Company Number 06127279

ROTHESAY LIFE LIMITED

STRATEGIC REPORT, DIRECTORS' REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2015

Strategic Report

The Directors present their Annual Report and the audited Consolidated Financial Statements for Rothesay Life Limited ('RLL') registered number 06127279, which together with its subsidiary Rothesay Assurance Limited ('RAL') makes up the Rothesay Group ('RL Group'). The Consolidated Financial Statements are presented for the year ended 31 December 2015. Comparative information has been presented for the year ended 31 December 2014.

1. Principal Activities

RLL has been established on the core pillars of high-tech and sophisticated risk management, conservative investment philosophy, continuous innovation to meet clients' needs, and excellence in delivery.

RLL was established in 2007 and has grown to be one of the leading and largest providers of regulated insurance solutions in the UK market for pensions de-risking, with over £18 billion of insurance contracts executed. This now includes the acquisition of annuity books from insurers via reinsurance with the expectation that this will be followed by a Part VII transfer.

The Company's business strategy is focused around three key areas:

i) Protect our in-force balance sheet to ensure that our obligations to policyholders can be met.
ii) Grow through writing value-driven new business.
iii) Safeguard our brand and culture.

2. Operational highlights

RLL has delivered a strong performance in 2015 which included these key highlights:

- Generated IFRS profit before tax of £356m and increased assets under management to £15.4bn.
- Completed the successful acquisition of a £1.2bn block of in-force individual annuities business from Zurich UK Life.
- Originated total new business of £3.5bn.
- Maintained a low-risk investment and longevity hedging strategy which, combined with disciplined underwriting, increased economic capital surplus by £34m to £964m.
- Executed £2.4bn of longevity reinsurance hedges.
- Transferred the long-term business of RAL into RLL, under a Scheme of Transfer pursuant to Part VII of the Financial Services and Markets Act 2000.

With the Zurich transaction, RLL has now acquired annuities using all forms and structures:

- Buy ins and buy outs.
- Reinsurance followed by Part VII Transfer, and
- Strategic acquisitions of life companies.

3. Review of 2015 and looking ahead

Bulk Purchase Annuity markets

2015 was a very strong year with volumes estimated to have exceeded £11bn. The pension buy in and buy-out market remains strong with a number of large transactions in the pipeline for 2016 despite low interest rates. The Board and Management expect volumes to match or exceed 2015 due to:

- Greater clarity on pricing and capacity from insurers post Solvency II implementation.
- A number of transactions were delayed, partly because of Solvency II, and should be completing during 2016.

Strategic Report (continued)

3. Review of 2015 and looking ahead (continued)

Reinsurance market

With the implementation of Solvency II, managing annuity business has become increasingly challenging, particularly for multi-line insurers who have non-core legacy annuity books. A number of UK insurers (and indeed foreign insurers with UK subsidiaries) do not have pro-active annuity strategies and may look to divest their legacy annuity books to release capital to redeploy into other lines of business (e.g. unit linked or protection) or other territories. Some insurers may look to do this for both their existing books of business as well as in connection with buying closed blocks in the future (i.e. when acquiring closed blocks in the future, the acquirer might seek to subsequently sell the associated annuity business).

Such transactions will generally take the form of reinsurance with other specialist annuity insurers such as RLL, followed subsequently by a Part VII transfer. The £1.2bn Zurich deal we completed in 2015 is a prime example of such transaction, with more likely to follow over 2016-2017.

Mergers & Acquisitions

RLL has successfully completed two major acquisitions. RLL have the expertise, experience and competence to acquire annuity liabilities in all forms – whether that is through buy-ins/buy outs, reinsurance or acquisitions. We believe Solvency II may result in major European insurers re-evaluating their core business strategies and we would expect a number of them to consider divesting business units and blocks of policies. Our shareholders remain supportive of both organic and inorganic growth and are confident of the management team's ability to integrate businesses successfully. We will continue to evaluate and pursue strategic M&A opportunities that meet our return targets and growth objectives.

Key Performance Indicators

Set out below are RLL's financial key performance indicators ('KPIs'). The Board and management have adopted the metrics for measuring RLL's aggregate performance and solvency. These metrics form an important part of RLL's business model and ongoing financial management.

	31 December 2015 £m	31 December 2014 £m
IFRS profit before tax	356	260
Operating Profit	381	279
New Business Premiums	3,492	1,397
Economic capital	2,018	1,689
Economic capital coverage	192%	223%
Assets under Management	15,356	12,842

IFRS profit before tax is our primary measure of profitability, capturing all recurring and non-recurring items and in particular market fluctuations which have a direct impact on distributable reserves and capital. IFRS profit before tax has increased by 37% to £356m, reflecting the strong performance in new business origination and cautious investment.

Operating Profit before tax is a measure of profitability capturing new business profit, in-force profit and assumption changes, but excluding market fluctuations and exceptional expenses. Operating profit increase by 37%, also reflecting our new business origination success.

New business sales are a key indicator of the RL Group's growth and realisation of its strategic objectives. New business sales include premiums written as bulk annuities and reinsurance.

Strategic Report (continued)

3. Review of 2015 and looking ahead (continued)

Key Performance Indicators (continued)

Economic capital coverage represents management's internal risk-based capital on a best estimate basis. The RL Group holds capital resources of £2,018m in excess of best estimate liabilities as at 31 December 2015, £329m increase since 2014 despite writing £3.5bn of new business.

Assets under Management ('AUM') measure the total financial investments, including cash. As at 31 December 2015, the RL Group held assets of £15.4bn, an increase of £2.5bn. This figure can be derived from the Consolidated Statement of Financial Position as shown in the table below:

	31 December 2015 £m	31 December 2014 £m
Total assets	25,508.3	21,874.8
Less reinsurance assets	(273.6)	(288.7)
Less payables and financial liabilities	(9,878.3)	(8,743.8)
Assets under Management	**15,356.4**	**12,842.3**

4. Strategy

RLL has been established on the core pillars of high-tech and sophisticated Risk Management, conservative Investment philosophy, continuous innovation to meet clients' needs, and excellence in delivery.

