STM Life Assurance PCC Plc

Solvency and Financial Condition Report ('SFCR')

(for the financial year ended 31 December 2017)

Contents

Executive Summary

The new EU wide regulatory regime for insurance companies, known as Solvency II, came into force with effect from 1 January 2016. As this document is the second Solvency and Financial Condition Report (SFCR) that is required to be published by STM Life Assurance PCC Plc (STM Life or 'the Company'), comparatives are now included.

The Company's aim as an organisation is to provide products and services that enable its policyholders to maintain and grow their assets in a tax efficient manner catering for the legislation and tax in their country of residence. This service is delivered in a timely, personal and friendly manner using technology as appropriate.

The Company writes and administers contracts of insurance as follows:

- Annuity contracts (Class I)
- Unit-linked contracts (Class III & Class IV)

There were no material changes to our business and performance, system of governance, risk profile, valuation for solvency purposes and capital management during the reporting period.

The table below summarises the Company's capital position, under Solvency II, at the end of 2017. The Company applies the standard formula for calculation of its Solvency Capital Requirements (SCR). SCR is the amount of capital that the Company must hold to protect it from extreme risk events and to comply with EU regulation.

Solvency II Balance Sheet (£M)		**2017**
Assets		320.7
Best Estimate Liabilities	312.6	
Risk Margin	1.4	
Total Liabilities		314.0
Eligible Own Funds to cover capital requirements		6.7
Solvency Capital Requirement		3.4
AMCR		3.3
Excess Assets over AMCR		**3.4**
Excess Assets over Calculated SCR		**3.3**
Calculated SCR Coverage Ratio		**195.1%**
AMCR Coverage Ratio		**206.7%**

Approval by the Board of Directors of the Solvency and Financial Condition Report

Financial period ended 31 December 2017.

We certify that:

1. The Solvency and Financial Condition Report ('SFCR') has been properly prepared in all material respects in accordance with the Gibraltar Financial Services Commission ("GFSC") rules and Solvency II Regulations; and

2. We are satisfied that:
    a. Throughout the financial year in questions, the Company has complied in all material respects with the requirements of the GFSC rules and Solvency II Regulations as applicable to the Company: and
    b. It is reasonable to believe that, at the date of publication of the SFCR, the Company has continued so to comply, and will continue so to comply in future.

Approval by the Board of the SFCR and reporting templates

Kevin Dann
Managing Director
For and on behalf of the Board
Date: 5th May 2018

A. Business and Performance

A.1 Business

STM Life is a Protected Cell Insurance Company registered in 2008. The Company number is 100244.

The Company's registered office and operating address is:

Montagu Pavilion
8-10 Queensway
Gibraltar
GX11 1AA

The Company is authorised and regulated by the Gibraltar Financial Services Commission(GFSC).

PO Box 940
Suite 3, Ground Floor Atlantic Suites
Europort Avenue
Gibraltar
Tel:+350 20040283
Fax:+350 20040282
E-Mail: information@fsc.gi

The Company's external auditor is:

Deloitte Limited
Merchant House
22/24 John Mackintosh Square
Gibraltar
GX11 1AA

STM Life is a private company limited by shares and the ultimate owner is STM Group PLC. STM Life is regulated as a solo insurance entity.

The Company writes and administers contracts of insurance as follows:

- Annuity contracts (Class I)
- Unit-linked contracts (Class III & Class IV)

STM Life has established a branch in the UK and is authorised to carry out services in the following countries under EEA pass-porting arrangements:

Belgium	Italy
Cyprus	Ireland
Finland	Norway
France	Spain
Germany	Sweden
Malta	United Kingdom

A.2 Underwriting Performance

The Company is authorised to write long term insurance business. Premiums received in the year relate to new contracts of insurance written in 2017. The Company does not utilise any reinsurance.

The table below shows the Company's premiums, claims and expenses split by Solvency II lines of business for the period ended 31 December 2017.

	2017 £'000					**2016 £'000**
	Class I Annuities		Unit-Linked		**Total**	**Total**
Gross Premiums	33,318		99,503		**132,821**	**173,876**
Gross Claims	18,025		24,038		**(42,063)**	**(23,244)**
Expenses (Acquisition & administration)	(129)		(9,972)		**(10,101)**	**(85,268)**

A.3 Investment Performance

The Company has an investment policy which complies with the requirements under the 'prudent person principle'.

The Company holds two categories of asset; unit linked and non-unit linked. The assets held to match the unit linked liabilities are ear-marked to cover the unit linked liabilities. All non-unit linked assets of the Company are included within the single long term business fund. As a result of the PCC structure of STM Life, the unit-linked assets relating to each individual cell are ring fenced from all other assets. STM Life does not make any investment decisions in relation to the unit-linked assets. These are made either by the Policyholder or their Investment Adviser.

The investment strategy of the non-linked assets in the long term business fund is to balance maximising returns, whilst retaining an ability to maintain adequate solvency, an appropriate degree of matching of assets to liabilities and to provide sufficient liquidity to meet the Company's cash-flow needs.

As at 31 December 2017, the Company's long term business fund comprised the following assets:

Type of Assets	Amount (£'000)	% of portfolio
Deposits with credit institutions	28,960	9.19
Cash at bank and in hand	60	0.02
Assets held to cover linked liabilities	286,159	90.79
Total	**315,179**	**100.00**

Investment income:	2017 £'000	2016 £'000
Investment Income:		
Dividends and interest income	3,036	1,493
Net gains on realisation of investments		
- Assets held to cover linked liabilities	(17,456)	(70,770)
	(14,420)	**(69,277)**
Net unrealised gains/(losses) on investments:		
- Assets held to cover linked liabilities	10,160	(9,709)
Total investment return:	**(4,260)**	**(78,986)**

B. System of Governance

B.1 Governance Structure

The Company Board has responsibility for the oversight of the Company's business and sets its strategy and risk appetite. The Board has established sub committees, under its overall authority, to deal with certain functions in detail. All members of the committees are considered to have appropriate skills and expertise to undertake their role within the committees.

