacy and appropriateness of scenario and reverse stress tests.

Delegation of board authority and decision making

The board delegates some decision-making powers to ad hoc and standing board committees and the running of the Company to the CEO, who in turn delegates to executive management, some of whom establish management committees to assist them in the discharge of their function. The Board Committee and Management Committee memberships are set down in Board and Committee membership lists. Each Committee has a terms of reference and the performance of the Committee against its Terms of Reference is reviewed annually by the Head of Governance.

The board itself remains responsible for, and makes the final decisions on, areas delegated for consideration to a committee, except where the Board has delegated the decision to a board committee.

In addition to the above there are a variety of delegations of authority and protocols that operate across the Company.

LMIE Key Functions

The following sections set out a summary of the LMIE key control functions of Actuarial, Risk Management, Compliance and Internal Audit. Each function is headed by an individual who performs either a Senior Insurance Management Function or Significant Influence Function role.

Actuarial Function

The Actuarial Function is headed by the Chief Actuary. The authority, resources and independence of the Actuarial Function are detailed in section B.7.1 Governance of the Actuarial Function. The activities of the Actuarial function are reported to the Board or its sub committees, the Risk Management Committee or Audit Committee as appropriate.

The Actuarial function co-ordinates work carried out by the Actuarial, Capital Management, Underwriting, Exposure Management, Reinsurance and Finance teams in calculating technical provisions; providing an opinion on underwriting policy and reinsurance arrangements and contributing to the effective implementation of the risk management system.

Risk Management

The Risk Management function is headed by the Chief Risk Officer (CRO). The authority, resources and independence of the Risk Management Function are detailed in section B.3 Risk Management. The activities of the Risk Management function are reported to the Board or the Risk Management Committee as appropriate. The CRO reports directly to the CEO and the Chair of the Risk Management Committee who is an independent Non-Executive Director.

The Company’s approach to risk management centres on the principle that 'risk' is fundamental to the way in which the Company operates. It is embedded in the roles and responsibilities of individuals and committees throughout the Company’s first line functions. The Risk Management function role is primarily one of facilitator, developing and maintaining effective risk processes and systems. Risk Management offers appropriate challenge and oversight across the business, in order to provide second line assurance to the Board that risk taking remains consistent with its appetite and appropriately controlled.

Compliance Function

The Compliance function is led by the Head of Compliance. The authority, resources and independence of the Compliance Function are detailed in section B.5.2 Description of How the Compliance Function is implemented. The activities of the Compliance Function are reported to the Board and the Risk Management Committee or Audit Committee as appropriate.

The Compliance Function is responsible for assisting the business in ensuring compliance and monitors and oversees the business in this regard. The Compliance Function interprets, advises, monitors and reports on all regulatory matters for LSM.

Internal Audit

Internal Audit is an independent, objective assurance and consulting activity designed to help LSM accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of Risk Management, control and Governance processes.

The Head of the Internal Audit Function reports functionally to the Chair of the Audit Committee and administratively to General Counsel with direct access to the President and Managing Director. The authority, resources and independence of the Internal Audit Function are detailed in section B.6.3 Independence and Objectivity. The findings of the Internal Audit function are reported to the Audit Committee. The Chair of the Audit Committee is also the Chair of the Board and provides a summary of the Committee's activities to the Board.

Group Structure

The Company is a wholly-owned subsidiary of the Liberty Mutual insurance Group. Boston-based Liberty Mutual Insurance Group is a diversified global insurer and amongst the largest P&C insurers in the world based on gross written premium. The company also ranks in the Fortune 100 list of largest corporations. Liberty Mutual Insurance Group offers a wide range of insurance products and services through two strategic business units (SBU): Global Consumer Markets and Global Risk Solutions. The company is part of Global Risk Solutions.

Material changes in the system of governance

There have been no material changes in the system of governance during the period.

The governance structure is reviewed on an annual basis by the Head of Governance in order to ensure that it is effective and appropriate to the organisation. Included in that review is a review of board committee terms of reference to ensure that the board and committees are performing all of their duties and not acting outside of their authority. The annual effectiveness review ensures that the performance of the board, its committees and individual directors is formally evaluated.

In 2017 the composition of the board changed with the then Group Chief Underwriting Officer, already a board director, succeeding the President & Managing Director following the latter's resignation. Phil Hobbs was appointed as Deputy Managing Director to take a position on the board. In 2017, Liberty Mutual Group created Global Risk Solutions a new SBU within Liberty Mutual Group. The company is part of this SBU.

Remuneration Policy

Principles of the Remuneration Policy

The Company's remuneration policy applies to all employees and is based on the Liberty Mutual Group's compensation philosophy: to be competitive to market; to pay for performance; and to provide pay growth through promotional opportunities.

The policy describes the components of fixed and variable pay delivered to employees and demonstrates how good corporate governance and sound risk management prevent excessive risk taking which are the keystones of LMG's compensation philosophy.

The company is committed to ensuring that:

- Performance goals are clearly designed and communicated to all employees through a robust, but transparent, performance management process.
- Performance goals are aligned with the long term strategy of the business and the requirements of each individual employee.
- Customers and the insurance markets are protected from any negative impact associated with mismanagement of remuneration at any level of the organization.
- Incentive schemes are designed in such a way as to reward short and long term performance and ensure that employees are not incentivized to engage in inappropriate risk taking

The Remuneration Policy is overseen and approved by the Board Remuneration Committee and is reviewed annually to ensure alignment of pay practices with all relevant legislation and regulations.

The Remuneration Committee reviews and approve all elements of remuneration for subject employees and ensures that strong risk management practices are in place. It does this on an annual basis to ensure:

- A clear distinction between operating and control functions, to avoid conflicts of interest, both in the operating of the organization, as well as in terms of remuneration.
- Impartiality when it comes to executive pay.
- That final decisions regarding remuneration are taken in such a way as to protect the long-term interests of the company's stakeholders.

The Board Remuneration Committee may consult with key LMG and LSM corporate functions to ensure that incentive schemes do not expose the company to undue risk taking.

Share options, shares or variable components of remuneration

The Board remains responsible for ensuring that all remuneration components comply with the Remuneration Policy. Remuneration programs may be made available to company employees through and administered by one or more Liberty Mutual Group affiliates. Remuneration elements typically consist of the following categories:

Compensation	**Fixed/Variable**
Base Salary	Fixed
Benefits, perquisites and any allowances	Fixed/Variable
Annual Incentives	Variable
Long Term Incentives	Variable

Variable Remuneration

Variable remuneration – Short Term Performance

Short term performance is measured by achievement of individual (personal) objectives and business objectives measured over a one-year timeframe.

Business unit and overall business performance is measured against annually established targets which take account of the prior year performance, business plans and the operating environment.

Variable remuneration – Long Term Performance

Long term performance is generally measured by reference to profit against the business plan and growth against a defined peer group over a period of three financial years, commencing with the financial year in which the award is made. Long term performance for eligible employees is paid at the beginning of the fourth year following the cycle.

As an unlisted mutual holding company, LMIG has no share price that can be utilized or shares to be granted through stock options, so most long term incentive schemes operate as cash plans or through performance derived unit values for grants.

Supplementary pension schemes for members of the Board and other key function holders

The company's remuneration policy does not include any supplementary pension or early retirement schemes for members of the Board or other key function holders. The Company offers all staff the opportunity of making contributions into a defined contribution scheme, which the company will match up to a limit.

Material transactions during the reporting period

Material transactions include transactions with shareholders, with the parent entity, with persons who exercise a significant influence on the undertaking, and with members of the administrative, management or supervisory body. During the reporting period there were no material transactions.

SECTION B. 2 – Fit and Proper Requirements

Specific requirements concerning skills, knowledge and expertise applicable to the persons who effectively run the undertaking

LMIE requires all persons who perform key functions and are classified as Senior Insurance Managers, to fulfil the following requirements at all times:

a) Their professional qualifications. knowledge and experience are adequate to enable sound and prudent management (**fit**); and
b) They are of good repute and integrity (**proper**)."

The professional competence (**Fit**) is based on the person's experience, knowledge and professional qualifications, and also whether the person has demonstrated due skill, care, diligence and compliance with relevant standards in the area that he/she has been working in. Such a person should also be of good repute (**Proper**), and the assessment includes taking relevant references.

For the propriety assessment, the person in question must be assessed by LMIE to establish that they meet LMIE's minimum requirements for a 'Fit & Proper' person. These requirements include being able to demonstrate appropriate levels of probity, honesty, integrity, reputation, competence & capability, previous experience, knowledge of their area and financial soundness. In order to establish this, a person's credit & criminal record, professional qualifications (including Continuous Performance Development or equivalent training requirements) and supervisory experiences will be checked, alongside the recruitment process which will involve a CV review, interview and reference check.

In addition, every person carrying out a Senior Insurance Manager Function must be approved by the regulator to do so. Senior Insurance Managers must also comply with the PRA Conduct Standards and the FCA Conduct Rules.

Some requirements have been, or can be, assessed as 'collective knowledge', i.e. that not every member in the management body (or any function) are expected to possess expert knowledge, competence and experience within all areas of LMIE, but that they as a whole have the ability to provide sound and prudent management of the LMIE.

Process for assessing the fitness and propriety of the persons who effectively run the undertaking

The specific requirements outlined above will be reviewed using the Fit & Proper process adopted by LMIE. This evaluation will normally take place on an annual basis, or alternatively at any time that there is a material change such as internal promotion or move. The process is performed by the Compliance function and consists of the following:

- Assessment of the person's professional and formal qualifications, knowledge and relevant experience within the insurance sector, other financial sectors or other businesses and whether these are adequate to enable sound and prudent management; take account of the respective duties allocated to that person and, where relevant, the insurance, financial, accounting, actuarial and management skills of the person.

- Take account of the respective duties allocated to individual members to ensure appropriate diversity of qualifications, knowledge and relevant experience to ensure that the business is managed and overseen in a professional manner; and an assessment of that person's honesty and financial soundness based on evidence regarding their character, personal behaviour and business conduct including any criminal, financial and supervisory aspects relevant for the purpose of the assessment.

Evidence of the outcomes of this assessment must be retained. The records of this will be maintained in the following places (where appropriate); within the performance review, within the record of the recruitment process, within minutes of board meetings which record annual performance reviews, within training records & Continuous Performance Development, and within reports relating to annual board effectiveness reviews.

In the case of recruitment, HR will be responsible for recruiting appropriate staff.

The procedures outlined above ensure that all those holding controlled functions:

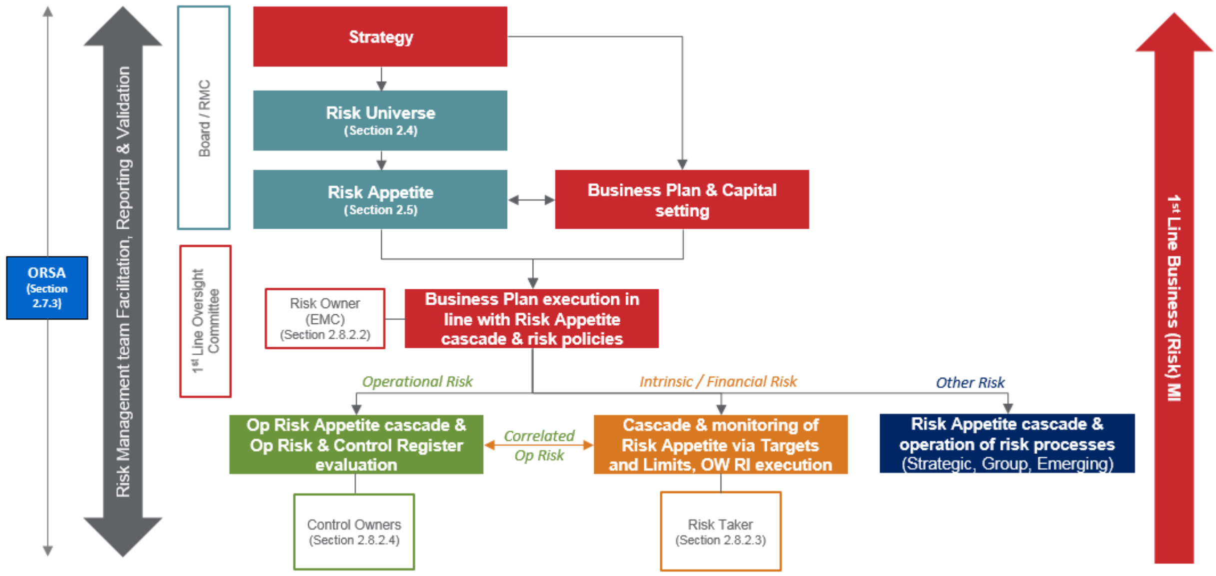
- Meet the requirements of the Regulators' 'fit and proper' test and follow its principles;
- Comply with the Statement of Responsibilities; and
- Report anything that could affect their ongoing suitability

SECTION B. 3 – Risk Management System including Own Risk and Solvency Assessment (ORSA)

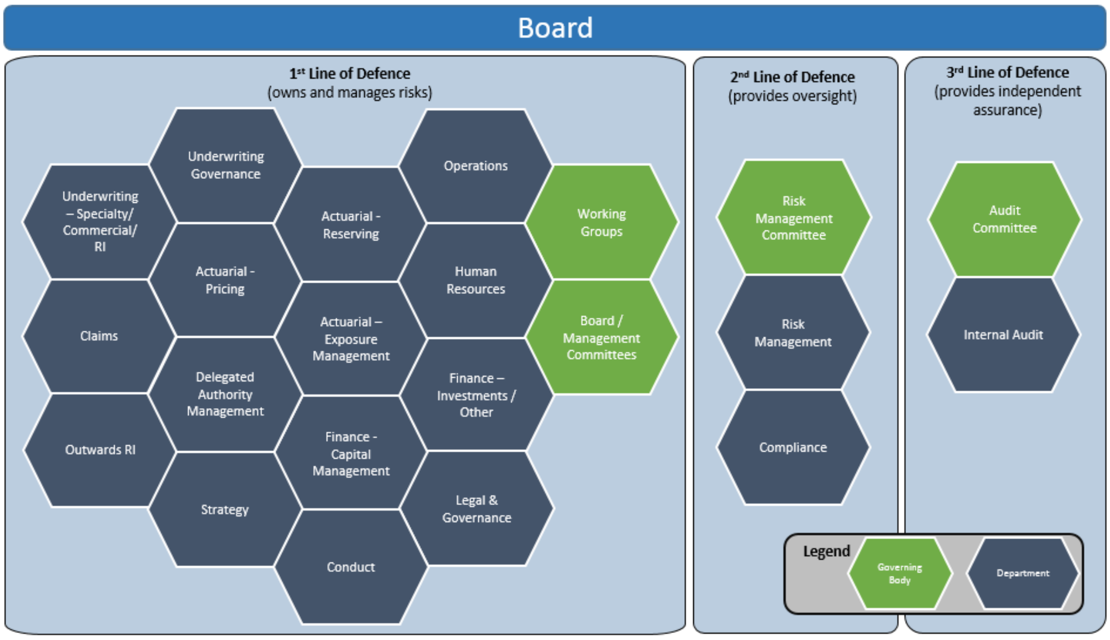
Description of the Risk Management System

The Risk Management and Internal Control Framework (RMF) is designed to enable LSM's operations to engage with risk in a controlled fashion consistent with the Board's appetite and available capital capacity in order to generate risk adjusted returns to the Group. It also sets LSM's approach to how we define risk and cascade risk appetite and the processes for ensuring the appropriate and timely identification, reporting, monitoring and management of risk and capital.