Our existing clients include the pension schemes and members associated with such blue chip companies as British Airways, Civil Aviation Authority, General Motors, GKN, InterContinental Hotels, Philips, Rank, RSA and Zurich.

We apply a conservative, economic-capital based approach to our business and attempt to avoid unrewarded and unnecessary risk to safeguard our balance sheet and use surplus capital for growth. We pursue growth by focusing on quality – not just volume – of new business. We execute transactions across the full spectrum of organic and inorganic opportunities by targeting business that offers the most attractive risk-adjusted reward.

We build our business on a foundation of long-term relationships and avoid short-term opportunism. We focus on retaining the best and most relevant talent to ensure we can maintain our excellence in delivery to our customers, clients, counterparties and partners.

Our strategy can be further explored using the five key areas of New Business Origination, Underwriting, Investment Management, Risk and Capital Management and Operations and Administration.

New Business Origination

We focus on selecting transactions that offer the most attractive returns taking into account the associated risks and capital required. We are not a league table driven company and deals are chosen on their individual merit. As a result, new business volumes are likely to vary from year to year.

Our team of experienced insurance and pension professionals are experts in their field and our new business origination team has been at the forefront of innovation. We are particularly pleased to have been awarded Risk Manager of the year 2016 by Pensions Age.

Strategic Report (continued)

4. Strategy (continued)

New Business Origination (continued)

The RL Group's wholesale annuity proposition encompasses 3 main structures:

- **Pension Buy-ins.** Pension schemes acquire a bulk annuity policy from Rothesay Life Limited which insures pension benefit payments due to a specified portion of members. The scheme holds the policy as an investment. This type of transaction is often a first step towards a pension buy-out.
- **Pension Buy-outs.** Pension schemes acquire a bulk annuity policy from Rothesay Life Limited which insures all pension benefit payments due to all existing members and subsequently dissolves the scheme entirely. The bulk annuity converts into individual polices for each underlying member and the pension scheme no longer exists.
- **Reinsurance.** Insurance company enters into a reinsurance contract with Rothesay Life Limited which insures a specified block of annuity obligations they have previously acquired. Reinsurance is often followed by a full legal transfer of the underlying annuities to Rothesay Life Limited under a court-approved Part VII Transfer.

Underwriting

We adopt a meticulous approach to underwriting which involves evaluating and quantifying the key risks associated with acquiring pension annuity liabilities ahead of completion.

Our underwriting team comprises actuarial, pensions, operational, trading, investment and legal expertise, all of whom have extensive experience in their respective areas. We operate an integrated asset-liability risk model and benefit from sophisticated computer systems which allow all pension liability acquisitions to be assessed real time using prevailing market conditions and investment opportunities. This approach allows us to be opportunistic where we see value and reactive to client needs, but also protects the balance sheet by ensuring consistent quality of origination.

In addition to underwriting of financial risks, our specialist operations, administration and legal team conduct extensive due diligence consistent with the highest standards in the industry in advance of execution to both quantify and mitigate operational and data-related risks.

Investment Management

RLL's £15.4bn asset portfolio is managed in-house by a specialist investment team (the exception being the use of cash funds) whose primary objective is to earn secure returns by investing in low risk assets that benefit from collateral, hedging arrangements or other security and extract value from illiquidity. Investment management is integrated with underwriting, risk and capital management.

Strategic Report (continued)

4. Strategy (continued)

Distinct Investment approach

The RL Group's annuity liabilities are long-term in nature and we back them using fixed income instruments. Our primary focus is on ensuring that the assets we invest in are secure through both their inherent credit-worthiness and additional structural features. We minimise credit risk by investing in an optimal combination of liquid, low-risk government bonds, less liquid highly-secured or collateralised investments and cash:

- **Secured investments**: 41% of the portfolio is invested in secured lending against property or other collateral. Many of these investments are bespoke where very high levels of collateral have been negotiated and returns are generated through liquidity premium.
- **Infrastructure:** 7% of the portfolio is invested in regulated infrastructure such as water, energy and transportation. These investments are typically long-dated and backed by ring-fenced low-risk income streams.
- **Government and Supranational Bonds:** 41% of the portfolio is invested in low risk government bonds, supranational bonds or quasi-sovereign bonds. This portion of the portfolio backs our very long-dated cashflows but is also available to meet collateral calls and cash requirements.
- **Cash:** 3% of the portfolio is invested in immediately realisable cash investments.

RLL adopts a market consistent approach to reserving for residual credit risks as they arise and adopts a dynamic strategy of monitoring and re-hedging these risks daily.

Collateral and Liquidity Management

A large amount of the portfolio is, by design, highly secured, but less liquid. In order to address this, we both manage the collateral held against those investments and also hold substantial liquidity buffers at all times to protect the firm against potential liquidity calls. To achieve this, RLL operates a maximum liquidity outflow ('MLO') framework which stress-tests and reports liquidity continually to ensure sufficient cash and liquid securities (primarily gilts) are available at all times to meet obligations. In addition, we stress test collateral backing investments to ensure security is not compromised due to market moves. These positions are overseen by dedicated treasury operations and a trading desk.

Strategic Report (continued)

4. Strategy (continued)

Industry Leading Expertise

RLL's Investment function is almost entirely in-house (the exception being the use of cash funds). Our team consists of origination, structuring, legal, trading, risk, modelling, operations and capital expertise. We have built the teams by hiring talent from the financial services industry to focus on core coverage areas of real estate, infrastructure, structured finance and government.

Operating the team in-house is critical to the success of the business given it ensures:

- Assets and liabilities are managed in an integrated manner.
- Regulatory capital and risk are a dynamic consideration in decision making.
- Investment opportunities feed into new business underwriting real-time which reduces uncertainly of anticipated returns.