The two committees currently in place are Risk, Audit and Compliance Committee chaired by an NED, and Investment Committee chaired by the Managing Director.

The Board is the main decision making body for the Company. It determines the strategic direction and has responsibility for the overall management of the Company's business affairs. The Board sets the Company's values and standards and has overall responsibility for ensuring that obligations to policyholders and other stakeholders are understood and met. The Board monitors and oversees the Company's operations with the purpose of maintaining competent management, sound planning, robust and prudent risk and capital management, an effective internal control environment, a culture of risk awareness and ethical behaviour, and compliance with statutory and regulatory obligations.

The Board consists of such number of individuals as the Board may determine from time to time. The Board of Directors as at 31 December 2017 were:

Kevin Dann (Managing Director)
Peter Gatenby (Non-Executive Director)
Ian Costain (Non-Executive Director)

Risk, Audit and Compliance Committee
The Risk, Compliance and Audit Committee assists the Board in its leadership and oversight of risk across the Company including the understanding and, where appropriate, optimisation of current and future risk strategy, overall risk appetite and tolerance, risk management framework including risk policies, process and controls, and the promotion of a risk awareness culture throughout the Company. The Committee also assists the Board in fulfilling its oversight responsibilities in respect of the integrity of the Company's systems of internal control, financial processes, financial statements and performance of its internal audit function.

The Committee consists of two Non-Executive Directors and the Managing Director. The STM Group Head of Enterprise Risk Management attends meetings of the Committee by invitation.

The primary responsibilities of the Risk, Audit and Compliance Committee are to:

- Ensure that independent, effective and sufficiently resourced Risk Management and Compliance functions are established and that these functions operate effectively as the second line of defence.
- Review and assess the adequacy and effectiveness of the risk and compliance management systems across the Company.
- Review and recommend the approval of the risk management, compliance and governance policies across the Company.
- Make recommendations to the Board concerning the Company's overall risk appetite, tolerance and strategy.
- Monitor, and advise the Board on, the current risk exposures of the Company and future risk strategy. Inform the Board of the outcome of the statutory audit and explain how the statutory audit contributed to the integrity of financial reporting.
- Monitor the financial reporting process and submit recommendations on proposals to ensure its integrity.
- Monitor the effectiveness of the Company's internal control and risk management systems and, internal audit.
- Monitor the statutory audit of the annual financial statements, in particular its performance, taking into account any findings and conclusions.
- Review and monitor the independence of the statutory auditors and in particular the appropriateness of the provision of non-audit services.
- Be responsible for the procedure for selection of statutory auditors and recommend the auditor to be appointed.

Investment Committee

The Investment Committee oversees compliance with the Investment Policy and reviews its continuing appropriateness in the light of changing circumstances with consideration to the needs of both policyholders and shareholders.

The Committee consists of two Non-Executive Directors and the Managing Director.

The primary responsibilities of the Investment Committee are to:

- Set the Investment Policy.
- Periodically review the appropriateness of the Investment Policy in light of current circumstances of the Company, in particular in respect of capital requirements and overall market conditions.
- Develop and keep under review the appropriateness of key risk indicators and tolerances, and information provided by third parties, such as financial institutions, asset managers and rating agencies.
- Oversee the application of the Investment Policy.

Remuneration Policy

The Company's approach to remuneration is an integral part of the Business strategy and the policy is designed to attract, retain and motivate competent, experienced and skilled staff. The policy is based on the following principles:

a) Reward and remuneration will be clear and up to date with the market so that individuals are motivated and the Company is able to attract and retain key talent.
b) Remuneration packageswill be competitive and willrecognise the relative remuneration in comparable markets.
c) Remuneration will be determined fairly and objectively across the Company.
d) Variable reward for the Directors and key function holders will be linked to strategic objectives as well as considering current and future risks.
e) Total remuneration may include a fixed base salary as well as a variable discretionary bonus and other financial and non-financial employee benefits.

Remuneration for Executive Directors and persons responsible for key functions consists of a fixed salary, variable incentive pay, pension and other benefits.

Fixed Remuneration

This is the core element of the remuneration for Executive Directors and persons responsible for key functions within the Company. It is the Company's policy to pay a salary that is relevant to the specific role and responsibilities.

Each year the level of Directors' remuneration is reviewed so that it continues to be competitive and provides proper and risk-based incentives to the Executive Directors.

Base pay will normally be reviewed annually in January taking into consideration RPI and CPI as a guide in any cost of living uplift.

Non-Executive Directors

Remuneration for Non-Executive Directors comprises a basic fee.

Fees are benchmarked against similar roles in comparable organisations and calculated on an annual rather than a daily basis. However, it is assumed that to fulfil the basic role of a Non-Executive Director, sufficient time and commitment is required each month for review work and attendance at regular Board meetings, the Company's AGM, Special General Meetings where appropriate, other ad hoc meetings with regulators and advisers as may be required and training courses.

Non-Executive Directors remuneration is not performance related nor pensionable and Non-Executive Directors do not participate in any incentive plans.

Fees for Non-Executive Directors are determined by the Executive Directors and subject to approval of the Board as a whole. They are designed to recognise the responsibilities of Non-Executive

Directors and to attract individuals with the necessary skills and experience to contribute to the objectives of the Company.

B.2 Fit and Proper

Skills, knowledge and expertise

The Company, through its 'fit and proper' procedures, ensures that persons who effectively run the business or hold responsibility for other key functions (termed Solvency II staff) have, individually and collectively, an appropriate depth and diversity of knowledge, skills, qualifications, and experience relevant to their respective roles and duties, in order to manage and oversee the running of the organisation in an effective, compliant, and professional manner.

The Solvency II staff collectively possess appropriate qualifications, experience, and knowledge about at least:

1. Insurance and financial markets.
2. Business strategy and business model.
3. System of governance.
4. Financial and actuarial analysis.
5. Regulatory framework and requirements.