The following diagram outlines how risk management information and reporting is cascaded / escalated through the organisation:



LSM has adopted the Three Lines of Defence model for risk management and underpins this with clear roles and responsibilities for each of the departments and individuals involved in risk management across the organisation. Whilst Risk Management is a second line of defence function, there are key functions (Capital Management & Actuarial) who contribute to and have responsibilities within the risk management system.



The Risk Universe sets out the full scope of risk categories to which LSM could be exposed and forms the basis for their monitoring, measurement and reporting. Risk categories are defined as either intrinsic, operational, or other risks. Intrinsic risks are those risks with which LSM actively engages for the pursuit of profit, for example insurance (premium and reserve) risk. Intrinsic risks are managed via Board-approved risk appetites. Operational risks are those risks that LSM does not actively seek in order to generate profit, but nonetheless engages with to fulfil business objectives.

Risks are only accepted where they are aligned with the strategy and LSM has the appropriate expertise to manage them; risks that do not meet these criteria are not accepted. All risks accepted must have an expected reward that is commensurate with the risk, and contribute to ROE in the long term; LSM has no appetite for unrewarded risks.

The Risk Management team's main role is maintaining and facilitating the Risk Management Framework (RMF) to allow the business to take risks in a controlled fashion, including the periodic validation of first line activities and reporting. Other responsibilities include: supporting the business in cascading Risk Appetite and designing appropriate controls and Management Information (MI) to enable this to flow through to front line risk taking; managing the processes of Internal Model Validation, ORSA, Stress Testing and Reverse Stress Testing; Maintaining the Operational Risk & Control Register; and maintaining the Emerging Risk Log and facilitating the Emerging Risks process.

The Chief Risk Officer (CRO) prepares a quarterly report for inclusion at the Risk Management Committee meetings. The report details the risk profile summary, risk strategy, risk categories and position against risk appetites for each category of risk. The Risk Management Committee (RMC) is in place and reviews risks across core areas of the business including those areas responsible for cascading risk appetite and monitoring and managing risk levels across the risk universe. The RMC is responsible for the oversight of the all elements of the RMF, including consideration of forward-looking and horizon-scanning aspects of risk management. The RMC escalates material matters to the Board for review, discussion and challenge

The results of any risk management reviews/validation of first line risk management activities or reporting will also be outlined in the CRO reports; these will be conducted on a risk/rotational basis and external subject matter experts will be used where appropriate. The reporting is designed to provide assurance to the RMC and Board that the underlying processes are operating effectively, highlighting any exceptions and remedial actions taken during the period to date and provide a holistic view of risk levels across the full scope of risks faced by the organisation.

Implementation of the Risk Management System

RMF support the business planning and capital setting process which was initiated with a review of the proposed changes to Board-level risk appetites.

The Board Risk Appetite statements are reviewed at least annually through the Business Planning and Capital Setting process and may be revised at any point in the year in response to an actual or projected change in strategy or business planning, subject to Board approval.

The following diagram has been created to demonstrate how the annual Risk Appetite review process is incorporated into the overall strategy and business planning (including capital setting) cycle.

Own Risk and Solvency Assessment (ORSA)

Own Risk and Solvency Assessment Process

Risk Management is responsible for preparing the Own Risk and Solvency Assessment ("ORSA") report. This involves summarising the outcomes of the RMF, including the evolution of the risk profile and performance against risk appetites. Risk Management will also evaluate capital requirements as calculated by the Capital Management Team and Actuarial against actual levels of capital held by each entity.

Since 2017 LMIE projects its solvency needs for the three years coming based on the approved LSM business plan. It then tests the impact of certain scenarios on the projected solvency as a result of changes in projected profits, own funds and regulatory capital requirements. The details on the solvency projections are reported in the LMIE ORSA.

The drafting of the ORSA report will, however, require input from a number of areas around the business. This includes: Finance, Actuarial, Strategy, and Capital Management. Risk Management worked with these teams to obtain the relevant information for the ORSA report. A mapping of ORSA report inputs to the business area responsible is maintained at a granular level via the ORSA Record, which assists in providing a roadmap for future iterations of the ORSA report. Data inputs are subject to data quality standards as set out in the Data Policy.

The ORSA Record captures sources of information used in producing the ORSA report, as a significant part of the ORSA process involves collating and referencing risk management activities and business decisions that have taken place throughout the year.

The ORSA process and reports are ultimately owned by the LSM Board, which delegates some of its powers of challenge and review to its associated committees. The Risk Management Committee considers the ORSA reports in detail, provide comments and feedback to Risk Management and recommend the ORSA reports to the Board for final sign-off. The Strategic Planning and Analysis (SPA) Committee provides expert challenge and sign-off of the quantitative inputs to the ORSA which are prepared as part of the business planning and regulatory capital-setting process.

The ORSA is a process as well as a report. The ORSA includes both the economic capital position of LMIE and its regulatory capital position, by reference to the Solvency Capital Requirement (SCR) and the Minimum Capital Requirement (MCR), as at 31st December 2017.

ORSA reports for LMIE have been prepared for review by the RMC and submission to the relevant regulator at least annually. The ORSA reports are produced in line with the annual business planning exercise. Key elements of the ORSA, for e.g. the quarterly capital assessment forms part of the quarterly CRO report to the RMC and the Board.

As part of the ORSA embedding process, Risk Management, through the quarterly Chief Risk Officer Report to the RMC / Board, have presented some of the more fluid elements of the ORSA, such capital and solvency positions. This is summarised in the annual ORSA report reviewed and signed off by the Board.

We believe that our Internal Model (IM) calculation is more reflective of our own view of risk although we would highlight that it has not been subjected to validation and has known limitations. The Standard Formula is therefore used for the setting of regulatory capital via the Solvency Capital Requirement.

Ad hoc ORSA reports may be prepared at any time following material changes to each entity's business. These can be identified through a number of ORSA triggers, including but not limited to:

- Acquisitions/disposals;
- Change in risk profile leading to Standard Formula inappropriateness;
- Current trading/investment environment changes leading to a material actual or projected change in capital and solvency profile.

The evaluation of ORSA triggers is considered on a quarterly basis.

SECTION B. 4 – Internal Control System

Description of Internal Control System

LSM operate a centralised Operational Risk and Control Register, Magique, which is managed by Risk Management. Magique captures all operational risks and the controls used to mitigate them. Executive Operational Risk Owners are responsible for ensuring that the risks captured in Magique adequately cover the areas for which they have responsibility. In addition, they are required to assess whether the controls in these areas are appropriately designed to mitigate the risks to an acceptable level, as well as reporting any areas of concern the relevant oversight committee. Control owners are required to provide an assessment of the design and performance of each control which drives an overall RAG rating.

LSM maintains a Liberty Attestation Process (LAP) control framework that is designed to mitigate the risk of financial misstatement. All LAP controls are signed off on a monthly basis, requiring attestation from all Executive Risk Owners that they are satisfied that the key controls for their respective areas have been performed and operating as expected. In addition to this they have to attest that they are not aware of any changes in their control environment.

Description of how the Compliance Function is implemented

The Compliance function has in place a Policy and Plan that was approved by the Risk Management Committee in December 2017. The LSM Compliance Policy and Plan is in scope of the LSM Documentation standards and therefore requires approval on an annual basis or when significant changes are made to them.

No changes have been made to the LSM Compliance Policy or Plan outside of its normal annual review cycle.

The RMC has the following formal responsibilities in respect of LSM's Compliance Function:

- Review annually the risk management and internal control frameworks.
- Review risk management principles and policies, and management's efforts regarding the establishment of cultural awareness of risk and compliance with such policies, and consider approval of significant policies.
- Review reports on legal and regulatory compliance and development
- Review the adequacy of regulatory risk mitigation programmes

SECTION B. 5 – Internal Audit Function

Internal Audit Policy

The Internal Audit Policy provides a summarised view of the areas in which Internal Audit operates, its main objectives and the approach to reach these. This document contains the Internal Audit Mission Statement and Internal Audit Charter. The Internal Audit Policy is reviewed on an annual basis by the Head of Internal Audit and approved by the Audit Committee. There have been no significant changes to the policy during the 2017 reporting period.

Operations and Assurance

The primary role of Internal Audit is to help the Board of Directors protect the assets, reputation and sustainability of the organisation to ensure that Liberty Specialty Markets (LSM) and its customers prosper. Internal Audit serves the Audit Committee of the Board of Directors by:

- Delivery of the risk-based Internal Audit Plan
- Performing independent and objective evaluations of internal control processes
- Providing assurance as to the effectiveness of internal control processes
- Advising on the adequacy, effectiveness and efficiency of systems, controls and operation, and
- Helping the organisation to develop a systematic, disciplined approach to evaluate and improve the effectiveness of Risk Management, control and Governance processes

The primary responsibilities of Internal Audit apply to all relevant legal entities and operating units within LSM, as well as any joint ventures, business partnerships and outsourced arrangements and are to:

- Conduct independent reviews in accordance with standards for the professional practice of internal auditing codified by the Institute of Internal Audit (IIA) that evaluate:
    - The reliability of financial reporting
    - Safeguarding of assets
    - The efficiency and effectiveness of significant business control processes
    - Compliance with policies, procedures, laws and regulations

- Provide periodic reports of audit findings, together with agreed actions for Management to address internal control deficiencies

- Monitor the completion of Management Actions arising from audit findings

- To provide management with advice about the establishment of effective control systems and procedures as necessary / required

- Evaluate the potential for the occurrence of financial crime and how LSM manages fraud risk

- Co-ordinate work with Management to help identify key risks and controls from an understanding and on-going evaluation of LSM's business strategy, products and operational processes. Since it is not practical for Internal Audit to provide total assurance on all controls, resources will be focused on the delivery of the annual risk based Internal Audit Plan.

- Develop and deliver the risk-based Internal Audit Plan, which is evaluated annually across a three-year horizon. The LSM Risk Register identifies the risk universe and the top corporate risks ranked by likelihood and impact. The Internal Audit Plan is informed, but not determined, by the Risk Register and views of management. The audit plan is approved by the Audit Committee on an annual basis and reviewed / approved for changes on a quarterly basis The audit plan is designed to review controls in place to mitigate identified risks.

- As part of the creation of the Internal Audit Plan, the work of other assurance providers will be considered in order to maximise coverage and efficiency of the assurance opinion provided. To the extent that Internal Audit places reliance on the work performed by other assurance providers, the independence, objectivity, skill set, and scope of the work will be assessed to ensure that the assurance provided by Internal Audit meets the required professional standards.

- Liaise with External Audit, ensuring that wherever possible reliance is placed upon the work conducted by Internal Audit, and

- Internal Audit may receive additional requests from the Audit Committee, Board of Directors or Management to assist with reviewing internal control related issues or provide advice about the enhancement thereof. Internal Audit will conduct this work with due regard to its independence and objectivity and in line with IIA standards.

Independence and Objectivity

Internal Audit is an independent, objective assurance and consulting activity designed to help LSM accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of Risk Management, control and Governance processes.

Internal Audit reports functionally to the Chairman of the Audit Committee and administratively to the General Counsel. The Head of Internal Audit is directly responsible to the Audit Committee. In order to maintain independence, Internal Audit maintains direct access to the President & Managing Director and Chairman of the Audit Committee. Annually the Head of Internal Audit will meet in isolation with the Audit Committee to confirm that their independence and objectivity has not been impaired by undue influence.

In accordance with Article 271(2) of Delegated Regulation (EU) 2015/35 there are no persons within the Internal Audit function who assumes any responsibility for any other function or carry out activities that are inappropriate with respect to the nature, scale and complexity of the risks inherent in the business or poses a conflict of interest risk.

SECTION B. 6 – Actuarial Function

Governance of the Actuarial Function

The Actuarial Function performs the effective implementation of Article 48 of the SII directive 2009/138/EC.

The Actuarial Function reports to the LSM Board. The Chief Actuary reports to the President and Managing Director and is responsible for the work carried out in the Actuarial Function. The work relied upon by the Actuarial Function is carried out by many different departments within LSM with the Chief Actuary co-ordinating this work. The work is carried out by the Actuarial, Capital Management, Underwriting, Exposure Management, Reinsurance and Finance teams. The Chief Actuary escalates any matters to the Executive Committee and/or the LSM Board as appropriate.

The Chief Actuary is a Fellow of the Institute and Faculty of Actuaries, with over 10 year post qualification experience and subject to professional standards. As such the work carried out will meet the independence and free from influence requirement of Solvency II. The Actuarial Function consists of members of LSM's actuarial team. The Actuarial Function reports its recommendations to the LSM Board in order to maintain its independence.

The actuarial function is implemented through carrying out the following tasks:

- coordinate the calculation of technical provisions
- ensure the appropriateness of the methodologies and underlying models used as well as the assumptions made in the calculation of technical provisions
- assess the sufficiency and quality of the data used in the calculation of technical provisions
- compare best estimates against experience
- inform the administrative, management or supervisory body of the reliability and adequacy of the calculation of technical provisions, oversee the calculation of technical provisions in the cases set out in Article 82
- express an opinion on the overall underwriting policy
- express an opinion on the adequacy of reinsurance arrangements
- contribute to the effective implementation of the risk management system referred to in Article 44, in particular with respect to the risk modelling underlying the calculation of the capital requirements set out in Chapter VI, Sections 4 and 5 and to the assessment referred to in Article 45

Co-ordinating the calculation of Technical Provisions

In coordinating the calculation of technical provisions, the actuarial function will, at a minimum:

- Apply methodologies and procedures to assess the sufficiency of technical provisions and ensure that their calculation is consistent with the underlying principles
- Assess the uncertainty in the estimates.
- Apply judgment as appropriate, using any relevant information and the knowledge and expertise of the individuals involved
- Ensure that problems related to data quality are dealt with appropriately and that, where there are deficiencies in data quality, appropriate alternative methods are applied, subject to proportionality
- Ensure that risks are appropriately categorised into homogeneous risk groups
- Factor in relevant market information

- Track against previous estimates and justify any material differences
- Ensure appropriate allowance is made for embedded options and/or guarantees

With regard to technical provisions, the actuarial function will also:

- Ensure that methodologies and models used to calculate the technical provisions are appropriate, both in themselves and with regard to the specific lines of business they are applied to, taking into account the way the business is managed and the available data
- Ensure that management actions included in the calculation of technical provisions are objective, reasonable and verifiable
- Assess whether the IT systems used in the actuarial reserving procedures are adequate for that purpose
- Review revised best estimates against past best estimates and use the insights gleaned to improve the quality of current best estimates
- Compare observed values against the assumptions used in the calculation of technical provisions, in order to evaluate the appropriateness of the data used and the methods applied in their estimation
- Inform the board on the reliability and adequacy of the calculation of technical provisions, on the degree of uncertainty in the ultimate outcome and the circumstances that might lead to a significant deviation from the best estimate. It must clearly set out how it arrived at its opinion and explain any concerns it may have as to the sufficiency of technical provisions
- Determine when data is of insufficient quality to apply a standard actuarial method and a case-by-case approach should be followed instead. It must apply judgment to establish assumptions and safeguard the accuracy of the results

Providing an opinion on underwriting policy and reinsurance arrangements

The actuarial function's opinion on underwriting policy will include the following issues:

- Opinion on the overall business plan and sufficiency of premiums to cover future losses in expected and stressed scenarios
- Inclusion of the analysis and results of the actuarial function's assessment
- Consideration of any concerns that the actuarial function may have as to the adequacy of the business plan
- Outline recommendations to improve the plan and considerations of realistic alternatives to the current business plan
- Inclusion of an assessment of the consistency of the plan with the risk appetite
- Assessment of the consistency of the plan with the assumptions used in the estimation of the technical provisions
- Comment on the sufficiency of premium to cover any option or guarantees in the future
- Consideration of exposures to external and internal influences such as inflation, legal risk or changes in mix
- Consideration of anti-selection, of whether the underwriting process and controls used to manage the risk of anti-selection have been effective and of the likelihood of any anti-selection

The actuarial function's opinion on the adequacy of reinsurance arrangements will include:

- Opinion on the adequacy of the reinsurance arrangements
- Consideration of any concerns that the actuarial function may have as to the adequacy of the reinsurance arrangements, including recommendations for improvement and consideration of alternative structures.
- Assessment of consistency of the reinsurance arrangements with the risk appetite and underwriting policy
- Analysis of effectiveness of risk mitigation including impact on capital requirements and claims volatility
- Analysis of the adequacy of the reinsurance providers taking into account their credit standing
- Expected cover under stress scenarios in relation to underwriting policy.
- The adequacy of the calculation of technical provisions arising from reinsurance

The actuarial function will provide written reports to the board at least annually documenting the tasks undertaken and highlighting any shortcomings identified, and how such deficiencies could be remedied.