The Company's key asset management principles are:

(i) Integrate asset and liability management.
(ii) Minimise outright credit risk through collateral, credit protection or other structural security.
(iii) Lock-in investment return and earn illiquidity premium.
(iv) Manage and mark collateral daily to minimise counterparty risks.
(v) Maintain sufficient liquidity buffer at all times.

Risk & Capital Management

RLL's risk management principles are driven by the key objectives for the business: to make timely payments to policyholders over a very long-term, to produce stable IFRS earnings and dividend cashflows from in-force business, and to limit policyholders' and investors' downside risk.

Risk Management

To best achieve these objectives, we adopt a low-risk approach to hedging and investment, which necessarily involves:

- A daily mark-to-market valuation approach for all assets and liabilities.
- A risk limit framework which ensures the stability of the earnings and solvency position of the business. Limits exist in relation to market, counterparty, demographic and longevity risks and are sized with reference to our overall risk appetite and capital position.
- A reserving approach for un-hedged risks which aims to ensure that reserves calibrate to the market price of hedging those risks. This enables management to dynamically risk hedge the portfolio based on early market indicators, without reducing expected investment returns.

Framework: RLL monitors and controls exposures through a robust risk and control framework which encompasses the management of both in-force business and new business underwriting:

- Integrated system infrastructure which captures all assets and liabilities centrally and provides us with the capability to report and monitor risk daily at both the portfolio and the individual transaction level.
- Close co-ordination of underwriting, reinsurance, investment and risk hedging functions ensures risk management is central to all aspects of the business, and that new business pricing reflects latest market conditions, hedging costs, investment opportunities as well as comprehensive liability analysis.
- An independent risk and capital management control function provides continuous monitoring of risk exposures and daily attribution of profit and loss, providing timely information to management and enabling dynamic risk based decision making.

Strategic Report (continued)

4. Strategy (continued)

Risk Management (continued)

Governance: The day-to-day risk management is overseen by the Working Level Risk Committee, consisting of relevant senior managers within a delegated risk management framework. This committee reviews all material new investment, hedging or liability transactions.

The Board has overall responsibility for the management of the exposure to risks and is supported through the Audit Committee and the Board Risk Committee. The memberships of these committees consist of Non-Executive and Executive Directors. These committees ensure that the management of the business is conducted within the delegated risk framework from the main Board.

Risk Management in practice

RLL's three primary risks are liquidity risk, investment risk and longevity risk. In order to meet the objectives we set ourselves to produce stable earnings and limit downside risk to the in-force business, we adopt a conservative approach to both:

- **Liquidity Risk:** Given our extensive use of hedging and our investment in illiquid assets, it is important that RLL closely manages liquidity to ensure that we are able to make payments as they fall due and are able to post collateral under our derivative contracts as markets conditions change. We mitigate liquidity risk by holding sufficient cash and Gilts to meet the stresses defined in our risk management policy.
- **Investment Risk:** We undertake asset investment decisions with the primary objective of ensuring the projected returns that can be generated are secure and sustainable for the term of the policyholder reserves. When acquiring assets, we seek to minimise potential losses from default through the use of physical or structural security, or through implied or explicit sovereign support. In some instances credit hedging instruments are also used.
- **Longevity Risk:** We mitigate the risk of life expectancy extending through extensive use of reinsurance. To achieve this, we work with a diversified group of global insurance counterparties and enter into highly collateralised arrangements which reduce RLL's exposure to longevity risk by 77%.

Capital Management under Solvency I

Up until 31 December 2015, the RL Group was required to hold sufficient capital to meet the greater of the economic capital requirement (which is consistent with the Individual Capital Assessment but using a lower probability of default) and the regulatory Pillar 1 position. In practice it was the Pillar 1 requirement which was more onerous. As at 31 December 2015, RLL had capital surplus of £808.8m (2014: £493.8m RAL and RLL combined) giving a Pillar 1 capital ratio of 244% (2014: 204%).

On an economic capital basis, economic capital has increased from £1.7bn as at 31 December 2014 to £2.0bn as at 31 December 2015 compared to a capital requirement that has increased from £759m to £1,054m. In percentage terms the RL Group's economic capital coverage has fallen from 223% to 192%. Economic capital solvency is unchanged by the introduction of Solvency II.

Capital Management under Solvency II

From 1 January 2016, the previous solvency regime was replaced by Solvency II. Under Solvency II we are required to hold the greater of the capital required under the new Pillar 1 framework and the capital required under our own economic capital models, Pillar 2. As expected, the capital required for RLL under the new Pillar 1 exceeds that required under own economic capital models, consistent with our position under the previous solvency regime.

Under Solvency II Pillar 1, we are required to hold sufficient assets to meet:

- RLL's technical provisions being:
  - The liabilities of RLL calculated on a Best Estimate Basis (the 'BEL');
  - The cost of transferring non-hedgeable risks (known as the Risk Margin), plus

Strategic Report (continued)

4. Strategy (continued)

Capital Management under Solvency II (continued)

- The capital required to meet a 1 in 200 year stress (calculated on a prescribed basis and known as the solvency capital requirement or 'SCR').

Capital in excess of that required to meet the technical provisions is known as Own Funds.

As part of the transitional arrangements in relation to the introduction of Solvency II, RLL is permitted to take credit for transitional solvency relief which amortises linearly to zero over the next 16 years. The solvency relief was calculated as the difference between the technical provisions under Solvency II and the BEL under Solvency I Pillar 2. Given the improvement in the Solvency I Pillar 1 position over the second half of 2015, transitional solvency relief is insufficient to ensure that the solvency position of RLL on 1 January 2016 was the same as under the previous solvency regime.

The Pillar 1 capital surplus (Own Funds) for RLL under Solvency II on 1 January 2016 is £1,904m giving a coverage ratio of 158%.

As noted above, the transitional solvency relief amortises over sixteen years. Over the same period, the risk margin associated with business in force on 31 December 2015 is also projected to reduce. Projections show that over half of the amortisation of the transitional solvency relief will be met from the reduction in the risk margin.