Fitness and Propriety

To make sure that Solvency II staff are fit and proper, they are recruited giving due regard to the following:

1. Job application answers e.g., questionnaire, declarations.
2. Interviews, case studies, role plays, knowledge and skills tests and other recruitment assessments.
3. Employment history and experience e.g., CV and employment references.
4. Character references.
5. Identity verification, financial sanctions checks, and work permit checks.
6. Financial services register and Companies House checks.
7. Qualifications checks e.g., certificates, membership of professional bodies.
8. Background financial checks e.g., credit checks.
9. Background criminal checks e.g., disclosure and barring service.
10. Background social media checks e.g., LinkedIn, Facebook.
11. Background reputational and disciplinary/enforcement checks.
12. Regulatory authorisation application form declarations.
13. The candidate's openness and co-operation in providing such information when requested.

There are specific regulatory requirements relating to the obtaining and giving of employment references and the Company takes reasonable steps to obtain employment references from current and previous employers covering at least the previous six years.

All staff (regardless of role) are required under their contract of employment to observe and act in accordance with the Company's Code of Ethics and Conduct.

The Company has a 'Fit and Proper' policy including a Fit and Proper declaration applicable to all Solvency II staff. It requires information in respect of the following matters:

- Financial difficulties, arrangements with creditors, bankruptcy, etc.
- Criminal prosecutions, civil proceedings, etc.
- Complaints.
- Disciplinary matters.
- Business interests.

B.3 Risk Management Systems

Risk Management system

Risk management is a central part of the Company's business strategy and Own Risk and Solvency Assessment (ORSA) process. It is a continuous and developing process whereby the Company methodically identifies, assesses and responds to the risks attached to its objectives and activities with the goal of achieving sustained benefit for both the Company and its policyholders.

Risk management governance operates on the basis of 'the three lines of defence'.

- Board and executive management are responsible for setting strategy, performance, measurement and implementation of suitable risk management systems and controls.
- The Risk function sets the Company's policies and procedures. This function is responsible for overseeing risk management across the Company, being a function reporting to the Risk and Compliance Committee and ultimately the Board.
- Independent assurance on the effectiveness of the Company's systems and internal controls. This is a role fulfilled by the Risk, Audit and Compliance Committee, internal auditors, external auditors and other skilled external practitioners e.g. consulting actuaries.

The Board has the ultimate responsibility for setting the Company's risk management strategy, reviewing the Company's systems of risk management and internal control and their effectiveness and being responsible to the regulator and its policyholders for ensuring compliance with regulatory obligations including capital and solvency requirements of the ORSA.

The risk management strategy is documented and together with the supporting high-level risk policies for the defined categories of risk is subject to regular review, update and approval.

The business strategy has been converted into key strategic risk appetite measures. In order to establish parameters within which risk must be managed, the Company has developed a statement of 'Risk Appetite' and associated measures / triggers for action.

The Risk, Audit and Compliance Committee reviews the risk appetite at least annually before it is submitted to the Board for approval setting out where the Company should take risks. The Board determines the risk appetite, taking into consideration recommendations from the Risk, Audit and Compliance Committee and senior management. The extent to which the Company tolerates risks is described by performance indicators, operational parameters and process controls.

Risk Function

The Risk function is headed by the Chief Actuary.

Key responsibilities of the function include:

- Promotion, training, maintenance and development of the risk management framework.
- Monitoring of the consistency of application and embedding of the risk management framework across the Company.
- Providing regular risk reporting to the Risk and Compliance Committee and other Committees, as required.
- Undertaking second line monitoring to assess whether the first line of defence if operating effectively.

To ensure independence of the Risk function, it has a reporting line to the Risk, Audit and Compliance Committee and has access to the Chairman of that Committee.

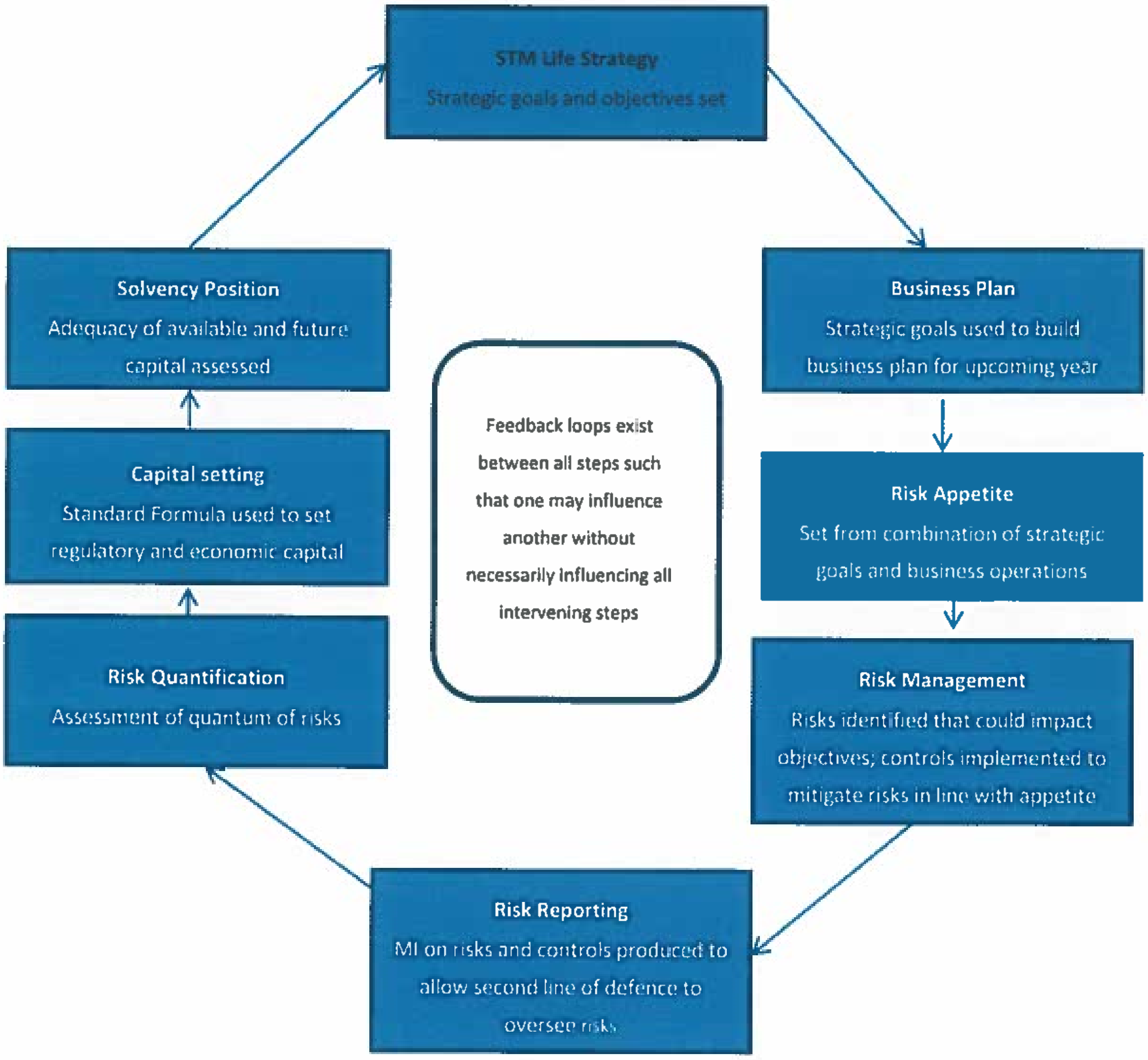
B.4 Own Solvency and Risk Assessment (ORSA)