Contribution to the effective implementation of the risk management system

In respect of the contribution to the effective implementation of the risk management system, the actuarial function's opinion on underwriting policy will include discussion of the following issues:

- Outline the actuarial function's role in the wider risk management framework of LSM
- Highlight how the actuarial function contributes to the SCR calculations
- Highlight how the actuarial function contributes to the ORSA
- For LSM, indicate any inconsistencies between the technical provisions, the reinsurance arrangements, the overall underwriting policy and the related assumptions and values in the internal model

SECTION B. 7 – Outsourcing Arrangements

Description of the Outsourcing Policy

LMIE has in place an Outsourcing Policy that ensures that all material outsourcing arrangements within LMIE are assessed properly and managed effectively throughout their lifecycle from inception to termination. The rationale for LMIE's outsourcing is multi-faceted and depends upon a number of different considerations. From a business perspective, any outsourcing arrangement must be commercially viable, and a business case must be made before inception of the arrangement.

However, in addition to this, outsourcing arrangements must be evaluated to check that they do not refrain LMIE from meeting its regulatory requirements.

There are a number of checks which a service provider has to go through before inception to make sure that this is not the case:

- the provider must not adversely affect LSM's ability to comply with regulatory obligations or service to policyholders,
- they must not adversely affect the ability of the regulators to carry out their supervisory powers; and,
- they must be able to meet all applicable legal and regulatory requirements (potentially involving fitness and propriety assessments on individuals)

Furthermore, there are several other components making up the rationale for outsourcing arrangements including consideration as to whether the agreement will allow LMIE to monitor and control its operational risk exposure, reviewing any conflicts of interest and ensuring that LMIE has appropriate contingency arrangements in place to allow business continuity should a significant loss of service from the provider occur.

Regardless of jurisdiction, the service provider will be expected to go through the same thorough assessment as to their suitability to engage in an LMIE outsourcing arrangement. LMIE will ensure that any service provider located outside of the UK will undergo an assessment which is in keeping with LMIE's risk appetite. In the case of any provider located outside of the UK, further advice must be sought from the Compliance function and General Counsel.

Lastly, it should be noted that all outsourcing arrangements are subject to the thorough standards and processes regardless of whether or not the service provider is within or outside the LMIE group of companies or the Liberty Mutual Insurance Group (LMIG). Providers within the LMIE group of companies or the LMIG will be dealt with at an appropriate 'arms-length'.

Outsourcing Register

Outsourcing of any critical or important operational functions or activities and the jurisdiction in which the service providers of such functions or activities are located are as follows:

Description of services provided	Jurisdiction
Head Office IT Support	USA
Binder Management services	UK
Exposure Management services	UK
Investment Management	USA

SECTION B. 8 – Any Other Information

The governance structure and corporate governance framework in place to ensure that LMIE meets a good standard of governance, is assessed annually by the board. The last assessment was completed in January 2018 and included an externally facilitated board effectiveness review. The effectiveness review concluded the Board is operating effectively. There have been no material changes to the system of governance during the reporting period and the governance structure is deemed adequate for the company's risk profile.

During the reporting period there was no other material information to disclose regarding LMIE's system of governance.

SECTION C – RISK PROFILE

The LSM Risk Universe Policy sets out how LSM undertakes the categorisation of exposed risks. The business objectives of the Risk Universe policy are to ensure:

- All risks that could impact the on-going viability of the company are identified.
- Identified risks are measured and managed in the most appropriate method.
- All risks are owned by the most appropriate Executive and that each risk is reported through the correct committee or working group.

SECTION C. 1 – Underwriting Risk

Underwriting risk arises from two sources - adverse claims development (reserve risk) and inappropriate underwriting (premium risk).

a) Measures used to assess risks:

Reserve risk is managed by frequent reviews of estimates by the Claims department.

Underwriting risk is managed by having in place a clear underwriting philosophy, procedures and controls in relation to pricing, rigorous selection criteria and the diversification of risks. Reinsurance is another important method for the management of underwriting risk.

Material risk exposures are managed through the insurance risk appetites, which cover the following areas:

- Exposure management – modelled exposure limits by natural catastrophe/other peril region (set at the LSM level) and cascaded to an entity level.
- Delegated authorities – limits on the level of premium to be written through delegated authorities.
- Broker exposure – limits on the level of premium from individual brokers.
- Underwriting – underwriting guidelines over pricing, business plan premium, line size limits etc.
- Portfolio concentration – limits on line of business concentration, short- and long-tail premium concentration, and long-tail reserves.

Actual levels of risk vs. risk appetite measures are continually monitored, and LMIE may either revise approved business plans to stay within appetite, or if appropriate, revise appetite where it is reflective of a change in the external / internal environment.

b) Material risks that LMIE is exposed to:

LMIE exposures are predominantly in long tail liability business. Realistic Disaster Scenarios (“RDS”) are prepared by the Exposure Management Team and reviewed by the Exposure Management Working Group. These are reported as part of quarterly Chief Risk Officer reports to the Risk Management Committee.

c) Risk concentration:

Insurance risk concentration occurs due to the concentration of an insurance operation in a particular geographic area, industry or insurance peril. It may also occur as a result of a correlation between individual insured perils. The Company has the largest exposures by premiums and reserves to the SII Lines of Business General Liability, Fire and Other damage and Motor.

d) Risk mitigation:

LMIE manages insurance risks by monitoring and controlling the nature of an accumulation by geographic location of the risks in each line of business underwritten, the terms and conditions of the underwriting and the premiums the Company charges for taking on the risk. Some of the key risk mitigation strategy for insurance risk are pricing guidelines, review of large and unusual transactions and purchase of reinsurance.

In addition to managing insurance risk through the use of risk appetites and the purchase of reinsurance, there are specific operational processes related to the acceptance, measurement and management of insurance risk exposures. LMIE had no investment in Special Purpose Vehicles during the reporting period, hence no risk transfer took place. The overarching approach to the management of all operational risks is covered by the Operational Risk and Controls Policy (see operational risk below).

e) Process for monitoring the effectiveness of Insurance risk mitigation techniques:

The RMC actively monitors the effectiveness of the above risk mitigation techniques. Sensitivity testing over the business plan has been performed along with the results of stress tests over capital, and reverse stress tests, where the focus is on identifying potential management actions to mitigate the effect of threats to the viability of the business. The results of the stress tests indicate that LMIE's capital was adequate to absorb the calculated losses. We feed findings from the PRA annual General Insurance stress tests into our own stress and scenario testing. RSTs have been considered at an LSM level, impacts and management actions were determined at the entity level where applicable.

The LMIE Actuarial Function Opinions (dated 13th December 2017) on the Underwriting Policy and the Adequacy of Reinsurance Arrangements were presented to the LMIE Board concluded that:

1. The business plan is appropriate as premiums are sufficient to cover expected claims and expenses in aggregate; and

2. LMIE's outwards reinsurance strategy is in line with risk and underwriting policy.

SECTION C. 2 – Market Risk

Market risk refers to the risk of losses on LMIE's investment portfolio, arising from fluctuations in the market value of the underlying investments. LMIE has a clear investment strategy that is reviewed regularly, which has a number of objectives; to match investments to LMIE's claims liabilities in terms of both currency and duration, to hold a diversified portfolio of investment types and, within that overall context, to maximise the return generated at an agreed board level of risk.

Material risk exposures are managed through the market risk appetites, which are detailed in LSM's Risk Management and Internal Control Framework, which cover the following areas:

- Net interest rate risk – limit on interest rate-sensitivity measure as a proportion of total market risk.
- Credit and spread risk – limit on credit and spread-sensitivity measure as a proportion of total market risk.
- Credit and spread risk – minimum security ratings.
- Private equity risk – limit on private equity-sensitivity measure as a proportion of total market risk.
- Exchange rate risk – limit on exchange rate-sensitivity measure as a proportion of total market risk.
- Portfolio duration risk – limit on yield curve sensitivity measure.

Market risk remained broadly stable during 2017, which was in line with expectations given the conservative nature of the investment portfolio. The investment managers have been plotting a course that recognises the generally buoyant nature of the global economy and asset prices, while at the same time acknowledging the elevated state of political risk and the associated threats to continued growth. There were no material changes in market risk appetite and planned exposure in the 2018 plan.

In addition, there are permitted investments guidelines and exposure limits which are approved by the Investment Committee.

LMIE has a dedicated investments team responsible for the oversight of its invested assets. Assets are selected and held subject to the market risk and liquidity risk appetites set by the Board.

From a market risk perspective this involves the investment of assets within agreed boundaries of interest, spread, credit, private equity, exchange rate and portfolio duration risk. LMIE also maintains sufficient liquidity to meet liabilities as they fall due.

These procedures ensure that LMIE meets the requirements of the 'prudent person principle' set out in Article 132 of the Solvency II Directive, namely that:

- LMIE only invests in assets and instruments whose risks LMIE can properly identify, measure, monitor, manage, control and report;
- All assets, in particular those covering the Minimum Capital Requirement and the Solvency Capital Requirement, are invested in such a manner as to ensure the security, quality, liquidity and profitability of the portfolio as a whole.

The Investment Committee makes recommendations to the Board regarding the long term framework and short term investment strategy for the investment of LSM's assets. The Investment Committee's market outlook will help inform the risk appetites that are recommended to the Board.

The investment portfolios are managed by Liberty Mutual Investments. the investment management arm of LMG, in accordance with investment guidelines approved by the Board of LSM. There is a minimum credit rating requirement of BBB- and an average quality requirement of A. Limits are also established regarding issue, counterparty, asset type and rating concentrations. Securities must be readily marketable.

In addition to managing market and liquidity Risk through the use of risk appetites and monitoring the environment, there are specific operational processes related to the acceptance, measurement and management of Market and Liquidity Risk exposures.

The overarching approach to the management of all operational risks is covered by the Operational Risk and Controls Policy.

SECTION C. 3 – Credit Risk

Credit risk arises from the possibility of default by one or more counterparties. This risk is managed by carrying out appropriate due diligence on prospective counterparties, looking at the credit ratings of reinsurers and monitoring these over time (a minimum rating of ‘A’ is required for any of LMIE’s reinsurance programmes) and having in place a robust credit control system.

Material risk exposures are managed through the credit risk appetites, which cover the following areas:

- Reinsurers – acceptance of credit concentration risk as a result of using a single reinsurance provider.
- Reinsurers – minimum credit ratings.
- Delegated authorities and brokers – due diligence process.
- Delegated authorities – limits on exposure to individual coverholders.
- Brokers – limit on Value at Risk (VaR) measure.

The position against the Tier 2 risk appetites for the six areas above are monitored and reported on a quarterly basis to the RMC and Board. Tier 2 appetites are those that sit one level below the Core risk appetites which are set at the capital impact level.

LSM’s reinsurers (both LMG and non LMG) at the time of placing the risk (i.e. during the live period of the contract) were at least of S&P A- rating or collateralised and moreover, no RI programme would be considered by LSM with a carrier that was less than this rating, unless there was an appropriate level of security provided (e.g. collateral held) in line with LSM’s risk appetite LSM accepts that there will be a commensurate increase in its entity capital requirements (based on IM) due to the strategy of using LMG as a reinsurance provider and this is factored into the entity capital calculations. In addition, the RMC is provided quarterly information on ongoing Review of LMG Financial Statements and Rating; LMG’s own reinsurance programme; periodic reports from LMG to board that there are no material risks likely to impact LMG Credit Ratings and Underwriting and reserving risk exposures to LMG and related entities

In addition, the quarterly CRO report tracks the internal RI purchase as a % of GWP and LMG RI recoverable proportion to the available capital resources. This is in line with the PRA prudent person principle.

In addition to managing credit risk through the use of risk appetites and monitoring thereof, there are specific operational processes related to the acceptance, measurement and management of credit risk exposures. The overarching approach to the management of all operational risks is covered by the Operational Risk and Controls Policy (see below).

SECTION C. 4 – Liquidity Risk

Liquidity risk refers to the possibility of LMIE having insufficient cash available to settle claims and other liabilities as they fall due.

Liquidity risk exposures are managed through the liquidity risk appetites, which focus on ensuring that investment grade bonds exceed a specified percentage of the total investment portfolio. These appetites are managed alongside the market risk appetites, using the same procedures as outlined in the market risk section above. In particular, the liquidity risk appetites cover the following areas:

- Investment grade bonds – minimum weighting within the LMIE portfolio;
- Maintaining a diversified and appropriately liquid portfolio aimed at minimising the mismatch in cash flows between assets and net liabilities.

Both these appetites also help meet the requirements of the ‘prudent person principle’ set out in Article 132 of the Solvency II Directive and discussed in the market risk section.

LMIE calculates expected profit in future premium (EPIFP) using a method proposed by an EIOPA task force (based on QIS5). This methodology is broken down as follows:

1. Take into account the best estimate calculation already computed, i.e. net technical provisions as at 31.12.2017;
2. Calculate a new best estimate under the assumption that no more premiums are to be received in the future, and other assumptions would be unchanged.
3. The difference between the two best estimates for homogenous risk groups (taking into account positive differences only) is the EPIFP.

Capital, Liquidity and other contingency plans to mitigate risk and meet projected requirements over the planning period are deemed appropriate including under stressed conditions.

SECTION C. 5 – Operational Risk

Operational risk covers the risks arising from the failure of internal processes, people or systems, or from external events.

LMIE has limited appetite for operational risks, which are an unavoidable consequence of conducting business, and therefore seeks to manage and reduce exposure through an appropriate system of controls and an appropriate risk culture.