It is worth noting that even without transitional solvency relief, RLL would be able to cover its Solvency II capital requirements.

New business will be priced to allow for the additional capital required under the Solvency II regime without transitional capital relief.

Matching adjustment: For most insurance business, the BEL must be discounted using a prescribed risk-free discount rate. However firms with illiquid liabilities such as annuity business can apply to discount these illiquid liabilities using the risk free rate plus what is known as the 'matching adjustment'. The matching adjustment is broadly equivalent to the liquidity premium that can be earned on the illiquid assets held to back illiquid liabilities.

RLL was successful in its application to use the matching adjustment and credit has been taken for the matching adjustment in the BEL numbers. From 1 January 2016, RLL is operating two separate funds – a matching adjustment fund and a non matching adjustment fund. The matching adjustment fund holds almost all of the single premium insurance business and sufficient qualifying assets to meet the associated BEL and risk margin. Regular premium business, the remaining single premium business and all of the remaining assets are held in the non-matching adjustment fund.

Partial internal model: Under Solvency II, insurers have the option of calculating the SCR either using the prescribed basis (the 'standard formula') or applying to use their own internal model. RLL is in the process of applying to use its own model for calculating the SCR in relation to credit risk but intends using the standard formula for all other risks (a 'partial internal model'). RLL is applying to use a partial internal model to ensure that the allocation of capital to investment is consistent with the low risk inherent in the types of highly secured and collateralised investments which are core to RLL's investment strategy. Approval of the partial internal model is unlikely to significantly change RLL's initial capital position under Solvency II but will ensure that RLL's capital position evolves appropriately under Solvency II as RLL makes new investments.

Strategic Report (continued)

5. Principal Risks and Uncertainties

The RL Group operates a low-risk business model that is supported by a robust risk management framework that ensures risks are well understood and controlled. This is facilitated by daily systematic quantification of all risks and a culture that promotes the importance of risk management. Integral to this is a thorough understanding and articulation of the RL Group's risk exposures. Determining the prevailing risk landscape within the RL Group allows Management, the Board Risk Committee and the Board to assess the appetite for each emerging risk and to ensure that all are quantifiable and managed consistently with our appetite to risk.

The RL Group's strategy is to acquire annuity liabilities from pension schemes and other insurance companies.

Exposure to the market risks associated with annuities is significantly hedged with financial instruments, whilst the longevity risk sourced is partly ceded to reinsurers when favourable opportunities are identified. The RL Group seeks investment opportunities in line with a high security, low credit risk investment strategy and counterparty credit risk is managed through structural credit mitigants.

An overview of the principal risk associated with the business including an outline of how they are each managed is provided below:

Interest Rate Risk: RLL invests in fixed income securities in order to back its annuity obligations to policyholders. Interest rate exposures arise due to movements in future expectations of interest rates to the extent that the market value of assets is not sufficient to meet the present value of the annuity obligations.

RLL hedges its exposure, allowing for netting across its investment assets and insurance liabilities, by entering into a portfolio of interest rate swaps. The portfolio is constructed by analysing the sensitivity of all investment assets and insurance liabilities to movements in each of the underlying market instruments used to derive the swap curve. A portfolio of interest rate swaps can then be constructed which replicates these sensitivities. In this way RLL can mitigate the risk to changes in the level, slope and curvature of the swap curve. Monitoring and re-hedging occur on a daily basis.

Inflation Rate Risk: A proportion of RLL's annuity payments are linked to published inflation indices (e.g. UK RPI, UK CPI) and may be subject to caps and floors. Inflation rate exposure therefore arises due to movements in future expectations of inflation rates to the extent that the market value of assets is not sufficient to meet the present value of the annuity obligations.

RLL hedges its net exposure by analysing the sensitivity of all investment assets and insurance liabilities to the movements in each of the underlying market instruments and constructing a portfolio of inflation swaps that replicate these sensitivities.

In this way, RLL can mitigate the risk to changes in the level, scope, curvature and volatility of the inflation swap curve. Monitoring and re-hedging occur on a daily basis.

Exchange Rate Risk: Although RLL principally operates in the UK with the vast majority of assets and liabilities denominated in GBP, a small proportion of RLL's pension obligations and investment assets are denominated in EUR or USD.

RLL hedges its net asset/liability currency exposure back to GBP by entering into a portfolio of exchange rate swaps which also match the term of the exposure. The portfolio is constructed by analysing the sensitivity of all investment assets and insurance liabilities to movements in the exchange rates between GBP and each of the currencies to which RLL is exposed. Monitoring and rehedging occur on a daily basis.

Credit Default Risk: RLL seeks investment opportunities including government debt, government guaranteed debt, supranational debt, corporate debt, secured debt and secured loans. Therefore RLL is exposed to credit default risk.

Strategic Report (continued)

5. Principal Risks and Uncertainties (continued)

Credit Default Risk (continued)

The investment strategy pursued seeks to minimise credit default risk and lock in an illiquidity premium, which is achieved in a number of ways:

- Investing in low risk asset classes such as government guaranteed bonds,
- Investing in asset classes with security and other structural mitigation which protects RLL against loss in the event of a borrower default, including over-collateralisation, and
- Limiting outright credit risk through the use of credit derivative hedges. The resulting asset and accompanying hedge package provide a residual rate of return with lower risk.

Our expertise is weighted toward structuring, legal and collateral management skills, which allows us to accumulate an asset base for which few fundamental credit assessments are required. Monitoring and re-hedging of RLL Group's credit exposure occurs on a daily basis.

Counterparty Default Risk: RLL utilises longevity reinsurance and OTC derivative transactions to efficiently manage risk across the portfolio. Reinsurance transactions are structured as unfunded longevity swaps. Examples of OTC derivatives use include the purchase of credit protection on bonds held in negative basis packages, interest rate and inflation delta hedging and also the hedging of inflation volatility risk. RLL is therefore exposed to the failure of these counterparties.