The Board uses the ORSA process and report to assess its risk-based capital requirement, based on the Company's business strategy.

The Company has determined that the Solvency II standard formula would be used to calculate the required solvency capital and to assess overall solvency needs. A three year base case projection of the Solvency II Balance Sheet and solvency capital requirement (SCR) position is produced based on a number of key assumptions about the level of new business, economic and demographic risks, insurance risks including morbidity, lapses and future expense assumptions. These projections are then subjected to a range of stress tests in robust downward scenarios including stresses for lower than expected new product sales, worsening morbidity, lapses and expenses over and above assumptions.

The ORSA process is an integral part of the Company's governance and risk management framework and risk management system enabling the Board to make risk based informed decisions aligned to business strategy, risk appetite, capital and solvency needs. The framework below evidences the key steps of ORSA Framework and feedback loop embedded in the process.

The Board is ultimately responsible for ORSA framework, ORSA Policy and Process approval and ORSA report. The Board reviews, challenges and has approved the ORSA Policy and Process. The Board can delegate the responsibilities to its sub-committee and key business functions for the on-going review of ORSA in the day to day business activities and monitoring of any significant changes that impact on the ORSA. The Risk function is responsible for the day to day ORSA Policy and Process and will inform the Board regularly through the Risk and Compliance Committee for review and approval.



The Company's ORSA process operates continuously through the course of the year and is accompanied with periodic formal reporting. The full ORSA report is produced at least annually for the Board with monitoring of critical metrics from the ORSA on a quarterly basis through regular risk and capital MI reporting. Additionally, the ORSA is performed at intermediate times if capital adequacy is impacted either through capital erosion from a material event or a material change in the risk profile.

B.5 Internal Control Systems

The Company has established an internal control framework encompassing key controls of the business, both financial and non-financial, which enables the Company to achieve its key business objectives within its defined risk appetite. The effectiveness of these controls and their delivery of the key business objectives and risk appetite of the Company are regularly reviewed by the Board and its appointed sub-committees.

A risk management framework is in place so that risks are managed within the stated risk appetite. The Company's risk registers, both `top down' and `bottom up' document the Company's key risks and associated controls. These risks and controls have assigned owners and are subject to periodic reviews as part of the risk management process.

Key controls include:

- **Business planning process** – performed annually and sets the business objectives and key performance indicators. Performance against these objectives is monitored throughout the year by the Board and Executive Management.

- **Risk appetite process** – performed at least annually in line with the business planning process and sets the detailed risk appetite for the key risk areas within the Company.

- **Investment risk controls** – have been developed and documented within the Investment Policy detailing the investment principles and strategy as well as defining investment parameters, policies and controls and how the assets are valued.

- **Data validation processes** – detailed data quality control procedures, including analytical review and detailed cross checking to validate that the data within our systems and used for reporting is accurate and complete.

- **Escalation processes** – the control processes above in addition to other key measures e.g. risk appetite measures, loss events, root cause analysis and progress against audit actions are presented to the appropriate sub-committee.

The financial statements are subject to controls in the production and review before they are published. The actuarial methodology and assumptions follow actuarial practices and standards and are subject to review and approval by the Board. The final statements are also subject to external audit review and are signed-off by the Board prior to being published.

Compliance Function

The overall responsibility for overseeing the compliance of the Company, advising and supporting the business on compliance matters is a key function and approved by the regulators as a controlled function (Compliance Oversight). This key function is held by the Managing Director and the compliance activities are outsourced to the STM Gibraltar Head of Compliance who is deemed to be an appropriately competent person and responsible for ensuring the effectiveness of Company's systems and controls to meet regulatory compliance, and compliance reporting to the regulators.

The Compliance function is established as an independent control function and has formal status within the overall governance framework. The Head of Compliance is not engaged in areas of the business which could create a conflict of interest.

The function has access to all information as necessary to carry out its responsibilities and is responsible for reporting to executive management any breaches or non-compliance with relevant policies, rules and regulations.

The main activities of the Compliance function include:

- Training – to make sure staff receive regulatory training and information.
- Advice and Guidance–to support the business in respect of regulatory requirements and to make sure that any new regulatory rules are communicated to the relevant business areas.
- Compliance Monitoring – to assess the appropriateness of compliance controls and make sure that a monitoring plan is produced and implemented.
- Regulatory reporting– to respond to regulatory requests for information and submit reporting and information as required.
- Reporting – the function provides an annual Compliance report and ongoing quarterly information to the Risk, Compliance and Audit Committee.