Conduct risk considerations covering customer focus and market integrity continued into 2017.

Outsourcing is also noted as a specific area of operational risk, which is managed through the Outsourcing Policy maintained by Compliance.

The primary mechanism for operational risk mitigation is controls, which are “a mechanism which supports the achievement of LSM's corporate objectives within its agreed appetite by either preventing or detecting issues. Controls are embedded into day to day business processes and mitigate business risks identified by the Risk Owners”.

Examples of the types of controls are:

- Preventative: E.g. underwriting guidelines/authorities, documented policies & procedures
- Detective: E.g. underwriting exception reports

The Risk Management team work with control owners across the organisation to ensure that all the controls they are responsible for are appropriately documented.

A key control is one that is important to LSM or one of the legal entities at an overall level (rather than being a control which is just important for a specific function within LSM, however it is expected that there will typically be at least 1 key control for each function and risk).

Incident reporting is an important aspect of effective operational risk management. LSM allocates incidents into two categories:

- Loss event
- Near miss

A loss event is defined as an incident or occurrence that has led to loss or damage to finances, property or reputation which could impact the organisation's ability to achieve its objectives.

A near miss is defined as an event or occurrence that could have but did not result in loss or damage to finances, property or reputation which could impact the organisation's ability to achieve its objectives.

Incidents will normally be identified by an individual or their manager/head of department as part of business as usual processes. In addition, the Risk Management team will validate completeness of incidents reported via an annual review of all controls for which the heads of departments are responsible.

The Risk Management team will enter all reported incidents into the risk management system, Magique, in order to keep track of historical losses or near misses. This will allow oversight into areas where the aggregation of multiple incidents may give risk to a review of the controls in place.

Magique is LSM's Operational risk register which captures risks and controls against those risks. LSM monitors these controls on a regular basis through Magique.

Magique is a new system and therefore reporting was developed further during 2016. During 2017, the RM team have targeted various stakeholders across the organisation to deliver training and guidance on Magique.

SECTION C. 6 – Other Material Risks

LMIE recognises that along with the benefits of being part of the LSM organisation, there is also a risk that matters could arise in one part of the organisation that negatively impact the other parts of the organisation. To mitigate the impact of this, the chairman of any committee reviewing risk information ensures that due attention is given to each legal entity. LSM recognises that this must continue even in times of stress to one entity.

LMIE’s Risk Universe also identifies sources of ‘other risk’ which are not fully captured via the quantitative risk modelling process:

- Strategic risk
- Group risk
- Emerging risk

Risk appetite statements for insurance risk incorporate a number of metrics that also cover elements of strategic risks (e.g. delegated authority arrangements and brokers); these are included and measured under insurance risk.

There are no quantitative risk appetite statements for group or strategic risk; they are either controlled to an acceptable level and/or monitoring measures are put in place, with reporting on an exceptions basis.

The identification of emerging risks is an important part of LMIE’s Risk Management process. Identification of emerging risks comes from multiple sources and processes across LSM, and all identified emerging risks are recorded by the Risk Management team in the Emerging Risk Inventory.

SECTION C. 7 – Any Other Information

LSM has two approaches to risk management defined by how the risk is categorised in the Risk Universe Policy. Intrinsic risks, which we actively seek, are managed through the use of risk appetites that are cascaded. Operational risks and other risks (strategic and group risk) for which LSM has limited appetite are managed through the Operational Risk & Internal Controls Policy and associated procedures.

Through the setting of risk appetites, the LMIE Board is acknowledging the existence of these risks and setting the boundary of risk taking that is acceptable given the current business environment. Risk Owners are empowered to manage their risks within the boundaries set.

As part of the 2017 LMIE ORSA, the sensitivity of profits, own funds, capital requirements and solvency ratio to changes in premiums, expenses and investment income was tested.

Stress and scenario testing specifically applied to the LMIE balance sheet was also completed during Q3 2017 in respect of the PRA’s General Insurance Stress Test (GIST) exercise. Following on from the results of the sensitivity tests and RSTs a series of contingency plans (CP) have been reviewed by the Board. These CPs will form part of the Recovery plan that is being developed with Compliance.

LMIE recognizes that along with the benefits of being part of the Liberty Mutual Group there is also a risk that matters could arise in one part of the organization that may negatively impact other parts of the organization.

SECTION D – VALUATION FOR SOLVENCY PURPOSES

Solvency II requires an economic market consistent approach to the valuation of assets and liabilities sheet in accordance with Article 75 of the Solvency II Directive 2009/138/EC. A number of assets and liabilities require different valuation methods to those used in the financial statements included in LMIE's financial statements for the year ended 31 December 2017. The financial statements are prepared under UK GAAP.

The functional currency of LMIE is US$, therefore Solvency II reporting is reported in US$.

The table below provides a summary of the Solvency II and the UK GAAP valuation of assets, based on the Solvency II balance sheet headings and the Solvency II approach to classifying assets and liabilities.

An explanation of the Solvency II valuation methods is provided in the following sections.

$(000)	Section Ref	2017 Solvency II	2017 Solvency II valuation adjustments	2017 Solvency II classification adjustments	2017 Statutory Accounts (UK GAAP)	2016 Solvency II	2016 Solvency II valuation adjustments	2016 Solvency II classification adjustments	2016 Statutory Accounts (UK GAAP)
Deferred Acquisition Costs	D.1.1	0	145,579	0	145,579	0	92,441	0	92,441
Deferred tax assets		0	0	0	0	0	0	0	0
Pension benefit surplus	D.1.2	8,117	0	0	8,117	4,333	0	0	4,333
Property, plant and equipment held for own use	D.1.3	0	9,825	0	9,825	0	11,231	0	11,231
Investments	D.1.4	2,286,214	(22)	83,120	2,369,312	2,280,968	(20)	86,357	2,367,305
Reinsurance recoverable	D.1.5	845,951	825,590	(469,711)	1,201,830	624,065	656,860	(311,058)	969,867
Deposits to cedants	D.1.6	32,497	0	0	32,497	29,415	0	0	29,415
Insurance and intermediaries receivables	D.1.7	136,362	0	469,711	606,073	132,684	0	311,058	443,742
Reinsurance receivables	D.1.8	26,884	0	0	26,884	56,803	0	0	56,803
Cash and Cash equivalents	D.1.9	275,890	0	(101,823)	174,067	194,638	0	(104,987)	89,651
Any other assets	D.1.10	29,276	0	18,703	47,979	13,152	0	18,630	31,782
Total Assets		**3,641,191**	**980,972**	**(0)**	**4,622,163**	**3,336,058**	**760,512**	**0**	**4,096,570**
Technical Provision	D.2	2,591,341	1,012,435	(186,872)	3,416,905	2,225,635	743,817	(186,418)	2,783,034
Deferred tax liabilities	D.3.1	13,610	(6,970)	0	6,640	13,390	1,611	(2)	14,999
Insurance & intermediaries payables	D.3.3	11,464	0	0	11,464	22,695	0	0	22,695
Reinsurance payables	D.3.2	0	0	186,872	186,872	0	0	166,466	166,466
Payables (trade, not insurance)	D.3.4	68,404	0	0	68,404	38,294	0	19,952	58,246
Any other liabilities, not elsewhere show	D.3.5	135	0	0	135	28,801	0	2	28,803
Total Liabilities		**2,684,955**	**1,005,465**	**0**	**3,690,420**	**2,328,815**	**745,428**	**0**	**3,074,243**
Excess of assets over liabilities		**956,236**	**(24,493)**	**(0)**	**931,743**	**1,007,243**	**15,084**	**0**	**1,022,327**

SECTION D. 1 – Assets (other than Technical Provisions)

D.1.1 Deferred acquisition costs

Acquisition costs represent commissions payable and other expenses related to the acquisition of insurance contract revenues written during the financial year. They are taken into consideration in the calculation of the Solvency II TP's, resulting in no separate asset or liability being recorded, hence, the value is Nil for Solvency II. Acquisition costs are deferred under UK GAAP and expensed in line with the earning of the corresponding premiums.

D.1.2 Pension benefit surplus

LMIE operates a defined contribution pension scheme for its employees. The assets of the scheme are held separately from those of LMIE in an independently administered entity.

In addition, LMIE has a closed defined benefit pension scheme which provides retirement benefits based upon final salary. The scheme is administered by a separate board of Trustees which is legally separate from the Company.

The pension surplus asset is recognised by LMIE and is valued in accordance with both IAS19 and FRS 102, the treatment is the same under both reporting standards and is consistent with the valuation under Solvency II.

FRS 102 allows the company to recognise any scheme surplus on its balance sheet provided that it is able to recover the surplus either through reduced contributions in the future or through refunds from the Scheme. As at 31 December 2017, the pension benefit surplus in respect of the defined benefit scheme under Solvency II valuation is $8.1m (2016: $4.3m).

The pension scheme assets and liabilities are reported on a net basis on the balance sheet.

D.1.3 Property, plant and equipment held for own use

Plant and equipment consist of computer equipment, fixture, fittings and office equipment. There is no active market or achievable exchange value for these assets, therefore under Solvency II the Company has elected to value the assets at Nil.

Under UK GAAP these are valued at cost less accumulated depreciation and accumulated impairment losses.

D.1.4 Investments

The Company generates cash from its underwriting, trading and financing activities and invests the surplus cash in financial investments. These include government bonds, corporate bonds, pooled investments funds and deposits with credit institutions.

Financial Investments and cash and cash equivalents

	2017 Solvency II $(000)	2017 Solvency II valuation and classification adjustments $(000)	2017 Statutory Accounts (UK GAAP) $(000)	2016 Solvency II $(000)	2016 Solvency II valuation and classification adjustments $(000)	2016 Statutory Accounts (UK GAAP) $(000)
Bonds						
Debt Securities and other fixed income securities	0	2,189,401	2,189,401	0	2,218,851	2,218,851
Government Bonds	638,752	(638,752)		915,574	(915,574)	0
Corporate Bonds	1,600,367	(1,600,367)		1,311,258	(1,311,258)	0
Collateralised securities	9,247	(9,247)		15,271	(15,271)	0
Collective Investments Undertakings	33,684	(16,856)	16,828	34,650	(21,157)	13,493
Deposits other than cash equivalents	4,135	158,942	163,077	4,216	130,754	134,970
Prepayments and Accrued Income	0	18,703	18,703	0	18,642	18,642
Total Investments	**2,286,185**	**101,824**	**2,388,009**	**2,280,969**	**104,987**	**2,385,956**
Cash and Cash Equivalents	275,890	(101,824)	174,066	194,638	(104,987)	89,651
Total Investments and Cash and Cash Equivalents	**2,562,075**	**0**	**2,562,075**	**2,475,607**	**0**	**2,475,607**

Solvency II requires the financial investments to be recognised in the Solvency II balance sheet using fair value principles, which includes adding the accrued interest to the value of the underlying investment. Under UK GAAP the valuation is also at fair value, but excludes the accrued interest which is recognised in any other assets.

Under Solvency II the financial investments are segregated as follows, determined by their market characteristics, using specific CIC identification codes:

- Bonds - to include both government and corporate bonds and collateralised securities. Valuation predominately in accordance with Level 2 as described below, with a small amount valued per Level 1 or Level 3.
- Collective Investment Undertakings – such as money market funds. Valued in accordance with Level 3 as described below.
- Deposits other than cash - deposits with maturity date greater than 90 days such as Letters of credit. Valued in accordance with Level 2 as described below.

The following valuation hierarchy is used:

Level 1 – quoted market prices in active markets for the same assets.

Level 2 – quoted market prices in active markets for similar assets.

Level 3 – alternative valuation methods using a variety of valuation techniques that include the use of discounted cash flow models and/or other mathematical models. The inputs from these models are derived from observable market data where possible, but where observable market data are not available, judgement is required to establish fair values.

Cash and cash equivalents comprise cash at banks and in hand and short term deposits with an original maturity date of 90 days or less.

All of the Company’s assets are measured at fair value therefore no measurement differences arise between Solvency II and UK GAAP.

D.1.5 Reinsurance recoverable

Reinsurance recoverable represent the reinsurer's share of technical provisions. Refer to Section D.2 for further details on technical provisions.

D.1.6 Deposits to cedants

Solvency II requires Deposits to cedants to be reported at fair value. Fair value is considered to be equivalent to the valuation under UK GAAP, which is based on amortised cost less any adjustment for expected default. Therefore, there are no valuation differences between Solvency II and UK GAAP.

D.1.7 Insurance and intermediaries receivables

The valuation of Insurance and intermediary receivables required by Solvency II is no different to that required for UK GAAP, therefore no valuation differences exist between the two.

As required by Solvency II, premiums receivable that are not yet due are re categorised to TP's for the Solvency II balance sheet. Overdue premium remain within 'insurance and intermediaries receivables'.

D.1.8 Reinsurance receivables

The valuation of Reinsurance receivables required by Solvency II is no different to that required by UK GAAP, therefore no valuation differences exist between the two.

D.1.9 Cash and cash equivalents

Cash and cash equivalents in the Solvency II balance sheet consist of deposits that can be exchanged for currency on demand at par value and are valued at their par value. There is therefore no difference between the value of cash and cash equivalents in the Solvency II balance and in the UK GAAP balance sheet. Cash and cash equivalents are classified differently between UK GAAP and Solvency II.

D.1.10 Any other assets

Any other assets are made up of the following items:

	2017 $(000)	2016 $(000)
Other Assets	6,360	
Prepaid Expenses	9,274	13,152
Intercompany Receivables	13,643	
Total	**29,277**	**13,152**

The valuation of any other assets required by Solvency II does not differ to that required by UK GAAP, therefore no valuation differences exist between the two.

SECTION D. 2 – Technical Provisions

Technical Provisions by Line of Business

The Company has applied appropriate methodologies and procedures to assess the sufficiency of the Technical Provisions (TPs) and the calculation is consistent with the requirements set out in Articles 76-86 of the SII Directives.

The TPs consist of the claims technical provision, the premium technical provision (which together form the best estimate liability) and the risk margin.

The TPs have been estimated at a homogeneous line of business level. The segmentation of lines are based on obligations that are managed together and which have similar characteristics. Direct General Liability and Direct Fire and Other Damage to Property business represent over 85% of the LMIE TPs. The Company has no exposure to Health or Life TPs, including Periodic Payment Orders.