All such contracts are subject to daily margining requirements to ensure changes in their fair value are appropriately collateralised. Where there is residual gap risk, the value of each contract is adjusted to reflect their credit riskiness. Furthermore, we look to further reduce our exposure by diversifying counterparties and purchasing credit protection.

Insurance Risk: The projection of annuity obligations used for pricing and reserving requires a number of actuarial assumptions to be made. Similar to other bulk annuity providers, the performance of RLL's business will primarily depend on the actual experience of mortality rates and mortality trends. Systemic changes in mortality rates could arise, for example, from a cure for a major disease (e.g. cancer) being found in the near term. Such a cure may have a limited immediate impact on mortality rates, as time is required for a cure to be trialled, brought to market and widely adopted, however it could have significant impact on longer-term expectations of mortality rates.

These insurance risks are mitigated through strict underwriting criteria and the use of reinsurance when favourable opportunities are identified. Assumptions utilised in the projections are determined using recent historic experience, rating models or reinsurance pricing. Given the nature of the larger bulk annuities that RLL writes, the assumptions used can be derived specifically from the population under consideration.

To date, all reinsurance contracts entered by the RL Group have been implemented through the use of unfunded longevity swaps where no initial premium outlay is required. Under a longevity swap, the reinsurer will pay the RL Group the actual experienced annuity obligations in exchange for a fixed fee schedule payable by the RL Group. 77% longevity risk was hedged as at 31 December 2015.

Liquidity Risk: A lack of liquidity within the business may both prevent RLL from being able to pay annuity obligations as amounts fall due, and also may limit RLL's ability to satisfy collateral calls as they arise. Such outcomes will clearly limit the ability of RLL to continue as a going concern and write new business.

RLL's Liquidity Policy requires sufficiently liquid assets to be held in order to meet collateral outflows in extreme market conditions to ensure that sufficient liquid assets are held to satisfy collateral calls. RLL assumes conservative instantaneous market shocks to a range of parameters and measure both the impact on the value of assets held which may be used to satisfy collateral posting requirements and also movements in the value of derivatives which may require collateral to be posted to derivative counterparties (Maximum Liquidity Outflow or 'MLO'). The liquidity position of RLL under such a stress is continually monitored. While a material liquidity buffer exists, ongoing monitoring also allows mitigating actions to be taken at an early stage if required.

Strategic Report (continued)

5. Principal Risks and uncertainties (continued)

Operational Risk: RLL is exposed to operational risk, which is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. In particular, this includes the failure of key outsourcing arrangements, business disruption, fraud and the loss of key management.

This definition also includes legal risk and reputational risk, as RLL considers reputational risk critical to its franchise and therefore has adopted this broad definition of operational risk.

The process through which RLL Group's operational risk universe is determined and subsequent estimates of frequency and severity are assessed is captured in the Operational Risk Policy document. This process safeguards the ongoing improvement of the control environment and ensures that operational risk is identifiable and mitigated as RLL continues to grow.

RLL is reliant on the use of external parties to provide some services, for example policyholder administration for the bulk arrangements and annuitized schemes with JLT and Towers Watson. As part of Goldman Sachs' divestment of 64% of the parent company to Blackstone, GIC and MassMutual in 2013, the RL Group has undertaken a separation project. Goldman Sachs still provides certain systems and processes support under a service agreement. The RL Group is therefore exposed to the potential failure of these outsourcing partners. All risk management and high value functions are managed in-house in order to mitigate this risk and to ensure direct oversight.

Regulatory Risk: A change in the regulatory, legal or political environment may have consequences on the RL Group's Business model, operations and financials. The RL Group is subject to financial regulation in the UK and the UK regulatory framework that applies to life insurance companies, in particular the RL Group is required to comply with capital adequacy requirements.

Although the Solvency II regime has now been implemented, it remains subject to future amendments to improve its operation and to better align approaches across Europe. In addition, RLL's application to use a partial internal model is dependent on PRA approval.

The Solvency II Pillar I balance sheet is more sensitive to interest rates and inflation than the IFRS balance sheet due to the inclusion of the risk margin in the calculation of technical provisions. As the RL Group currently hedges close to the IFRS balance sheet against movements in interest rates and inflation, the Solvency II Pillar I balance sheet remains sensitive to changes in interest rates and inflation. In particular, a fall in interest rates or an increase in inflation would lead to a deterioration in the Solvency II Pillar I balance sheet.

In 2015 the UK government announced a number of regulatory changes in relation to the introduction of secondary annuity market, allowing annuitants to sell their policies to third parties. Full implementation of the rules is expected by April 2017. Whilst this will have operational implications for RLL, sale of a policy does not impact the benefits provided.

RLL now has over 62,000 individual policyholders and is therefore exposed to conduct risk.

RLL maintains ongoing dialogue with the relevant regulators and industry bodies in order to ensure ongoing compliance and the ability to react quickly to any unanticipated changes.

Political Risk: In the event that the UK were to vote in favour of exiting the European Union, it is likely that there would be a period of increased market volatility. The negotiations surrounding any exit are likely to take a significant amount of time and it is then unclear what scope or appetite the UK government would have to amend the UK regulatory framework that applies to life insurance companies.

Strategic Report (continued)

6. Statement of Going Concern Viability

In accordance with provision C.2.2 of the 2014 revision of the Corporate Governance Code, the Board of Directors of RL Group have assessed the prospect of the RL Group over a longer period than the twelve months required by the 'Going Concern' provision. The Board of Directors conducted this review for a period of three years, which is consistent with the RL Group's strategic business plan and Own Risk Solvency Assessment (ORSA), which also covers a three-year period. The three-year strategic business plan and ORSA considers the RL Group's new business volume, projected revenue and earnings, cost and expenses, leverage, capital coverage and other key financial ratios. These and other metrics are subject to sensitivity analyses which involves evaluating the metrics under various upside and downside scenarios. Based on the results of this analysis, the Board of Directors have a reasonable expectation that the RL Group will be able to continue in operation and meets its liabilities and obligations as they fall due over the three-year period of the assessment.