B.6 Internal Audit

The Internal Audit function is a Key Function under Solvency II and is currently held by the Managing Director. The Internal Audit activities are outsourced to Mazars LLP.

On an annual basis the Internal Audit function formulates and present an annual audit plan to the Risk, Audit and Compliance Committee for approval. The internal audit plan is risk based and appropriate to the nature, scale and risks of the Company. The plan is developed to make sure that all areas within the business are subject to a review at least every 3 years although key business risks are subject to annual review. The plan is flexible so that changes can be made during the year as a result of changes in priorities, external conditions and risk areas.

Based on the audit plan, the internal audit function assesses the adequacy and effectiveness of controls covering areas of governance, operations and information systems.

B.7 Actuarial Function

The Chief Actuary has overall responsibility for the actuarial function and is the management function holder approved by the GFSC.

Currently the function holder is a qualified actuary who is a Fellow of the Institute and Faculty of Actuaries and has complied continuously with the specific professional obligations this requires.

The Actuarial function is established as an independent control function and has formal status within the overall governance framework. The function has access to the required resources through an internal team and access to external actuarial expertise for additional resource and peer review. The function is required to provide an annual report to the Board setting out the tasks undertaken by the function and its results.

The key responsibilities of the Chief Actuary role are:

- Providing actuarial advice to the Company's senior management and Board.
- Regulatory reporting of technical provisions and solvency capital requirements.
- Contributing to effective risk management system through modelling of risks and actuarial forecasts that form part of the ORSA process.
- Ensuring the effectiveness of the Company's actuarial methodology, assumptions, systems and controls for actuarial investigations and reports.
- Providing actuarial opinion on data quality, underwriting and reinsurance effectiveness.

B.7 Outsourcing

When considering outsourcing, the Company considers how it will fit with business strategy, the key risks the arrangement could present and the ability to continue to meet regulatory requirements.

The Company has an Outsourcing Policy in place which provides guidance and sets out the process to follow when considering an outsourced service provider.

The policy sets out at least the following:

- The due diligence includes an assessment of key risks and material factors that could impact on the potential service provider's ability to perform the required business activity. This includes checks including financial, regulatory, conflicts of interest, information security and business continuity.
- All outsourcing arrangements must be established with a written contractual agreement setting out the expectations and obligations of each party. The agreements must include certain terms to make sure they address risks and meet regulatory requirements.
- The contract requires internal approval as set out in the policy, and where a critical function is outsourced, this requires Board approval.

- A record of all outsourced arrangements is maintained with a process for regular monitoring and annual certification.

The Company is currently utilising the following service providers to undertake critical and important functions on its behalf:

Outsourced Provider	Service outsourced	Jurisdiction
Peter Gatenby Consulting	Chief Actuary	Spain
STM Group	Marketing Collateral, Compliance	Gibraltar
Mazars LLP	Internal Audit	UK
Oxford Actuaries & Consultants	Actuarial Software	UK

C. Risk Profile

Risk Assessment Process

Risk management is an integral part of the Company's business activities to ensure that the strategic objectives are maintained. The integrated approach ensures that value is created by identifying the right balance between risk and reward, whilst making sure that obligations are met and the outcomes remain in the best interest of policyholders.

The extent to which the Company tolerates risks is described by performance indicators, operational parameters and process controls set out in the 'Risk Appetite'. The Company's risk appetite determines the level of action/mitigation to be implemented against identified risks. There is direct interaction between the risk appetite and those risks highlighted in the risk assessment. Risks are rated on impact and probability and it has been determined that any risk with a residual risk rating high will require an action plan which will state what action is to be taken and on what timescale.

Prudent person principle

The Solvency II Regulations require that the "Prudent Person Principle" is applied to the Company's asset investment. The Company adheres to the principle by investing in a range of fixed interest and money market assets of an appropriate quality and level of diversification. There are also holdings in currency to minimise the impact of adverse market movements.

The weightings of the different asset classes and the nature of the underlying assets are regularly monitored and are reviewed quarterly by the Investment Committee to consider their appropriateness. Assets held in respect of the Solvency and Minimum Capital Requirements are also reviewed to ensure they offer an appropriate level of security and liquidity.

Risk Profile

The Company faces a number of risks which are summarised below and detailed in sections C1 – C5.

The risk profile depends on the nature of the insurance policies issued as at 31 December 2017, the assets held to match the liabilities and own funds.

The Company has around 1,421 in force unit linked bonds and Class I annuities.

Given the narrow range of in force contracts the Company only has exposure to some of the core underwriting risks. These are summarised in the table below. However, there are no material concentrations.

Contract Type	Mortality	Longevity	Morbidity	Expense	Lapse
Class I annuity contracts					
Unit-linked contracts	Minimal			Y	Y

Overall risk exposure

The Company uses the Solvency II Standard Formula approach to assess its exposure to risk. The most significant risks faced by the Company are underwriting risk (lapse and expense) and market risk. The two largest elements of market risk are concentration risk, primarily the term deposits backing the Class I annuities, and equity risk (collecting less charges than anticipated on those unit linked policies where charges are expressed as a percentage of policy value following an equity shock).

C.1 Underwriting Risk

Underwriting risk arises when premiums and investment income are insufficient to pay the contractual benefits on a policy or when the actual demographic experience and/or expenses of administering a group of policies is worse than assumed in the calculation of best estimate liabilities.

Mortality Risk

Where insurance contracts pay out a lump sum on death, the Company is exposed to the risk either that there are more deaths than expected or that policyholders die, on average, sooner than expected.

Mortality risk is not a significant risk for the Company for the following reasons:

- The majority of unit-linked contracts pay a death benefit of 101% of the value of the units with a maximum of the value of the units plus £2,000. Consequently the sum at risk for STM Life is very small and the mortality risk is set at zero on grounds of proportionality.
- Annuity contracts are not subject to mortality risk as higher death rates reduce the value of the main benefits.