A quantitative summary of the technical provisions by Solvency II Line of Business is provided in the table 1 below:

Table 1 Updated
Non-Life Technical Provisions by Best Estimate Liability and Risk Margin
$ '000s

Solvency II Class of Business	Gross BEL	Reinsurance Recoverable BEL	Risk Margin	Total TP
General liability - Direct	1,636,759	(453,438)	93,382	**1,276,703**
Fire and other damage to property - Direct	432,342	(219,467)	12,083	**224,958**
Credit and suretyship - Direct	91,778	(45,766)	9,202	**55,215**
Motor vehicle liability - Direct	65,727	(15,054)	2,827	**53,500**
All Other Lines	232,080	(112,226)	15,161	**135,015**
Total non-life obligation	**2,458,686**	**(845,951)**	**132,655**	**1,745,390**

General Liability Insurance

The General Liability Line makes up 73% of the SII TPs. The underlying reserves for direct casualty (general liability), financial lines (D&O and E&O), and professional lines contribute the majority of the TPs for this SII line. The UK segment of this line is impacted by the change in the Ogden Discount Rate from plus 2.5% to minus 0.75% as set by the Lord Chancellor in February 2017. The increase in the best estimate from before the Lord Chancellor announcement to the company's yearend 2017 estimate is an increase in net TPs of around $20m. The most material differences between Solvency II TP's and the GAAP reserves (net of future premium) for this line of business include:

- $93m for the Risk Margin which is highest for this line of business given the long-tailed nature of the underling business
- $30m for additional expense provisions and $25m for Events Not in the Data
- Offset by $83m for the profit in the Premium Provisions

Fire and Other Damage to Property

The Fire and Other Damage to Property Line makes up 13% of the SII TPs. The underlying reserves for direct property and energy lines contribute the majority of the TPs for this SII line. SII adjustments are applied to the GAAP reserves (net of future premium) to obtain the SII TPs. The most material adjustments that result in a small decrease in the TPs when compared to the GAAP reserves include:

- $26m for the profit in the Premium Provisions
- Offset by $12m for the Risk Margin and $8m of additional expense provisions

Credit and Suretyship

The Credit and Suretyship Line makes up 3% of the SII TPs. The underlying reserves for direct surety, financial, political and credit risk lines contribute the majority of the TPs for this SII line. SII adjustments are applied to the GAAP reserves (net of future premium) to obtain the SII TPs. The most material adjustments that result in a decrease in the TPs when compared to the GAAP reserves include:

- $85m for the profit in the Premium Provisions
- Offset by $9m for the Risk Margin and $5m of additional expense provisions

No other Solvency II Line of Business make up more than 5% of the Company's total SII TPs, and the aggregate change relative to the GAAP basis across all the other SII Lines is less than 1% of the total TPs.

Technical Provisions Valuation Methodology

The relevant Solvency II Directive and Delegated Acts text and associated guidance require the TPs to represent a best estimate plus a risk margin, where the best estimate corresponds to the probability-weighted average of future cash flows, taking account of the time value of money.

Technical Provisions valuation methodology of the Company groups the following key components:

- Claims Provisions: best estimate provisions that relate to earned exposure.
- Premium Provisions: best estimate provisions that relate to unearned exposure and include policies which are bound but not yet incepted at the valuation date.
- Risk Margin: additional provision to bring the above best estimate to the level required to transfer the obligations to a third part undertaking.

The Claims and Premium Provisions would include allowance for future premiums, expenses and Events Not In Data (ENIDs). Payment projections are then derived for all the future cash in-flows and out-flows.

Claims Provisions

The gross claims provisions are calculated separately for attritional, large and catastrophe claims with no margin allowance for prudence. The methodology is the same as that used to estimate the Actuarial Function's view of the UK GAAP reserves (with no margin for prudence), before allowance for ENIDs, expenses and discounting.

The methods used to estimate the Claims Provisions are deterministic claims-based and exposure-based methods and are in line with best practice non-life actuarial techniques, such as the Chain Ladder and Bornhuetter-Ferguson methods.

The process for estimating the reinsurance recoveries follows a netting-down approach of the gross claims provisions. The gross attritional, large and catastrophe splits do not apply. Instead, reinsurance claims provisions are estimated for Proportional and Non-Proportional outwards reinsurance treaties separately.

Reinsurance bad debt (counterparty default) is taken into account using the credit rating of each individual reinsurer and their ability to pay.

Premium Provisions

Premium provisions relate to claim events occurring after the valuation date and during the remaining in-force coverage of policies.

The ultimate premium by year of account is broken down into the following components:

- Earned (included in claims provisions)
- Unearned incepted
- Unincepted but legally bound (BBNI)
- Unbound

The analysis and split of premium between unearned incepted, BBNI and unbound is carried out at the policy level. Earning patterns are calculated by policy taking into account inception and expiry date. The inception date of a policy is used to determine whether it is incepted or not, except for delegated authorities where the underlying inception profile is used. The commitment date recorded on source underwriting systems is used to determine whether a policy is bound or not except for delegated authorities – see Definition of an Existing Contract.

The ultimate premium that is unbound is not included in the Technical Provisions. The gross Premium Provisions are calculated separately for unearned incepted and BBNI risks:

- Unearned Incepted claims are calculated as the unearned incepted premium multiplied by the underwriting year prior loss ratio from the latest actuarial reserve analysis.
- BBNI claims are calculated as the BBNI premium multiplied by the business plan loss ratio for each line of business.

Definition of an Existing Contract

Under SII all existing contracts are included in the valuation as opposed to incepted contracts under UK GAAP Technical Provisions. Contracts are recognised as existing once LMIE becomes a party to the contract or when the contract between undertaking and policyholder is legally formalised. The source underwriting systems record the commitment date, written date and the inception date of the contract.

For binder and delegated authority business this is assessed on a “look through” basis with the boundaries of the actual underlying contracts of insurance being tested. The Company’s approach is to include one months’ worth of new business of underlying inceptions for each delegated authority.

Outwards Reinsurance

The key principle followed for LMIE reinsurance premium provisions is to ensure the best estimate underlying the technical provisions is consistent with the inwards policies (The Principle of Correspondence). In addition, for existing reinsurance contracts, any contractually bound contracts are also included in full with no consideration to the future inwards business.

The SII valuation assumes that future reinsurance purchases will be made in line with the current business plan (a future management action) and that an equivalent reinsurance spend and benefit will be available to cover unearned and BBNI business.

The future claims inflow on unearned and BBNI business is adjusted for the probability of counterparty default. The methodology takes into account both the probability of default and the loss given default.

Future Premium

The estimation of the TPs allows for claims cashflows to be offset by premiums receivable (gross of reinsurance) and premiums payable (on outwards reinsurance) that are expected to occur in the future but are not overdue at the valuation date.

The premium receivable and payable for Claims Provisions and Premium Provisions are valued consistently with the UK GAAP basis other than the additional allowance for BBNI business. Therefore, the premium receivable and payable are both larger than the GAAP basis.

Any potential lapses in premiums are taken account in the cashflow analysis.

Expenses

SII requires the best estimate to include all cashflows arising from expenses that will be incurred servicing the policies over their lifetime.

Allocated loss adjustment expenses (“ALAE”) figures are included within the claims numbers used for premium provisions and claims provisions.

Expenses have been split for analysis purposes into acquisition costs, unallocated loss adjustment expenses (“ULAE”) and other additional expenses including Investment Management Expenses.

- **Acquisition Costs:** Gross and reinsurance acquisition costs by year of account and line of business are supplied from the underwriting source systems.
- **ULAE:** ULAE provision is estimated using the same methodology as the UK GAAP reserves.
- **Investment Management Expenses and Other Expenses:** The actual and budgeted investment management expenses incurred by LMIE on a per annum basis are used as the basis to estimate the total investment management expense provision for the run-off of the current liabilities, assuming a future rate of management expense inflation and that the expenses will reduce in line with the managed assets.

Other expenses have been derived using the Company’s expense model to derive an estimate of the headcount and associated cost for each department which supports the legally bound contracts over the life of their future cashflows.

Events not in Data (ENIDs)

SII requires that the best estimate technical provisions be a probability weighted average of all possible future outcomes.

The methods used such as Chain Ladder and Bornhuetter-Ferguson are based to a degree on historical information and therefore do not allow for all future outcomes.

ENIDs are those events of high severity but very low frequency that are missing from our historical data sets and exposure information. An example of an ENID would be a latent claim such as the health hazard losses from asbestos and pollution that emerged in the 1980's.

By their nature any methodology applied will be subjective for ENIDs. The Company has taken the following approach:

- An uplift factor is obtained by comparing the current claims best estimate to the best estimate excluding the observations beyond the 1 in 200-year point from internal analysis of reserve risk and underwriting risk.
- For claims relating to earned business the reserving risk distribution is used.
- For claims relating to premium provisions the attritional and large combined underwriting distribution is used.
- No uplift has been applied to catastrophe claims.
- The uplift factor has been applied to the undiscounted claims reserves.
- A minimum uplift is applied by line of business.

Cashflows and Discounting

The best estimate technical provisions under SII take into account the time-value of money using the relevant risk-free interest rate term structure. This is undertaken for each material currency.

Claims and premium provisions are converted to deterministic cash flows by application of quarterly payment patterns. Ceded cash flows are assumed to be equal to those applied to the gross with a quarter lag.

The term structures used for discounting have been supplied by EIOPA for each currency. The Company has relied upon EIOPA to prepare these yield curves.

Risk Margin

The Risk Margin is calculated using a cost of capital approach. The cost of capital approach requires the Risk Margin to be calculated by determining the cost of providing the Solvency Capital Requirement (SCR) necessary to support the Technical Provisions over their lifetime. Therefore, the approach requires the Technical Provisions and SCR to be calculated for each future year until the business is fully run off.

The claims run-off pattern applied to the Technical Provisions and SCR for each future year until the business is run off is non-linear using a risk based approach.

A cost of capital rate of 6% per annum is used as the cost of holding the projected SCR in the future.

The Risk Margin is calculated for the whole business and allocated to SII lines of business.

Options and Guarantees

The Company has no material options and guarantees that require explicit consideration or adjustment within the TPs.

Comparison of GAAP and SII Valuation of Technical Provisions

The table below presents a comparison of the Company's UK GAAP provisions to those on a SII basis as at 31 December 2017. Note that the Company's UK GAAP reserve estimates contain margins when compared with the SII best estimate.

Comparison of gross and net technical provisions estimates as at 31 December 2017

($000s, applicable period-end balance sheet rates)

	Q4 2017		
	SII Basis [A]	UK GAAP [B]	UK GAAP vs. SII Basis [C] = [B] - [A]
Gross of Reinsurance			
Claims reserve (incl Risk Margin)	(3,228,713)	(2,436,527)	792,186
ULAE (and other SII expenses)	(84,798)	(32,822)	51,976
UPR (Net of DAC)	-	(695,905)	(695,905)
Future Premium Cashflows	722,169	239,841	(482,328)
Gross TP	**(2,591,341)**	**(2,925,413)**	**(334,071)**
Reinsurance			
Claims reserve	1,131,459	920,332	(211,127)
Bad Debt	(3,936)	(3,936)	-
UPR (Net of RI DAC)	-	179,362	179,362
Future Premium Cashflows	(281,572)	(186,872)	94,700
Reinsurance TP	**845,951**	**908,886**	**62,935**
Net GAAP / SII TP (including future premium)	**(1,745,390)**	**(2,016,526)**	**(271,136)**

The material differences from moving from a UK GAAP to SII basis are:

- An increase in gross and reinsurance claims reserves as a result of moving from the GAAP concept of holding a UPR to the Premium Provisions concept in SII.
- An increase in gross claims reserves as a result of holding a Risk Margin under SII being greater than the removal of the GAAP reserve margin at this valuation date.

- Allowance for ENIDs and discounting for the time value of future cashflows partially offsetting each other at this valuation date.
- An increase in gross pipeline premium and reinsurance pipeline premiums as a result of the wider definition in SII to consider all existing, legally bound, contracts as opposed to incepted contracts under UK GAAP.
- An increase in expense provisions under SII to cover the wider definition of all expenses that will be incurred servicing the in-force policies over their lifetime.

Changes in Technical Provisions from prior Reporting Period

There have been no material changes made to the relevant assumptions used compared to the previous reporting period, except in the case of the Ogden Discount Rate assumption following the Ministry of Justice announcement in September 2017 that “if a single rate were set today under the new approach the real rate might fall within the range of 0% to 1%”.

There have been no material changes in methods to estimate the TPs from 2016 to 2017.

Assumptions and Use of Expert Judgement:

Future Management Actions within the Technical Provisions

A key assumption within the valuation of the reinsurance Technical Provisions is that the reinsurance programmes will be renewed with similar terms to those currently in place and that the Company will continue to write a similar book of gross business in line with the 2017 business plan. Deviations from this could have a material impact on the technical provisions required.

No other future management actions were explicitly allowed for in the Technical Provisions.

Reserving Methods

The methods used are in line with best practice non-life actuarial techniques such as Chain-Ladder method or Bornhuetter-Ferguson method.

Assumption Selection

All modelling assumptions are documented by the Actuarial Function in line with UK professional standards. The assumptions used are appropriate for the work carried out by the Actuarial Function.

Consistency with Financial Market Information

Assumptions:

- **Future Inflation:** Other than in the choice of the expected loss ratios, the Company’s reserving methods do not make an explicit assumption for future claims inflation. Where historical development profiles are extrapolated into the future via the Chain Ladder method, these projection methods include an implicit assumption that historical trends in inflation will persist in the future.

- **Currency Rates of Exchange:** Future exchange rates are assumed to be equal to the current level.
- **Reserving Cycle:** Where possible allowance has been made for the reserving cycle.

Expert Judgement

The use of Expert Judgement is documented by the Actuarial Function. All modelling selections contain judgement and these reflect the nature of the insurance obligations, the material risks faced by the insurer and the purpose of that work.

Uncertainty associated with the Technical Provisions

There is a wide range of possible outcomes in assessing the Company's TPs. The TPs represent a best estimate plus a risk margin, where the best estimate corresponds to the probability-weighted average of future cash flows, taking account of the time value of money. Some of the key uncertainties in valuing the TPs include:

1. For all actuarial projections there are a range of possible results. The final outcome will depend on the actual development of claims. All actuarial techniques use the historic data to predict the likely development by line of business. Unforeseen changes may affect the suitability of that data and would be expected to have an impact on the accuracy of the results. Such issues would include unexpected claims inflation, changes in legislation and the emergence of new types of claim.

2. Over the years the Company has expanded into new areas of business or changed the makeup of accounts. These lines of business may not have fully developed history on which to base projections. For these lines we have typically selected market benchmarks. The accuracy of the results is dependent on the suitability of benchmarks used. The assessment of the appropriateness of these benchmarks may not be possible for some time. Additionally, long tail lines of business may still not be fully developed so the results will be dependent on the tail selected.

3. Actuarial techniques rely on the appropriateness of the historic data. The final outcome may rely on the development of individual claims reserves. It may take a considerable length of time for these claims to settle.

4. Some underwriting lines of business have results that are dependent on the performance of certain key contracts, either through large exposures or through a large volume of business being written under the contract, relative to the size of the account.

5. Estimates make no provision for potential future claims arising from new latent caused or types of claim not as yet materially recognised in the historical experience unless identified through our discussions with LMIE underwriters, claims specialists or other senior management.

6. Some of the Company's casualty lines of business are exposed to catastrophe events. Some lines are also exposed to natural catastrophes. For these lines the ultimate claims are highly dependent on the future incidence of these events.

7. No provision has been made in our estimates for post balance sheet events occurring after 31st December 2017.

8. A large part of the Company's TPs comprise long-tailed Casualty and Financial Institutions exposures which are inherently more uncertain in their nature and particularly sensitive to the effects of the global financial crisis and subsequent economic downturn since 2008.

9. Loss Ratios used in projections may be subject to an additional degree of uncertainty in the current soft market conditions and following the significant growth of the Company's book since 2002.

10. Another feature of long-tailed casualty lines in a soft market is that they tend to exhibit a "reserving cycle" in that, for a number of reasons, there is strong empirical evidence suggesting claims development patterns show a tendency to lengthen.

11. The Company writes material and increasing amounts of business through coverholders and facilities. This can lead to lengthened development in lines which are a combination of open market and binding authority business as the proportion of binding authority business increases.