7. Date of authorisation of issue

The Financial Statements were authorised for issue by the Board of Directors on 22 March 2016.

ON BEHALF OF THE BOARD

A. Loudiadis

Chief Executive Officer

22 March 2016

Report of the Directors

The Directors present their Annual Report and the audited consolidated Financial Statements for Rothesay Life Limited, registered number 06127279, (the 'Company' or RLL) for the year ended 31 December 2015. Comparative information has been presented for the year ended 31 December 2014.

1. Results

The consolidated results for RL Group's for the year are set out in the Consolidated Statement of Comprehensive Income on page 18.

2. Dividends

On 2 November 2015 the Directors recommended the payment of an interim dividend to its parent company Rothesay Holdco UK Limited (RHUK) of £130m (2014: £nil). The Directors recommended no final ordinary dividend in respect of the year (2014: £nil). Please refer to Note 26 to the Financial Statements for additional detail.

3. Directors

The Directors of the Company who served throughout the year and to the date of this report, except where noted, were:

Name	Appointed	Resigned
S. Q. Abbas		
R. D. A. Berliand	31 March 2015	
R. A. De Beir Jarratt		
G. Earle	30 March 2015	
R. King		
N. Kheraj	9 March 2015	
A. Loudiadis		
D. McDonogh		
D. G. Paterson		31 December 2015
C. D. Pickup		
W. J. Robertson	4 January 2016	
K. Satchell		

4. Qualifying Third Party Indemnities

The Articles of Association of the Company provide for the Directors and officers of the Company to be indemnified in respect of liabilities incurred as a result of their office. The Company also provides certain protections for RL Group Directors and senior management against personnel financial exposure that they may have incurred in their capacity as such. These include qualifying third party indemnity provisions (as defined under section 234 of the Companies Act 2006) in force for the benefit of the Directors of the RL Group during the year.

Report of the Directors (continued)

5. Disclosure of Information to Auditors

In the case of each of the persons who are Directors of the Company at the date when this report was approved:

- so far as each of the Directors are aware, there is no information relevant to the audit of which the Company's auditors are unaware; and
- each of the Directors has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any information relevant to the audit and to establish that the Company's auditors are aware of that information.

6. Independent Auditors

The Company has passed Elective Resolutions in accordance with the Companies Act 1985 to dispense with the holding of annual general meetings, the laying of Financial Statements before general meetings and the annual reappointment of auditors. PricewaterhouseCoopers LLP will, accordingly, continue in office as auditors of the Company pursuant to Section 487(2) of the Companies Act 2006 and paragraph 44 of Schedule 3 to the Companies Act 2006 (Commencement No. 3 Consequential Amendment, Transitional Provisions and Savings) Order 2007.

The RL Group intends to invite tenders for the 2017 audit contract during 2016.

7. Statement of Directors' Responsibilities

The Directors are responsible for preparing the Strategic Report, Report of the Directors and the Financial Statements in accordance with applicable laws and regulations. Company law requires the Directors to prepare Financial Statements for each financial year. Under that law the Directors have prepared the Financial Statements in accordance with IFRSs as adopted by the EU. Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that year. In preparing these Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the EU have been followed, subject to any material departures disclosed and explained in the Financial Statements; and
- prepare the Financial Statements on the going concern basis unless is inappropriate to presume that the Company will continue in business.

Report of the Directors (continued)

7. Statement of Directors' Responsibilities (continued)

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the Financial Statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Legislation in the United Kingdom governing the preparation and dissemination of Financial Statements may differ from legislation in other jurisdictions.

8. Internal Control and Risk Management Systems

The RL Group has established internal control and risk management systems in relation to the process for preparing Consolidated Financial Statements. The key features of these internal control and risk management systems are:

- The Risk function and management conduct checks on internal controls quarterly.
- The Internal audit function reviews and assesses controls on an ongoing basis.
- Management regularly monitors and considers developments in accounting regulations and best practice in financial reporting, and where appropriate, reflects developments in the Consolidated Financial Statements. The Audit Committee is kept appraised of such developments.
- The RL Group's results are subject to various levels of review by management.
- The Audit Committee and the Board review the draft Consolidated Financial Statements. The Audit Committee receives reports from management and the external auditors on significant judgements, changes in accounting policies, changes in accounting estimates and other pertinent matters relating to the consolidated financial statements.
- The Financial Statements are subject to external audit.

9 Date of Authorisation of Issue

The Financial Statements were authorised for issue by the Board of Directors on 22 March 2016.

ON BEHALF OF THE BOARD

A. Loudiadis

Chief Executive Officer

22 March 2016

Independent Auditors' report to the members of ROTHESAY LIFE LIMITED

Report on the Financial Statements

Our Opinion

In our opinion:

- Rothesay Life Limited's Group and Company Financial Statements (the 'Financial Statements') give a true and fair view of the state of the Group's and Company's affairs as at 31 December 2015 and of the Group's profit and the Group's and the Company's cash flows for the year then ended;
- the Group Financial Statements have been properly prepared in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the European Union;
- the Company Financial Statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the Financial Statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

What we have audited

The Financial Statements, included within the Strategic Report, Directors' Report and Financial Statements (the 'Annual Report'), comprise:

- the Consolidated and Company Statement of Financial Position as at 31 December 2015;
- the Consolidated Statement of Comprehensive Income for the year then ended;
- the Consolidated and Company Cash Flow Statement for the year then ended;
- the Consolidated and Company Statement of Changes in Equity for the year then ended; and
- the notes to the Financial Statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and IFRSs as adopted by the European Union and, as regards the Company Financial Statements, as applied in accordance with the provisions of the Companies Act 2006.

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinion on Other Matters Prescribed by the Companies Act 2006

In our opinion, the information given in the Strategic Report and the Report of the Directors for the financial year for which the Financial Statements are prepared is consistent with the Financial Statements.