Longevity Risk

Where insurance contracts pay out benefits which are dependent on survival or which lead to higher claims costs with increased longevity, the Company is exposed to the risk either that there are fewer deaths than expected or that policyholders die, on average, later than expected. The key exposures to longevity risk are non-profit annuities in payment. The Class I annuity that STM Life currently sells is a short term annuity with a term of 2 years and 1 month. The annuity payments are effectively guaranteed and therefore there is no longevity risk.

Lapse Risk

This is the risk that a policyholder lapses or surrenders their policy earlier than expected resulting in a loss to the Company. For all unit-linked contracts, there is a surrender penalty in place for early lapse to recoup acquisition costs and hence the Company is protected against the risk of not recouping these costs. The main lapse risk that the Company is exposed to is that of higher lapses than expected meaning that charges will be lower than expected and hence the difference between charges and costs will be smaller than expected. This leads to a lower than expected negative non-unit reserve.

Overall, a fall in lapse rates leads to the greatest loss in own funds when compared to an increase in lapses or a mass lapse.

Expense Risk

The Company is currently in a period of rapid growth and the rate of growth in number of policies and hence charges collected from those policies is significantly steeper than the rate of growth in administration costs. Consequently per policy expenses are reducing and some of this reduction has been taken into account when calculating technical provisions as at 31 December 2017.

Expense risk has been calculated as at 31 December 2017 for the first time.

Assessment and risk mitigation techniques

The Company has processes in place to monitor each of the underwriting risks:

- The risk register covers the key underwriting risks and is reviewed quarterly with a summary reported to the Risk, Audit and Compliance Committee on a quarterly basis.
- The Company's risk appetite statement sets thresholds for underwriting risk as a proportion of the undiversified basic SCR.
- Regular monitoring of lapse and expense assumptions.

A full valuation of the technical provisions and life obligations SCR is performed each quarter and the SCR coverage is reported to the Company's Board.

Risk sensitivity for underwriting risks

The Company assesses underwriting risk by considering a number of stand-alone stress tests and scenarios affecting material demographic and expense assumptions in its ORSA. The analyses consider the impact of an immediate shock to the starting balance sheet in addition to the impact on its forward-looking assessment of the future balance sheet position.

C.2 Market Risk

This represents the risk that the Company's solvency coverage is adversely affected by changes to financial market conditions which impact the fair value of assets held. The assets held in relation to unit-linked policies are not subject to market risk as all the investment risk is borne by the policyholder. For each policyholder the assets backing their policy are held in separate cells and completely ring fenced from all other policyholder and shareholder assets.

For funds backing the Class I annuities and Own Funds the Company holds a portfolio of UK and overseas assets comprising fixed interest and money market assets and is therefore subject to the Market Risk Module.

Material market risks

The two largest elements of market risk areconcentration risk, primarily the term deposits backing the Class I annuities, and equity risk (collecting fewer charges than anticipated on those unit linked policies where charges are expressed as a percentage of policy value following an equity shock).

Interest Rate Risk

Interest rate risk arises when a fluctuation in interest rates adversely affects the Company's SCR coverage. Both an increase and a decrease in interest rates are tested and the basic SCR is based on the more onerous reduction in interest rate scenario. This is driven by the basic SCR in respect of the assets backing the Own Funds.

The Own Funds are invested in fixed interest assets and thus there is a small, beneficial exposure to interest rate movements.

Concentration Risk

Concentration risk tests the resilience of own funds against the diversification of a portfolio of assets. The largest element of concentration risk for STM Life arises from the term deposits used to back the Class I annuity liabilities. The single largest institution used for these investments is currently Lloyds Bank with 51.3% of the portfolio invested in one and two year term deposits with Lloyds.

Equity Risk

No own funds are invested in equities by STM Life. Equity risk arises from the fact that anticipated future charges may not be collected following a large fall in equity values for those policies (185 out of 1,421) where the charging basis is a percentage of policy value rather than a percentage of initial premium.

Currency Risk

There is an element of currency risk which arises from the fact that some policies are expressed in currencies other than GBP. The main two other currencies in the current portfolio are Euros and US Dollars.

Spread Risk
There is a small amount of spread risk arising from the intergroup loan of £434,000 as at 31 December 2017.

Assessment and risk mitigation techniques
The Company has processes in place to monitor market risks:

- The risk register covers key market risks and is reviewed quarterly with a summary reported to the Risk and Compliance Committee on a quarterly basis.
- The Company's risk appetite statement sets thresholds for market risk as a proportion of the undiversified basic SCR.
- A regular review of surplus assets takes place at Investment Committee Meetings.
- Investment mandates specify maximum exposure limits to lower quality bond assets.
- A process is in place whereby management are informed before any transactions take place which would reduce average credit rating of the bond portfolios.

Risk sensitivity for market risks
The Company has assessed the sensitivity of the SCR coverage to a number of scenarios involving an instantaneous shock to the risk free yield curve such that risk free rates were assumed to be zero. This was performed on both a stand-alone basis and combined with the demographic assumption shocks. As market risk is such a small element of the SCR the shocks tested do not have a significant effect on SCR coverage.

C.3 Credit Risk

The only material credit risk that the Company faces is counterparty default risk.

Counterparty Default Risk
This risk arises when a counterparty is unable to fulfil its obligations to the Company, thereby leading to a loss of the Company's financial assets. As at 31 December 2017 the main component of this risk is due to the funds for two Class I annuities being held in cash in client bank accounts awaiting investment in term deposits.

Assessment and risk mitigation techniques
The Company has processes in place to monitor counterparty default risk:

- The risk register covers key default risks and is reviewed quarterly with a summary reported to the Risk and Compliance Committee on a quarterly basis.
- The Company's risk appetite statement sets thresholds for counterparty exposure in terms of monetary limits per counterparty and credit quality standing of counterparties. These are monitored regularly through the Risk and Compliance Committee.
- Each time that a new Class 1 annuity is written the management look at the options available, credit rating of the financial institutions, how much is already invested with

various financial institutions and currency of the liabilities before making a decision on which term deposits to invest in.