12. The outward treaty reinsurance programmes are denominated predominantly in US dollars. An uncertainty arises in the estimation of recoveries due to movements in foreign exchange rates before the losses are settled in a non-settlement currency.

13. There is uncertainty in the market around case estimates as a percentage of incurred claims reducing, which would suggest case estimates are becoming weaker.

14. There is uncertainty in the market that more recent years of Casualty business will perform relatively better than older years after allowing for rate movements and inflation due to improvements in underwriting.

15. Technical Provisions are impacted by economic variables. The general methods used by the Actuarial Function implicitly allow for inflation by assuming the weighted average rate of past inflation will occur in the future. If future inflation was above the past long term rate then the undiscounted technical provisions would increase.

16. Quantification of ENIDs are inherently difficult to value. The Actuarial Function has had to determine what is not included within its original best estimate and to determine what the best estimate would be for the very low frequency, high severity ENIDs. ENIDs are challenging to validate due to the absence of historical observations by their nature in the LMIE dataset.

17. The timing of future payments is always uncertain and can greatly be affected by many variables. The timing of the Company's cashflows and the yield curves by currency provided by EIOPA impact the discounting credit within the TPs.

18. The uncertainty associated with the Premium Provisions is greater than the earned reserves as a result a greater impact future economic and market conditions and as a result of the potential for insured catastrophes.

19. There have been a number of recent court judgement and changes in the legal claims environments relating to personal injury claims in the UK that increases the uncertainty

surrounding the size of future claims. For example, the latest consultation around the Ogden Discount Rate applicable to lump sum damages invested by claimants is that this should be reviewed at least every three years.

Matching Adjustment

The matching adjustment referred to in Article 77b of Directive 2009/138/EC has not been applied by the Company. Therefore, no quantification is provided of the impact of a change to zero of the matching adjustment on that undertaking's financial position, including on the amount of technical provisions.

Volatility Adjustment

The volatility adjustment referred to in Article 77d of Directive 2009/138/EC has not been used by the Company. Therefore, no quantification is provided of the impact of a change to zero of the volatility adjustment on that undertaking's financial position, including on the amount of technical provisions.

Transitional Risk free Interest Rate-term Structure

The transitional risk-free interest rate-term structure referred to Article 308c of Directive 2009/138/EC has not been applied by the Company. Therefore, no quantification is provided of the impact of not applying the transitional measure on the undertaking's financial position, including on the amount of technical provisions.

Transitional Deduction

The transitional deduction referred to as Article 308d of Directive 2009/138/EC has not been applied by the Company. Therefore, no quantification is provided of the impact of not applying the deduction measure on the undertaking's financial position, including on the amount of technical provisions.

SECTION D. 3 – Other Liabilities (other than Technical Provisions)

D.3.1 Deferred tax liabilities

Deferred tax is calculated on the difference between the values ascribed to certain assets and liabilities recognised and valued for Solvency II purposes and the values ascribed to assets and liabilities as recognised and valued for tax purposes. The valuation of deferred tax assets and liabilities is based on the principles prescribed by Section 29 of FRS 102, whereby a deferred tax asset or liability can be recognised on temporary difference where it is probable that they will reverse in future periods.

Deferred tax is measured using tax rates and laws that have been enacted or substantively enacted at the balance sheet date and that are expected to apply to the reversal of the timing difference.

For Deferred tax liability under UK GAAP, please refer to Note 7 of the LMIE 2017 Financial Statements. SII adjustments are applied in areas such as provision for risk margin and discounting, resulting in an adjusted deferred tax amount under Solvency II.

D.3.2 Reinsurance payables

Solvency II requires reinsurance payables to be reported at fair value, the UK GAAP reinsurance payables are held at amortised cost and are considered to be a close approximation to fair value. Therefore, there are no valuation differences between Solvency II and UK GAAP.

D.3.3 Insurance and intermediaries payables

The valuation of Insurance and intermediary payables required by Solvency II does not differ to that required by UK GAAP, therefore no valuation differences exist between the two.

D.3.4 Payables (trade, not insurance)

The valuation of Payables (trade, not insurance) required by Solvency II does not differ to that required by UK GAAP, therefore no valuation differences exist between the two.

D.3.5 Any other liabilities not elsewhere shown

Any other liabilities are made up of the following items:

	2017 $(000)	2016 $(000)
Accounts Payable		(5,765)
Accrual General		24,419
Other liabilities	135	10,147
Total	**135**	**28,801**

The valuation of any other liabilities required by Solvency II does not differ to that required by UK GAAP, therefore no valuation differences exist between the two.

SECTION D. 4 – Alternative Methods for Valuation

There are no material assets or liabilities for which alternative valuation methods are used, other than the valuation of certain financial investments as described in section D.1.4 (Level 3).

SECTION D. 5 – Any Other Information

LMIE do not have any other material information to be disclosed.

SECTION E – CAPITAL MANAGEMENT

SECTION E. 1 – Own Funds

Objective, Policies and Processes for managing Own Funds

The purpose of own funds management is to maintain, at all times, sufficient own funds to cover the Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR) with an appropriate prudence margin. The Company holds quarterly board meetings, in which the proportion of own funds over SCR and MCR are reviewed.

As part of own funds management, LMIE prepares ongoing annual projections and reviews the structure of own funds and future requirements. The business plan, which forms the base of the ORSA, contains a three-year projection of funding requirements and this helps focus actions for future funding.

The solvency monitoring plan is set out below which will apply to both the Standard Formula (SF) and the Internal Model (IM) (one-year) calculations. LMIE currently uses the standard formula (SF) to calculate capital requirements as its internal model (IM) has not yet been approved. However, the internal model is used alongside the SF to help LMIE understand and manage risks to its business, and challenge SF outputs where appropriate.

>125% of the SF and IM (one-year) calculations	• Quarterly SCR updates in line with the SF Policy and IM update cycle • Potential to pay dividends if solvency exceeds 125% on both SF and IM basis • Board decision subject to degree of excess capital, plan and volatility
115% - 125% of the SF and IM (one-year) calculations	• No dividends will be paid • Quarterly SCR updates in line with the SF Policy and IM update cycle • Monitor risk of solvency deteriorating in the following three months
110% - 115% of the SF and IM (one-year) calculations	• No dividends will be paid • Full quarterly re-run of the SCR • Capital contingency planning activity • Monitor risk of solvency deteriorating in the following three months
100% - 110% of the SF and IM (one-year) calculations	• No dividends will be paid • Regular communication to PRA • Board approval of capital remediation plan (the remediation plan shall include an allowance for scenarios that are expected to self-correct, for example an unforeseen, sharp and steep fall in financial markets) • Action: restore capital to an appropriate level determined by the Board over a period of at least 6 months
SF SCR - MCR	• 2 months to submit a recovery plan • 6 months to restore SCR cover (capital injection or reduce risk profile)
MCR (between 25% and 45% of SCR)	• 3 months to restore MCR cover • Capital injection or reduce risk profile

LMIE believe the selected margins above, both the IM one-year capital and the SF calculations are appropriate for the following reasons:

- They reflect a sufficient margin for the LMIE business model and risk profile, supported by a solvency monitoring plan (set out below);

- LMIE policyholders benefit from a guarantee from our parent company, which is as a consequence reflected in the credit rating of LMIE; and
- LMIE parent company has demonstrated a record of recapitalising LMIE, the directors believe that there is no reason to expect that LMIE would not be recapitalised in the event that this is what is required in the future.

Business plans are prepared over a three-year time line. LMIE do not anticipate changes in future business plans that will significantly alter future capital requirements. However, as the impact of Brexit is felt there remains the possibility that capital requirements, and therefore solvency ratios, will be affected by any structural adjustments that are necessary, as preparations are made to leave the EU.

Structure, Amount and Quality of Own funds by Tier

Tier 1 Unrestricted

Capital Structure	2017 $(000)	2016 $(000)
Share Capital	290,225	290,225
Share Premium	100,000	100,000
Reconciliation Reserve	566,011	617,020
Available and Eligible Own Funds	**956,236**	**1,007,245**
SCR	749,200	710,000
MCR	264,211	245,900
SCR Coverage Ratio	**128%**	**142%**
MCR Coverage Ratio	**362%**	**410%**

Solvency II distinguishes between basic Own Funds and ancillary Own Funds. LMIE's eligible Own Funds are all basic Own Funds.

LMIE's ordinary share capital and related share premium are classified as Tier 1 unrestricted capital and are available to meet the SCR and MCR.

LMIE is required to satisfy local solvency requirements in certain non-EU jurisdictions. In some cases, this requires holding funds in local custody accounts, but these funds are considered to be fungible and not ring-fenced and immaterial.

The Reconciliation Reserve is made up of the remainder of the excess of assets over liabilities and classified as Tier 1 capital in accordance with the Solvency II regulations:

Reconciliation Reserve

	2017 $(000)	2016 $(000)
Excess of assets over liabilities	956,236	1,007,245
Other basic own fund items - Ordinary share capital (gross of own shares)	(290,225)	(290,225)
Other basic own fund items - Share premium account related to ordinary share capital	(100,000)	(100,000)
Reconciliation reserve	**566,011**	**617,020**

Own Funds changes in the period

The changes to Own Funds during the reporting period are:

	2017 $(000)	2016 $(000)
Own Funds at 1 January	**1,007,245**	**838,902**
Total comprehensive (loss)/income for the year as reported in the Company's financial statements	(90,501)	38,610
Issue of ordinary shares	-	100,000
Solvency II valuation adjustment movements:		
Financial Investments	1,323	(11,107)
Technical Provisions	44,295	(6,348)
Movement in discounting	30,009	(17,069)
Movement in Risk Margin	(23,415)	24,204
Movement in Equalisation Reserve	-	41,386
Deferred tax	(12,720)	(1,333)
Own Funds at 31 December	**956,236**	**1,007,245**

Material Differences between Financial Statement Equity and SII Excess of Assets over Liabilities

LMIE prepare its financial statements in compliance with FRS 102 and FRS 103, being the applicable UK GAAP accounting standards, and in accordance with the provisions of Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (The Regulations) relating to insurance companies.

The following table provides an explanation of the differences between UK GAAP equity and the Solvency II excess of assets over liabilities:

	2017 $(000)	2016 $(000)
UK GAAP equity attributable to shareholders	**931,742**	**1,022,339**
Valuation differences:		
Solvency II valuation adjustment movements:		
Fixed assets	(9,803)	(11,221)
Technical Provisions	110,311	66,015
Discounting	63,611	33,602
Risk Margin	(132,655)	(105,101)
Deferred tax	(6,970)	1,611
Solvency II excess of assets over liabilities	**956,236**	**1,007,245**

There is no material difference between net assets per the financial statements and the excess of assets over liabilities for the purposes of Solvency II.

Description of Deductions from Own Funds

No deductions are applied to own funds and there are no material restrictions affecting their availability and transferability.

SECTION E. 2 – Solvency Capital Requirement and Minimum Capital Requirement

Details and changes since the prior period reporting of the Solvency Capital Requirement and Minimum Capital Requirement

The Company has not applied to the PRA for the approval of an Internal Model and, as such, is required to use the Standard Formula to determine the regulatory Solvency Capital Requirement. The Company's SCR is subject to supervisory assessment.

The Company has not used undertaking specific parameters in the calculation of the standard formula Solvency Capital Requirement.

In deriving the SF SCR, the Company has relied on the simplifications set out in the following articles of the Delegated Acts:

- Article 107; simplified calculation of the risk mitigating effect for reinsurance arrangements or securitisation in respect of counterparty default risk
- Article 111: simplified calculation of the risk mitigating effect in respect of counterparty default risk
- Article 112: simplified calculation of the risk adjusted value of collateral in respect of counterparty default risk

These articles are applied in the context of Article 88 on proportionality being complied with for the risk mitigation effect.

The table below shows the SCR split by risk category and in aggregate:

Amounts in $000s	2016	2017	# Change	% Change
Non Life	559,254	578,687	19,433	3%
Market	153,329	153,098	-231	0%
Counterparty	91,926	96,065	4,140	5%
Operational	63,616	73,761	10,145	16%
Div. benefits/Tax offset	157,491	152,411	-5,080	-3%
LMIE SCR	**710,633**	**749,200**	**38,566**	**5%**
MCR	**245,958**	**264,211**	**18,253**	**7%**

Overall, the SCR has increased by 7% or $39m over the year.
Key drivers of change are as follows:

- Non life underwriting risk has gone up in line with the build-up of net claims provisions;
- Market risk is stable due to better interest rate risk and currency risk management, offset by increases in spread risk, reflecting shifts in investments;
- Counterparty default risk and Operational risk increases are in line with the deteriorations in technical provisions.
- $8m reduction in the benefit from deferred tax liabilities offset.

The MCR has increased by 7%. The table below shows the MCR inputs by Solvency II line of business and how they have changed over the year:

			2016			2017		
SII Classes	**TP Factor**	**Premium Factor**	**Net TPs**	**NWP**	**MCR Charge**	**Net TPs**	**NWP**	**MCR Charge**
Motor Liability	8.5%	9.4%	40,200	1,797	3,586	31,639	0*	2,689
Other Motor	7.5%	7.5%	3	222	17	89	0*	7
MAT	10.3%	14.0%	32,833	26,479	7,089	50,658	32,814	9,812
Fire & other damage to property	9.4%	7.5%	189,996	159,492	29,822	217,394	143,039	31,163
General liability	10.3%	13.1%	1,126,378	396,945	168,017	1,177,074	399,216	173,536
Credit & Suretyship	17.7%	11.3%	19,758	122,172	17,303	57,979	135,025	25,520
Legal expense	11.3%	6.6%	10,693	0	1,208	0	0	0
Assistance	18.6%	8.5%	0	0	0	0	0	0
Miscellaneous	18.6%	12.2%	6,891	973	1,400	2,756	808	611
Non-prop. Property RI	18.6%	15.9%	8,719	12,099	3,546	15,726	24,236	6,778
Non-prop. Casualty RI	18.6%	15.9%	33,593	14,089	8,489	48,245	15,543	11,445
Non-prop. MAT RI	18.6%	15.9%	27,405	2,426	5,483	11,176	3,594	2,650
Total			**1,496,468**	**736,695**	**245,958**	**1,612,735**	**754,222**	**264,211**

* NWP are zeroised for the purpose of deriving the MCR charge if negative.

Key drivers of change in the MCR are as follows:

- 8% increase in net technical provisions;
- 2% increase in net written premiums;
- change in mapping of Energy Offshore class from Fire to MAT, the latter attracting a larger charge.

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

This section is not applicable.

SECTION E. 4 – Differences between the standard formula and any internal models used

The Company does not have an approved full or partial internal model, according to Article 112(7), to calculate the Solvency Capital Requirement.

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

Compliance with both the MCR and SCR have been maintained during the reporting period.

SECTION E. 6 – Any Other Information

LMIE does not have any other material information to report.