Other Matters on which we are required to Report by Exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- We have not received all the information and explanations we require for our audit; or
- Adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- The Company Financial Statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Independent Auditors' report to the members of ROTHESAY LIFE LIMITED (continued)

Responsibilities for the Financial Statements and the Audit

Our responsibilities and those of the Directors
As explained more fully in the Statement of Directors' Responsibilities set out on pages 13-14, the Directors are responsible for the preparation of the Financial Statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of Financial Statements involves
We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the RL Group's and the Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the Financial Statements.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the Financial Statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited Financial Statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Lee Clarke

Lee Clarke (Senior Statutory Auditor)
For and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
22 March 2016

(a) The maintenance and integrity of the Rothesay Life Limited website 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 financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2015	Note	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Income			
Gross premiums written	2	3,763,630	1,679,335
Premiums ceded to reinsurers		(562,146)	(435,179)
Net Premiums Written		**3,201,484**	**1,244,156**
Investment return	4	(114,632)	1,778,936
Total Revenue		**3,086,852**	**3,023,092**
Expenses			
Claims and change in insurance contract liabilities		(3,199,527)	(3,228,526)
Change in the reinsurers' share of insurance contract liabilities		557,476	533,182
Net Claims Incurred and Change in Insurance Contract Liabilities	5	**(2,642,051)**	**(2,695,344)**
Operating expenses	6	(76,882)	(61,321)
Finance costs	7	(11,927)	(6,443)
Total Operating Expenses		**(88,809)**	**(67,764)**
Profit Before Tax		**355,992**	**259,984**
Income tax expense	10	(71,042)	(57,085)
Profit for the Year		**284,950**	**202,899**

All income and expenses related to continuing operations.

The Consolidated Statement of Comprehensive Income includes all income and expenses for the year. RL Group has no items required to be reported in other comprehensive income, therefore a separate Comprehensive Income Statement has not been presented.

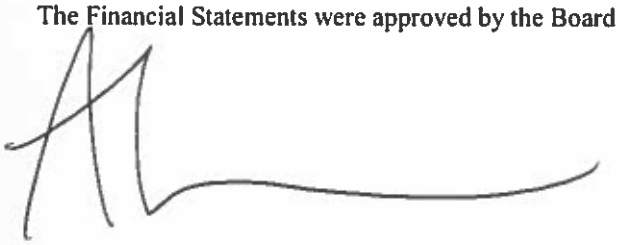
Notes 1 – 32 form an integral part of these Financial Statements.

Consolidated Statement of Financial Position

As at 31 December 2015	Note	31 December 2015 £000s	31 December 2014 £000s
Assets			
Property, Plant and Equipment	13	1,988	1,524
Financial investments	14	24,591,613	20,989,390
Reinsurance assets	16	273,632	288,654
Accrued interest and prepayments	17	164,980	130,816
Receivables	18	392,498	357,733
Cash and cash equivalents	19	83,582	106,711
Total Assets		**25,508,293**	**21,874,828**
Equity and Liabilities			
Share capital	24	183,901	183,901
Share premium	25	199,854	199,854
Retained earnings	25	659,812	504,862
Total Equity		**1,043,567**	**888,617**
Liabilities			
Insurance contract liabilities	20	14,207,475	12,105,682
Payables and financial liabilities	21	9,878,339	8,743,766
Borrowings	22	348,770	100,000
Deferred tax liabilities	23	2,792	3,429
Accruals and deferred income		27,350	33,334
Total Equity and Liabilities		**25,508,293**	**21,874,828**

Notes 1 – 32 form an integral part of these Financial Statements.

The Financial Statements were approved by the Board of Directors on 22 March 2016 and signed on its behalf by:



A. Loudiadis

Chief Executive Officer

22 March 2016

Company number 06127279

Consolidated Statement of Changes in Equity

For the year ended 31 December 2015

	Share Capital £000s	Share Premium £000s	Retained Earnings £000s	Total Equity £000s
As at 1 January 2015	183,901	199,854	504,862	888,617
Profit for the year	-	-	284,950	284,950
Dividends paid	-	-	(130,000)	(130,000)
As at 31 December 2015	**183,901**	**199,854**	**659,812**	**1,043,567**

For the year ended 31 December 2014

	Share Capital £000s	Share Premium £000s	Retained Earnings £000s	Total Equity £000s
As at 1 January 2014	155,121	112,379	301,963	569,463
Profit for the year	-	-	202,899	202,899
Shares issued	28,780	87,475	-	116,255
As at 31 December 2014	**183,901**	**199,854**	**504,862**	**888,617**

Consolidated Cash Flow Statement

For the year ended 31 December 2015	Note	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Cash Flows from Operating Activities			
Profit for the financial year		284,950	202,899
Adjustments for Non Cash Movements in Net Profit for the Year			
Depreciation		474	-
Interest income		(350,968)	(270,325)
Interest expense		11,927	6,442
Other adjustments		-	7,988
Tax expense		71,679	57,085
Net (Increase)/Decrease in Operational Assets			
Financial investments		(3,602,223)	(6,649,323)
Reinsurance asset		15,022	(124,329)
Receivables		(35,507)	(278,983)
Net Increase/(Decrease) in Operational Liabilities			
Insurance contract liabilities		2,101,793	2,464,431
Financial liabilities		1,230,119	4,026,346
Other payables		(100,403)	575,181
Deferred tax		(637)	-
Accruals		(11,345)	9,734
Net cash (used)/generated from Operating Activities		**(385,119)**	**27,146**
Interest paid		(6,565)	(4,349)
Interest received		316,804	277,747
Tax paid		(66,081)	(42,733)
Net Cash (Outflows)/Inflows from Operating Activities		**(140,961)**	**257,811**
Cash Flows from Financing Activities			
Proceeds from issuance of debt		248,770	-
Proceeds from issue of ordinary share capital (including share premium)		-	116,255
Dividends paid		(130,000)	-
Net Cash Inflows from Financing Activities		**118,770**	**116,255**
Cash Flows from Investing Activities			
Acquisition of plant, equipment and intangibles		(938)	(1,524)
Acquisitions of subsidiaries (net of cash acquired)		-	(354,814)
Net Cash Outflows from Investing Activities		**(938)**	**(356,338)**
Net (decrease)/increase in cash and cash equivalents		(23,129)	17,728
Cash and cash equivalent at 1 January		106,711	88,983
Cash and Cash Equivalents at 31 December	19	**83,582**	**106,711**