C.4 Liquidity Risk

Due to the nature of the assets and liabilities the Company is not exposed to liquidity risk.

C.5 Operational Risk

Operational risk is the risk of direct or indirect loss (actual or potential) resulting from inadequate or failed internal processes, people and systems or from external events. This includes risks relating to compliance, business processes, information technology, outsourcing and financial reporting.

Assessment and risk mitigation techniques
The Company's Operational Risk policy defines the types of operational risks faced and the processes in place to identify, assess, manage, monitor and report risks and events.

The following processes are in place to manage operational risk:

- Well established Risk function regularly performs operational risk monitoring, in order to assist in detecting deficiencies in the policies, procedures and processes of the Company and propose corrective actions.
- All departmental functions of the Company are required to conduct risk assessments which include specific operational risks inherent in their activities, including their identification and assessment with regard to the likelihood and impact on the Company, and report the identified events to through the Company's automated Risk Management System.
- Defined key risk indicators, to act as early warnings of increased risk of potential losses. Effective tracking of these indicators by the Risk function allows the Company to identify changing risks upon their occurrence and respond to them promptly.
- Disaster recovery and business continuity plans are put in place for all key functions/departments and take into account different types of plausible scenarios to which the Company's operations may be subject to. Such plans are periodically reviewed and tested.
- All outsourced activities are subject to due diligence and regular review and monitoring.

Risk sensitivity for operational risks
This is not currently a significant risk for the Company.

Conduct Risk
Conduct risk has the potential to arise if the Company's behaviours result in poor customer outcomes; it is inherent in any operation that provides products or services to customers. Delivering good customer outcomes is a key driver in building a valuable, sustainable business and is a key measure as part of the Company's risk appetite.

The Company's products are distributed through regulated intermediaries which mitigates the exposure to direct sales and distribution.

D Valuation for Solvency Purposes

D.1 Assets

Summary of asset valuation

The table below sets out the valuation of the Company's assets on a GFRS102 and Solvency II basis as at 31 December 2017:

Assets (£'000)	GFRS 102	Solvency II
Investments	28,960	28,961
Assets held to cover linked liabilities	286,159	285,493
Debtors	719	662
Other assets	4,302	4,884
Prepayments and accrued income	486	685
Total assets	**320,626**	**320,685**

Fair value measurement

In accordance with the Delegated Regulation, Solvency II figures are based on fair value. Where applicable, the Company measures the fair value of a financial instrument using the quoted price in an active market for that instrument.

Bonds – including Government bonds, Corporate bonds and Collateralised securities.

Government bonds consist of UK government gilts and treasury bonds. The valuation of gilts is based on level 1 methodology of the fair value hierarchy, whilst the valuation of treasury bonds and other fixed-interest securities (including corporate bonds and collateralised securities) are based on the level 2 methodology of the fair value hierarchy.

Deposits other than cash equivalents

Deposits other than cash equivalents consist of cash held on fixed term-deposits with a maturity date greater than 3 months and cash held with investment managers for investment purposes. The valuation of this is the total cash balances held and includes the interest accrued on the deposits up until the balance sheet date.

Assets held for index-linked and unit-linked contracts

The valuation of these assets is consistent with the fair value hierarchy.

Insurance and intermediaries receivables

The valuation of these assets follows the Solvency II fair value hierarchy. There is no difference between the Solvency II valuation and the GFRS 102 valuation.

Property, plant & equipment held for own use

Property, plant & equipment are held at fair value following the Solvency II level 2 and level 3 of the fair value hierarchy.

There is no difference between the Solvency II valuation and the GFRS 102 valuation of these assets.

Cash and cash equivalents

This consists of highly liquid cash holdings held and valued at their actual balances. There is no difference between the Solvency II valuation and the GFRS 102 valuation of these assets.

Receivables (trade, not insurance)

The valuation of these assets follows the Solvency II fair value hierarchy. There is no difference between the Solvency II valuation and the GFRS 102 valuation.

Any other assets, not elsewhere shown

The valuation of these assets follows the Solvency II fair value hierarchy. There is no difference between the Solvency II valuation and the GFRS 102 valuation.

D.2 Technical Provisions

Analysis of Technical Provisions

The table below shows the technical provisions split by line of business and between the best estimate liability and risk margin as at 31 December 2017.

Analysis of Technical Provisions (£000s)	Solvency II Value of Technical Provisions
Class 1 Annuity (BEL)	28,588
Unit Linked liabilities (BEL)	285,493
Non-unit liabilities (BEL)	-1,521
Risk Margin	1,406
Total	**313,966**

- The best estimate Solvency II cash flows are valued on a market consistent basis using UK specific risk free discount rates prescribed by EIOPA;
- Where the best estimate of liabilities for a group of similar contracts is negative, this has been allowed in the Solvency II technical provisions.
- An additional risk margin is required under the Solvency II regulations. This represents the cost of capital that another insurance undertaking would require to take on the Company's insurance liabilities using the 6% EIOPA cost of capital rate.

Main Assumptions

Valuation Discount Rates

The valuation interest rates used to discount the best estimate liability and risk margin is the relevant basic sterling risk free term structure of interest rates as at 31 December 2017 and provided by the European Insurance and Occupational Pensions authority ("EIOPA").

Discount rates rose very slightly during 2017 reflecting the change in the EIOPA term structure of risk free interest rates in the year.

Expenses

Best estimate per-policy expenses have been derived from the latest analysis of actual recurring maintenance expenses and actual volumes and mix of business as at 31 December 2017. The expenses allow for direct and outsourced servicing costs. An allowance has also been made for the fact that STM Life is growing rapidly and that the per policy expense will reduce over the coming years.

Salary related expenses are assumed to inflate in line with the Consumer Price Index and other expenses in line with general inflation expectations using the Retail Price Index as a benchmark.

The per policy expense assumption has reduced as at 31 December 2017 reflecting the new business written in 2017 whilst keeping expense levels fairly constant.