GLOSSARY OF TERMS

Reference	Description	Reference	Description
ABS	Asset Backed Security	LOC	Letter of Credit
AF	Actuarial Function	LSM	Liberty Specialty Markets
ALAE	Allocated Loss Adjusted Expenses	MCR	Minimum Capital Requirement
AOCI	Accumulated Other Comprehensive Income	MI	Management Information
BEC	Board Executive Committee	ORSA	Own Risk and Solvency Assessment
BBNI	Bound But Not Incepted	P&C	Property & Casualty
COR	Combined Operating Ratio	PRA	Prudential Regulation Authority
CP	Contingency Plans	PTOI	Pre-Tax Operating Income
CRO	Chief Risk Officer	QRT	Quantitative Reporting Templates
CUO	Chief Underwriting Officer	RAG	Red, Amber, Green
DGS	Direccion General de Seguros	RDS	Realistic Disaster Scenario
EIOPA	European Insurance and Occupational Pensions Authority	RI	Reinsurance
EPIFP	Expected Profit in Future Premium	RM&ICF	Risk Management and Internal Control Framework
ENID	Events not in Data	RMC	Risk Management Committee
EWI	Early Warning Indicator	RMF	Risk Management Framework
FCA	Financial Conduct Authority	RMS	Risk Management Solutions
GAAP	Generally Accepted Accounting Practices	ROE	Return on Equity
GBP	Great Britian Pound	RST	Reverse Stress Test
GWP	Gross Written Premium	SII	Solvency II
HR	Human Resources	S&P	Standard & Poor's
IA	Internal Audit	SCR	Solvency Capital Requirement
ICA	Individual Capital Assessment	SF	Standard Formula
IIA	Institute of Internal Audit	SFCR	Solvency and Financial Condition Report
IFRS	International Financial Reporting Standards	SPA	Strategy, Planning and Analysis
IM	Internal Model	SST	Stress & Scenario Test
LAP	Liberty Attestation Process	TP	Technical Provisions
LMAL	Liberty Managing Agency Limited	ULAE	Unallocated Loss Adjusted Expenses
LMG	Liberty Mutual Group	USD	United States Dollar
LMIE	Liberty Mutual Insurance Europe	YOA	Year of Account

APPENDIX A – QRT’S

All QRT’s are $000’s

List of Reported Templates:

S.02.01.02 - Balance sheet

S.05.01.02 - Premiums, claims and expenses by line of business

S.05.02.01 - Premiums, claims and expenses by country

S.17.01.02 - Non-Life Technical Provisions

S.19.01.21 - Non-Life insurance claims

S.23.01.01 - Own Funds

S.25.01.21 - Solvency Capital Requirement - for undertakings on Standard Formula

S.28.01.01 - Minimum Capital Requirement - Only life or only non-life insurance or reinsurance activity

S.02.01.02 – Balance Sheet - Assets

S.02.01.02

Balance sheet

		Solvency II value
	Assets	C0010
R0030	Intangible assets	
R0040	Deferred tax assets	
R0050	Pension benefit surplus	8,117
R0060	Property, plant & equipment held for own use	0
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	2,286,214
R0080	*Property (other than for own use)*	0
R0090	*Holdings in related undertakings, including participations*	5
R0100	*Equities*	0
R0110	*Equities - listed*	
R0120	*Equities - unlisted*	
R0130	*Bonds*	2,248,390
R0140	*Government Bonds*	638,752
R0150	*Corporate Bonds*	1,600,391
R0160	*Structured notes*	0
R0170	*Collateralised securities*	9,247
R0180	*Collective Investments Undertakings*	33,684
R0190	*Derivatives*	
R0200	*Deposits other than cash equivalents*	4,135
R0210	*Other investments*	0
R0220	Assets held for index-linked and unit-linked contracts	
R0230	Loans and mortgages	0
R0240	*Loans on policies*	0
R0250	*Loans and mortgages to individuals*	
R0260	*Other loans and mortgages*	
R0270	Reinsurance recoverables from:	845,951
R0280	*Non-life and health similar to non-life*	845,951
R0290	*Non-life excluding health*	845,951
R0300	*Health similar to non-life*	0
R0310	*Life and health similar to life, excluding index-linked and unit-linked*	0
R0320	*Health similar to life*	
R0330	*Life excluding health and index-linked and unit-linked*	
R0340	*Life index-linked and unit-linked*	
R0350	Deposits to cedants	32,497
R0360	Insurance and intermediaries receivables	136,362
R0370	Reinsurance receivables	26,884
R0380	Receivables (trade, not insurance)	0
R0390	Own shares (held directly)	0
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	0
R0410	Cash and cash equivalents	275,890
R0420	Any other assets, not elsewhere shown	29,276
R0500	**Total assets**	3,641,191

S.02.01.02 – Balance Sheet - Liabilities

S.02.01.02

Balance sheet

		Solvency II value
	Liabilities	C0010
R0510	Technical provisions - non-life	2,591,341
R0520	*Technical provisions - non-life (excluding health)*	2,591,341
R0530	*TP calculated as a whole*	0
R0540	*Best Estimate*	2,458,686
R0550	*Risk margin*	132,655
R0560	*Technical provisions - health (similar to non-life)*	0
R0570	*TP calculated as a whole*	0
R0580	*Best Estimate*	0
R0590	*Risk margin*	0
R0600	Technical provisions - life (excluding index-linked and unit-linked)	0
R0610	*Technical provisions - health (similar to life)*	0
R0620	*TP calculated as a whole*	
R0630	*Best Estimate*	
R0640	*Risk margin*	
R0650	*Technical provisions - life (excluding health and index-linked and unit-linked)*	0
R0660	*TP calculated as a whole*	
R0670	*Best Estimate*	
R0680	*Risk margin*	
R0690	Technical provisions - index-linked and unit-linked	0
R0700	*TP calculated as a whole*	
R0710	*Best Estimate*	
R0720	*Risk margin*	
R0740	Contingent liabilities	0
R0750	Provisions other than technical provisions	
R0760	Pension benefit obligations	
R0770	Deposits from reinsurers	
R0780	Deferred tax liabilities	13,610
R0790	Derivatives	
R0800	Debts owed to credit institutions	0
R0810	Financial liabilities other than debts owed to credit institutions	0
R0820	Insurance & intermediaries payables	11,464
R0830	Reinsurance payables	
R0840	Payables (trade, not insurance)	68,404
R0850	Subordinated liabilities	0
R0860	*Subordinated liabilities not in BOF*	
R0870	*Subordinated liabilities in BOF*	0
R0880	Any other liabilities, not elsewhere shown	135
R0900	**Total liabilities**	2,684,955
R1000	**Excess of assets over liabilities**	956,236

S.05.01.02 – Premiums, claims and expenses by line of business

S.05.01.02
Premiums, claims and expenses by line of business

Non-life

		Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)												Line of business for: accepted non-proportional reinsurance				Total
		Medical expense insurance	Income protection insurance	Workers' compensation insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Credit and suretyship insurance	Legal expenses insurance	Assistance	Misc. financial loss	Health	Casualty	Marine, aviation and transport	Property	
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130	C0140	C0150	C0160	C0200
	Premiums written																	
R0110	Gross - Direct Business				-72	-9	36,496	121,991	480,656	140,230			127,566					906,858
R0120	Gross - Proportional reinsurance accepted				0	0	12,277	89,844	123,067	60,859			11,103					297,149
R0130	Gross - Non-proportional reinsurance accepted														2,147	2,284	42,223	46,654
R0140	Reinsurers' share				-24	-3	2,619	75,898	191,023	63,778			126,754		8,725	654	21,518	490,942
R0200	Net				-47	-6	46,154	135,936	412,700	137,310	0		11,915		-6,577	1,630	20,705	759,720
	Premiums earned																	
R0210	Gross - Direct Business				-18	-2	51,274	127,140	449,327	97,648			126,434					851,803
R0220	Gross - Proportional reinsurance accepted				0	0	11,700	84,552	98,370	24,745			423					219,790
R0230	Gross - Non-proportional reinsurance accepted														2,201	2,240	20,165	24,606
R0240	Reinsurers' share				-24	-3	6,371	71,807	182,843	40,059			125,715		8,262	10,837	7,829	453,696
R0300	Net				6	1	56,603	139,885	364,854	82,334	0		1,142		-6,062	-8,597	12,336	642,502
	Claims incurred																	
R0310	Gross - Direct Business				-9,419	-1,164	26,362	305,882	310,794	37,732			85,243					755,430
R0320	Gross - Proportional reinsurance accepted				0	0	5,039	49,834	56,981	13,569			203					125,628
R0330	Gross - Non-proportional reinsurance accepted														1,494	1,336	11,336	14,166
R0340	Reinsurers' share				226	28	-3,774	159,797	84,825	16,682			84,516		1,068	1,123	16,828	361,319
R0400	Net				-9,645	-1,192	35,176	195,919	282,949	34,619	0		930		426	213	-5,492	533,904
	Changes in other technical provisions																	
R0410	Gross - Direct Business																	0
R0420	Gross - Proportional reinsurance accepted																	0
R0430	Gross - Non-proportional reinsurance accepted																	0
R0440	Reinsurers' share																	0
R0500	Net				0	0	0	0	0	0	0		0		0	0	0	0
R0550	**Expenses incurred**				-123	-15	17,526	49,461	141,473	38,077	0		-6,244		-453	1,317	7,011	248,030
R1200	**Other expenses**																	1,932
R1300	**Total expenses**																	249,962

S.05.01.02 – Premiums, claims and expenses by country

S.05.02.01
Premiums, claims and expenses by country

Non-life

		C0010	C0020	C0030	C0040	C0050	C0060	C0070
		Home Country	Top 5 countries (by amount of gross premiums written) - non-life obligations			Top 5 countries (by amount of gross premiums written) - non-life obligations		Total Top 5 and home country
R0010			FR	IE	ES	IT	US	
		C0080	C0090	C0100	C0110	C0120	C0130	C0140
	Premiums written							
R0110	Gross - Direct Business	545,666	98,012	15,350	38,442	24,755	15,928	738,153
R0120	Gross - Proportional reinsurance accepted	76,221	1,293	46,972	9,088	21,870	58,824	214,267
R0130	Gross - Non-proportional reinsurance accepted	26,571	2,342	117	1,235	1,539	15,919	47,722
R0140	Reinsurers' share	270,833	54,580	20,136	16,049	15,424	30,913	407,936
R0200	Net	377,624	47,066	42,303	32,716	32,739	59,759	592,207
	Premiums earned							
R0210	Gross - Direct Business	487,715	97,238	15,357	36,503	20,766	19,497	677,075
R0220	Gross - Proportional reinsurance accepted	39,190	903	2,317	9,774	23,339	49,817	125,339
R0230	Gross - Non-proportional reinsurance accepted	24,944	2,609	117	1,155	1,502	15,250	45,577
R0240	Reinsurers' share	252,232	52,615	8,633	13,427	15,061	37,603	379,570
R0300	Net	299,616	48,135	9,158	34,004	30,546	46,961	468,421
	Claims incurred							
R0310	Gross - Direct Business	359,557	72,019	8,060	22,742	12,334	64,000	538,711
R0320	Gross - Proportional reinsurance accepted	18,826	-718	27	5,631	16,433	29,538	69,737
R0330	Gross - Non-proportional reinsurance accepted	16,735	1,809	80	508	1,378	15,551	36,062
R0340	Reinsurers' share	160,701	38,908	2,043	8,897	7,378	42,130	260,056
R0400	Net	234,417	34,202	6,124	19,984	22,768	66,959	384,453
	Changes in other technical provisions							
R0410	Gross - Direct Business							0
R0420	Gross - Proportional reinsurance accepted							0
R0430	Gross - Non-proportional reinsurance accepted							0
R0440	Reinsurers' share							0
R0500	Net	0	0	0	0	0	0	0
R0550	**Expenses incurred**	123,786	19,402	5,575	12,579	14,113	16,537	191,992
R1200	**Other expenses**							0
R1300	**Total expenses**							191,992

S.17.01.02 – Non-Life Technical Provisions

S.17.01.02
Non-Life Technical Provisions

	Direct business and accepted proportional reinsurance												Accepted non-proportional reinsurance				Total Non-Life obligation
	Medical expense insurance	Income protection insurance	Workers' compensation insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Credit and suretyship insurance	Legal expenses insurance	Assistance	Miscellaneous financial loss	Non-proportional health reinsurance	Non-proportional casualty reinsurance	Non-proportional marine, aviation and transport reinsurance	Non-proportional property reinsurance	
	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130	C0140	C0150	C0160	C0170	C0180
R0010 **Technical provisions calculated as a whole**				0	0	0	0	0	0	0		0		0	0	0	0
R0050 Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole																	0
Technical provisions calculated as a sum of BE and RM																	
Best estimate																	
Premium provisions																	
R0060 Gross				1	14	659	32,650	-12,868	11,313	0		-18,510		-4,000	1,271	-11	10,519
R0140 Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default				-808	6	7,439	24,061	-85,312	19,799	0		-12,315		-1,620	774	3,662	-44,314
R0150 **Net Best Estimate of Premium Provisions**				809	8	-6,781	8,589	72,444	-8,486	0		-6,195		-2,380	497	-3,673	54,833
Claims provisions																	
R0160 Gross				31,869	82	65,069	404,030	1,640,227	120,726	0		38,300		81,479	26,941	39,444	2,448,167
R0240 Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default				1,039	1	7,630	195,226	535,597	54,262	0		29,348		30,854	16,262	20,045	890,265
R0250 **Net Best Estimate of Claims Provisions**				30,830	81	57,439	208,805	1,104,630	66,464	0		8,952		50,625	10,679	19,399	1,557,902
R0260 **Total best estimate - gross**				31,870	96	65,727	436,681	1,627,359	132,039	0		19,790		77,480	28,212	39,433	2,458,686
R0270 **Total best estimate - net**				31,639	89	50,658	217,394	1,177,074	57,979	0		2,756		48,245	11,176	15,726	1,612,735
R0280 **Risk margin**				3,754	0	2,827	12,336	93,382	9,202	0		1,030		6,264	1,828	2,032	132,655
Amount of the transitional on Technical Provisions																	
R0290 Technical Provisions calculated as a whole																	0
R0300 Best estimate																	0
R0310 Risk margin																	0
R0320 **Technical provisions - total**				35,624	97	68,554	449,016	1,720,740	141,241	0		20,820		83,744	30,040	41,465	2,591,341
R0330 **Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total**				231	7	15,070	219,287	450,285	74,060	0		17,034		29,235	17,036	23,707	845,951
R0340 **Technical provisions minus recoverables from reinsurance/SPV and Finite Re - total**				35,393	90	53,485	229,729	1,270,455	67,181	0		3,786		54,509	13,004	17,758	1,745,390

S.19.01.21 – Non-Life Insurance Claims

S.19.01.21
Non-Life insurance claims

Total Non-life business

Z0020 **Accident year / underwriting year** Underwriting Year

Gross Claims Paid (non-cumulative)
(absolute amount)

		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0170	C0180
	Year	Development year											In Current year	Sum of years (cumulative)
		0	1	2	3	4	5	6	7	8	9	10 & +		
R0100	Prior											1,815,902	1,815,902	1,815,902
R0160	2008	8,681	34,275	37,943	27,705	33,093	35,698	17,879	2,920	42,224	5,563		5,563	245,982
R0170	2009	10,967	25,042	16,679	22,636	16,593	33,526	17,521	2,387	13,054			13,054	158,404
R0180	2010	3,394	29,877	38,330	50,740	105,413	31,440	20,639	6,370				6,370	286,203
R0190	2011	10,283	71,975	66,528	39,224	35,978	33,658	17,025					17,025	274,669
R0200	2012	26,257	62,585	100,040	65,718	41,673	28,569						28,569	324,841
R0210	2013	17,614	75,592	61,194	65,809	34,262							34,262	254,471
R0220	2014	69,217	130,940	50,740	50,995								50,995	301,891
R0230	2015	34,374	185,212	112,951									112,951	332,537
R0240	2016	35,159	160,702										160,702	195,861
R0250	2017	34,548											34,548	34,548
R0260												Total	2,279,940	4,225,309