Lapses

Lapse assumptions are derived using actual experience and have regard to current trends in experience and, where appropriate the duration of the contract.

Lapse rates were updated to reflect relevant actual experience over recent years.

Mortality Assumptions

Mortality assumptions are set based on standard actuarial tables of mortality rates. Different rates are assumed for males and females.

Methodology

Technical Provisions are defined as the sum of the Best Estimate of Liabilities and the Risk Margin. The best estimate and risk margin are calculated separately.

Best Estimate of Liabilities

The Company has a data warehouse from which individual policy data is extracted and validated for completeness and accuracy. This data is used to calculate the Technical Provisions and Solvency Capital Requirement and has passed an appropriate level of controls.

The best estimate of insurance liabilities is calculated on a policy by policy basis for all contracts accepted on risk at the valuation date using a cash flow approach and generally accepted actuarial practices. The calculations generate probability weighted cashflows for each monthly time period within a policy's contract boundary. The cash flows are discounted using the EIOPA risk free yield curve and thus allow appropriately for the time value of money.

If the present value of future cash flows on a contract gives rise to a negative best estimate of liabilities, this has been allowed.

Risk Margin

The total risk margin is calculated as the sum of the present values of the cost of capital rate applied to the SCR of a reference undertaking, willing to take on the Company's insurance portfolio, in each future year until the obligations are extinguished and there is no remaining SCR. The future SCRs are modelled using a permitted simplification whereby the SCR is assumed to be proportional to the projected best estimate of liabilities for each group of similar contracts. If a contract has a negative best estimate of liabilities, projected policy volumes are used to run off the SCR.

The risk margin has been calculated by applying the Company's capital requirements arising under the standard formula SCR Life Risk Moduleas well as the a subset of the Counterparty Risk Module directly to the reference undertaking without adjustment. Market risk and remaining counterparty risk are assumed to be fully hedged.

Uncertainty in the Technical Provisions

Uncertainty arises from actual experience being different to the assumptions used in the calculation of the best estimate of liabilities. The most significant source of uncertainty is lapse rates. In particular this affects the BEL non-unit reserve.

D.3 Other Liabilities

There are no other liabilities on a Solvency II basis.

E Capital Management

E.1 Own funds

Comparatives

Figures as at 31 December 2017 and 2016 are shown in the following sections.

Objective, policies and processes for managing own funds

The Company is a wholly owned subsidiary ultimately of the STM Group. Own funds belong to the Shareholder. The Company aims to manage its funds such that there is an appropriate margin of own funds over the solvency capital requirement at all times. This is monitored formally through the Risk and Compliance Committee on a quarterly basis and more regularly through review of key market and demographic assumptions.

Own funds represent the excess of assets over liabilities and are invested in cash and other assets, fixed interest sovereign and corporate debt. Overall, the assets aim to generate positive returns for shareholders subject to an acceptable level of risk, compliance with regulatory requirements and the required level of liquidity.

Business planning is performed annually, covering a three-year projection period and is reported in the Company's Own Risk and Solvency Assessment.

Own Funds classified by tiers

Own funds are classed as Tier I capital as they are retained earnings and are shown in the table below.

Solvency II Balance Sheet (£M)		2017
Assets		320.7
Best Estimate Liabilities	312.6	
Risk Margin	1.4	
Total Liabilities		314.0
Eligible Own Funds to cover SCR and MCR		**6.7**

Solvency II Balance Sheet (£M)		2016
Assets		243.8
Best Estimate Liabilities	238.1	
Risk Margin	2.0	
Total Liabilities		240.1
Eligible Own Funds to cover SCR and MCR		**3.7**

E.2 Solvency and Capital Requirement and Minimum Capital Requirement

The amount of Solvency Capital Requirement ("SCR") and Minimum Capital Requirement("MCR") are shown in the table below.

	2017	£M	2016
Solvency Capital Requirement	3.4		2.4
Minimum Capital Requirement*	3.25		3.3

*The MCR 31 December 2017 was equal to £3.25m being the absolute minimum capital requirement.

Solvency Capital Requirement Split by Risk Module

The Company uses the standard formula as set out in the Solvency II Directive Article 230 to calculate the SCR and does not use any undertaking specific parameters.

The table below sets out the net basic SCR for each of the risk modules after diversification within risk module.

The risk module capital requirements are calculated without using simplifications.

Solvency Capital Requirement (£000s)	2017	2016
Market Risk	2,111	62
Counterparty Risk	282	1,311
Underwriting Risk (Life)	1,355	861
Diversification Benefit	-740	-475
Basic SCR	**3,008**	**1,759**
Operational Risk	1,074	655
Reported SCR	**3,442**	**2,414**

Minimum Capital Requirement

The components of the MCR calculation are shown below. The absolute floor of the MCR is prescribed by EIOPA as €3.7M for an insurer with long term liabilities. This equates to £3.25m in UK sterling using the exchange rate for year end 2017 as advised by the GFSC.

Overall MCR calculation	£M
SCR	3.4
MCR cap (45% of SCR)	1.5
MCR floor (25% of SCR)	0.9
Absolute floor of the MCR	3.25
MCR	**3.25**

E.3 Use of Standard Equity Risk Sub-module

Not Applicable.

E.4 Differences between Standard Formula and internal model

The Company uses the Standard Formula to assess its Solvency Capital Requirement.

E.5 Compliance with MCR and SCR

The Company has performed a full valuation at the end of each quarter during 2017. In the intervening periods, key risk factors are regularly monitored to identify whether they remain within tolerance levels.

APPENDICES

Appendix 1 Quantitative Reporting Templates

The following Quantitative Reporting Templates (QRTs) are required for the SFCR. All figures are presented in thousands of pounds with the exception of ratios that are in decimal. Please note that totals may differ from the component parts due to rounding.

QRT Ref	QRT Template name
S.02.01.02	Balance Sheet
S.05.01.02	Premiums, claims and expenses
S.05.02.01	Premiums, claims and expenses by country
S.12.01.02	Life and Health SLT Technical Provisions
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