Gross Undiscounted Best Estimate Claims Provisions
(absolute amount)

		C0200	C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0290	C0300	C0360
	Year	Development year											Year end (discounted data)
		0	1	2	3	4	5	6	7	8	9	10 & +	
R0100	Prior											110,291	107,194
R0160	2008	0	0	0	0	0	0	0	0	115,894	108,443		106,793
R0170	2009	0	0	0	0	0	0	0	38,798	33,634			32,743
R0180	2010	0	0	0	0	0	0	40,974	36,970				35,613
R0190	2011	0	0	0	0	0	102,579	87,034					84,134
R0200	2012	0	0	0	0	131,320	115,651						112,311
R0210	2013	0	0	0	201,032	195,322							190,298
R0220	2014	0	0	331,335	327,934								317,606
R0230	2015	0	423,861	513,762									497,729
R0240	2016	280,722	537,030										524,561
R0250	2017	452,179											439,183
R0260												Total	2,448,167

S.23.01.01 – Own Funds

S.23.01.01
Own Funds

		Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35	C0010	C0020	C0030	C0040	C0050
R0010	Ordinary share capital (gross of own shares)	290,225	290,225		0	
R0030	Share premium account related to ordinary share capital	100,000	100,000		0	
R0040	Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings	0	0		0	
R0050	Subordinated mutual member accounts	0		0	0	0
R0070	Surplus funds	0	0			
R0090	Preference shares	0		0	0	0
R0110	Share premium account related to preference shares	0		0	0	0
R0130	Reconciliation reserve	566,011	566,011			
R0140	Subordinated liabilities	0		0	0	0
R0160	An amount equal to the value of net deferred tax assets	0				0
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	0	0	0	0	0
R0220	**Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds**	0				
R0230	**Deductions for participations in financial and credit institutions**	0	0	0	0	
R0290	**Total basic own funds after deductions**	956,236	956,236	0	0	0
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	0				
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand	0				
R0320	Unpaid and uncalled preference shares callable on demand	0				
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	0				
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	0				
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	0				
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0				
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0				
R0390	Other ancillary own funds	0				
R0400	**Total ancillary own funds**	0			0	0
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	956,236	956,236	0	0	0
R0510	Total available own funds to meet the MCR	956,236	956,236	0	0	
R0540	Total eligible own funds to meet the SCR	956,236	956,236	0	0	0
R0550	Total eligible own funds to meet the MCR	956,236	956,236	0	0	
R0580	**SCR**	749,200				
R0600	**MCR**	264,211				
R0620	**Ratio of Eligible own funds to SCR**	127.63%				
R0640	**Ratio of Eligible own funds to MCR**	361.92%				

	Reconciliation reserve	C0060
R0700	Excess of assets over liabilities	956,236
R0710	Own shares (held directly and indirectly)	0
R0720	Foreseeable dividends, distributions and charges	
R0730	Other basic own fund items	390,225
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	0
R0760	**Reconciliation reserve**	566,011
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) - Life business	
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	252,293
R0790	**Total Expected profits included in future premiums (EPIFP)**	252,293

S.25.01.21 – Solvency Capital Requirement – Standard Formula

S.25.01.21

Solvency Capital Requirement - for undertakings on Standard Formula

		Gross solvency capital requirement	USP	Simplifications
		C0110	C0090	C0120
R0010	Market risk	153,098		
R0020	Counterparty default risk	96,065		
R0030	Life underwriting risk	0	9	
R0040	Health underwriting risk	0	9	
R0050	Non-life underwriting risk	578,687	9	
R0060	Diversification	-138,801		
R0070	Intangible asset risk	0		
R0100	**Basic Solvency Capital Requirement**	689,049		

	Calculation of Solvency Capital Requirement	C0100
R0130	Operational risk	73,761
R0140	Loss-absorbing capacity of technical provisions	0
R0150	Loss-absorbing capacity of deferred taxes	-13,610
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	0
R0200	**Solvency Capital Requirement excluding capital add-on**	749,200
R0210	Capital add-ons already set	0
R0220	**Solvency capital requirement**	749,200
	Other information on SCR	
R0400	Capital requirement for duration-based equity risk sub-module	0
R0410	Total amount of Notional Solvency Capital Requirements for remaining part	0
R0420	Total amount of Notional Solvency Capital Requirements for ring fenced funds	0
R0430	Total amount of Notional Solvency Capital Requirements for matching adjustment portfolios	0
R0440	Diversification effects due to RFF nSCR aggregation for article 304	0

S.28.01.01 – Minimum Capital Requirement

Linear formula component for non-life insurance and reinsurance obligations

	C0010
MCR_{NL} Result	264,211

	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
	C0020	C0030
Medical expense insurance and proportional reinsurance	0	
Income protection insurance and proportional reinsurance	0	
Workers' compensation insurance and proportional reinsurance	0	
Motor vehicle liability insurance and proportional reinsurance	31,639	0
Other motor insurance and proportional reinsurance	89	0
Marine, aviation and transport insurance and proportional reinsurance	50,658	32,814
Fire and other damage to property insurance and proportional reinsurance	217,394	143,039
General liability insurance and proportional reinsurance	1,177,074	399,216
Credit and suretyship insurance and proportional reinsurance	57,979	135,025
Legal expenses insurance and proportional reinsurance	0	0
Assistance and proportional reinsurance	0	0
Miscellaneous financial loss insurance and proportional reinsurance	2,756	808
Non-proportional health reinsurance	0	0
Non-proportional casualty reinsurance	48,245	15,543
Non-proportional marine, aviation and transport reinsurance	11,176	3,594
Non-proportional property reinsurance	15,726	24,236

Linear formula component for life insurance and reinsurance obligations

	C0040
MCR_L Result	0

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

Overall MCR calculation	C0070
Linear MCR	264,211
SCR	749,200
MCR cap	337,140
MCR floor	187,300
Combined MCR	264,211
Absolute floor of the MCR	2,910
Minimum Capital Requirement	264,211

APPENDIX B – Swiss Branch Financial Condition Report (FCR)

FINANCIAL CONDITION REPORT FOR LIBERTY MUTUAL INSURANCE EUROPE PLC, ZURICH BRANCH

For the period to 31st December 2017

SUMMARY

This appendix to the Liberty Mutual Insurance Europe Plc ('LMIE') Solvency & Financial Condition Report ('SFCR') has been prepared in relation to the operations of the Zurich branch of LMIE ('LMIE Zurich'), separately authorized by the Swiss Finance Market Supervisory Authority (FINMA) in accordance with the requirements of Articles 111a and 203a of the Insurance Supervision Ordinance and outlined in Circular 2016/2 – Disclosure – insurers, Principles for the financial condition report.

On the basis that LMIE is a UK authorized insurance company subject to Solvency II requirements (which include an equivalent disclosure regime to FINMA's) LMIE Zurich has obtained an exemption from the full requirements.

The purpose of this Appendix is to provide an overview of the key information in relation to LMIE Zurich under the broad headings of the information required by FINMA to accompany the full LMIE SCFR.

BUSINESS ACTIVITIES

There have been no material changes to the business activities of LMIE Zurich during 2017. LMIE Zurich is a key part of LMIE's overall European region's operations and underwrites mainly general liability focusing on financial lines, fine art and specie, terrorism, professional indemnity, energy and construction, D&O and cyber.

There are two ongoing developments that have impacted the branch's operations and will continue to do so into 2018:

LMIE European Strategy – LMIE has identified the European region (which includes Switzerland) as a key growth opportunity. In 2016 Kadidja Sinz was appointed the Head of Europe, and under her leadership a growth target of €200m has been targeted over a period to 2020. LMIE Zurich will be looking to positively contribute to this strategic target.

Brexit – the result of the UK vote to leave Europe in 2016 has a material impact on LMIE as a UK authorized insurance company with significant operations in Europe. LMIE has announced Brexit contingency plans (assuming a 'hard' Brexit where there are no cross border trade agreements in place) to re-domesticate LMIE to Luxembourg. Included within these plans has been the establishment of an intermediary based in Luxembourg in 2017. A branch of the Luxembourg intermediary, Liberty Specialty Markets Europe SARL ('LSME'), has been established in Switzerland. All staff within LMIE Zurich transferred to LSME Zurich with effect from 1st November 2017.

PERFORMANCE

LMIE Zurich has continued to grow in 2017. The GWP by end of 2017 showed a total of CHF 29’387’870.

The GWP development over the last 3 years is as follows:

GWP 2016	CHF 21’635’000
GWP 2015	CHF 18’216’069
GWP 2014	CHF 17’289’182

The profit as of end 2017 was CHF 10’140’209 before tax.

Claims history

Liberty Switzerland paid out losses of CHF 6’546’777 (i.e. about 60 individual losses). This increase of payments compared with 2016 results in particular because of the payment of a Large Loss of CHF 4’000’000 which had been previously reserved already in 2016. Most of the payments 2017 came out of losses that were well reserved already before this year, i.e. in 2016. Furthermore, the payment amounts increased because of the strong growth in the Fine Art & Species business which had some frequency losses.

Brief comments about the development in 2017

Despite the very challenging market environment LMIE Zurich can be pleased about the business written and the loss situation. There is still more than enough insurance capacity in the market and thus the premium level over all line of business Liberty sells is still heavily under pressure. We believe the so-called soft market will remain for the coming years.

Please refer to the Liberty Mutual Insurance Europe Limited Zurich Branch Annual Report and Financial Statements for further details of LMIE Zurich performance.

PREMIUMS, CLAIMS AND EXPENSES BY LINE OF BUSINESS

Currency: CHF or annual report currency
Amounts stated in millions

	Total		Direct Swiss business			
			Fire, natural hazards, property damage		General third-party liability	
	Previous year	Reporting year	Previous year	Reporting year	Previous year	Reporting year
Gross premiums	22	29	1	7	20	23
Reinsurers' share of gross premiums	-7	-10	0	-0	-7	-10
Premiums for own account (1 + 2)	15	19	1	6	14	13
Change in unearned premium reserves	-1	-1	-0	-0	-0	-1
Reinsurers' share of change in unearned premium reserves	-0	2	-0	-0	-0	2
Premiums earned for own account (3 + 4 + 5)	14	20	1	6	13	14
Other income from insurance business	-	-	-	-	-	-
Total income from underwriting business (6 + 7)	**14**	**20**	**1**	**6**	**13**	**14**
Payments for insurance claims (gross)	-1	-7	-0	-3	-1	-3
Reinsurers' share of payments for insurance claims	0	1	-	0	0	1
Change in technical provisions	-11	3	-0	-2	-11	4
Reinsurers' share of change in technical provisions	5	-0	-0	-0	5	-0
Change in technical provisions for unit-linked life insurance						
Expenses for insurance claims for own account (9 + 10 + 11 + 12 + 13)	**-7**	**-3**	**-0**	**-5**	**-7**	**2**
Acquisition and administration expenses	-7	-8	-1	-2	-6	-6
Reinsurers' share of acquisition and administration expenses	2	2	-	0	2	2
Acquisition and administration expenses for own account (15 + 16)	-5	-6	-1	-2	-4	-5
Other underwriting expenses for own account	-	-	-	-	-	-
Total expenses from underwriting business (14 + 17 + 18) (non-life insurance only)	**-12**	**-9**	**-1**	**-6**	**-11**	**-3**
Investment income	-	-				
Investment expenses	-0	-				
Net investment income (20 + 21)	**-0**	**-**				
Capital and interest income from unit-linked life insurance	-	-				
Other financial income	-	-				
Other financial expenses	-0	-1				
Operating result (8 + 14 + 17 + 18 + 22 + 23 + 24 + 25)	**1**	**10**				
Interest expenses for interest-bearing liabilities	-	-				
Other income	-	1				
Other expenses	-	-				
Extraordinary income/expenses	-	-				
Profit / loss before taxes (26 + 27 + 28 + 29 + 30)	**1**	**10**				
Direct taxes	-1	-5				
Profit / loss (31 + 32)	**1**	**5**				

CORPORATE GOVERNANCE & RISK MANAGEMENT

Corporate Governance

The Corporate Governance Framework detailed in the SFCR for LMIE applies to the operations of LMIE Zurich, notably the Board of Directors, and the activities of the key Board and Management Committees. An appointed individual, the General Manager, based in Zurich has lead responsibility for the day to day management of the branch with reporting lines to LMIE President & Managing Director.

In addition, LMIE Zurich has a local branch management committee to assist the General Manager to fulfil his responsibilities in relation to running the business of the branch (the Committee was effective from September 2017). The duties of the Committee are as set out below:

- Implementing the LMIE risk management and internal controls framework to meet the requirements both of the branch and LMIE;
- Monitoring the financial, operational and underwriting performance of the branch against targets, objectives and key performance indicators set by the boards;
- Monitoring the performance of processes and controls operating both at the branch level, and at LMIE on behalf of the branch;
- Where functions are performed by LMIE on behalf of the branch, ensuring that sufficient and appropriate MI is provided to allow monitoring of these, and that agreed actions are monitored and resolved;
- Reviewing and approving the section of the LMIE ORSA that applies to the branch;
- Reviewing compliance with applicable legal and regulatory requirements and LMIE protocols; and
- Approving and monitoring policies and procedures applicable to the branch.

Risk Management

LMIE Zurich has implemented the LMIE Risk Management & Internal Control Framework (referred to in this SFCR), which is applicable to all LMIE operations. Included within this framework is an addendum which outlines certain aspects of the overall framework specific to LMIE Zurich including:

- The role of the LMIE Zurich Branch Management Committee
- The maintenance of a separate LMIE Zurich Control Register (maintained on LSM's control register system – Magique)
- LMIE Zurich risk quantification

The process for preparing a section of LMIE's overall ORSA specific to LMIE Zurich, approved and signed off by the LMIE General Representative.

RISK PROFILE

LMIE's risk profile is assessed at an overall LMIE level as described in the SFCR. The Board does not believe there is a significant impact on the risk profile of LMIE from the operations of LMIE Zurich. As described above a separate control register is in place to monitor and oversee the control framework of LMIE Zurich.

VALUATION

The assets and liabilities of the Branch are valued in accordance with the accounting and valuation principles, specified by the Code of Obligations. Valuation principles not specified in the Code of Obligations are listed in the Liberty Mutual Insurance Europe Limited Zurich Branch Annual Report and Financial Statements.

CAPITAL MANAGEMENT & SOLVENCY

Through 2017 the Zurich Branch Management Committee has monitored the tied assets of LMIE Zurich. As at 31st December 2017 the solvency position of LMIE Zurich is:

Available Capital	CHF 110’463’493
Required Capital	CHF 76'760'853
Surplus	CHF 33'702'640
Capital coverage ratio	144%

The capital coverage ratio after considering the counterparty limits for Banque Cantonale de Geneve is 120%.