Company Statement of Financial Position

As at 31 December 2015	Note	31 December 2015 £000s	31 December 2014 £000s
Assets			
Investment in subsidiaries	12	2,669	421,381
Property, plant and equipment	13	1,988	1,524
Financial investments	14	24,588,952	18,338,666
Reinsurance assets	16	273,632	234,052
Accrued interest and prepayments	17	164,980	95,588
Receivables	18	392,498	326,364
Cash and cash equivalents	19	83,574	86,631
Total Assets		**25,508,293**	**19,504,206**
Equity and Liabilities			
Share capital	24	183,901	183,901
Share premium	25	199,854	199,854
Retained earnings	25	659,812	330,122
Total Equity		**1,043,567**	**713,877**
Liabilities			
Insurance contract liabilities	20	14,207,475	9,341,887
Payables and financial liabilities	21	9,878,339	9,314,452
Borrowings	22	348,770	100,000
Deferred tax liabilities	23	2,792	2,690
Accruals and deferred income		27,350	31,300
Total Equity and Liabilities		**25,508,293**	**19,504,206**

Notes 1 – 32 form an integral part of these Financial Statements.

The Financial Statements were approved by the Board of Directors on 22 March 2016 and signed on its behalf by:

A. Loudiadis.

Chief Executive Officer

22 March 2016

Company number 06127279

Company Statement of Changes in Equity

For the year ended 31 December 2015

	Share Capital £000s	Share Premium £000s	Retained Earnings £000s	Total Equity £000s
As at 1 January 2015	183,901	199,854	330,122	713,877
Profit for the year	-	-	279,690	279,690
Dividends received	-	-	180,000	180,000
Dividends paid	-	-	(130,000)	(130,000)
As at 31 December 2015	**183,901**	**199,854**	**659,812**	**1,043,567**

For the year ended 31 December 2014

	Share Capital £000s	Share Premium £000s	Retained Earnings £000s	Total Equity £000s
As at 1 January 2014	155,121	112,379	301,963	569,463
Profit for the year	-	-	28,159	28,159
Shares issued	28,780	87,475	-	116,255
As at 31 December 2014	**183,901**	**199,854**	**330,122**	**713,877**

Company Cash Flow Statement

For the year ended 31 December 2015	Note	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Cash Flows from Operating Activities			
Profit for the year		279,690	28,159
Adjustments for Non Cash Movements in Net Profit for the Year			
Depreciation		474	-
Change in insurance contract liabilities on Part VII		2,628,506	-
Realisation of gains on assets transferred in on Part VII		(3,050,707)	-
Impairment of subsidiary		418,712	-
Interest income		(276,548)	(214,587)
Interest expense		11,163	6,225
Tax expense		69,388	6,821
Net (Increase)Decrease in Operational Assets			
Financial investments		(1,652,175)	(7,037,817)
Reinsurance asset		28,827	(69,727)
Receivables		99,406	(255,239)
Net Increase/(Decrease) in Operational Liabilities			
Insurance contract liabilities		2,168,676	2,388,581
Financial liabilities		(1,079,160)	4,715,458
Other payables		(212,634)	571,653
Deferred tax		(508)	-
Accruals		(12,114)	9,733
Net cash (used)/generated from Operating Activities		**(579,004)**	**149,260**
Interest paid		(5,801)	(4,092)
Interest received		241,360	196,862
Tax paid		(17,393)	(37,732)
Net Cash (Outflows)/Inflows from Operating Activities		**(360,838)**	**304,298**
Cash Flows from Financing Activities			
Proceeds from issuance of debt		248,770	-
Proceeds from issue of ordinary share capital (including share premium)			116,255
Dividends paid		(130,000)	-
Dividends received		180,000	-
Net Cash Inflows from Financing Activities		**298,770**	**116,255**
Cash Flows from Investing Activities			
Acquisition of plant, equipment and intangibles		(938)	(1,524)
Acquisitions of subsidiaries (net of cash acquired)		-	(421,381)
Cash inflow on Part VII		59,949	-
Net Cash Inflows/(Outflows) from Investing Activities		**59,011**	**(422,905)**
Net decrease in cash and cash equivalents		(3,057)	(2,352)
Cash and cash equivalent at 1 January		86,631	88,983
Cash and Cash Equivalents at 31 December	19	**83,574**	**86,631**

Notes to the Financial Statements

Note 1 – Accounting Policies

(a) General Information

RLL is a registered company incorporated in the United Kingdom. The Company's registered office and principal place of business is Level 25, The Leadenhall Building, 122 Leadenhall Street, London, EC3V 4AB.

(b) Basis of Preparation

The Consolidated Financial Statements of the RL Group and those of the Company have been prepared and approved by the Directors in accordance with IFRS as adopted by the EU and those parts of the Companies Act 2006 applicable to those reporting under IFRS. The Financial Statements have been prepared on a going concern basis as disclosed within Note 6 of the Strategic Review.

The consolidated and separate Financial Statements of the Company are presented in sterling (£) rounded to the nearest thousand (£000s) except where otherwise stated. The separate Statement of Financial Position of the Company is presented on page 22.

The RL Group presents its Statement of Financial Position broadly in order of liquidity. An analysis regarding recovery or settlement more than twelve months after the year end is presented in the notes.

Assets and liabilities are offset and the net amount reported in the Statement of Financial Position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expenses are not offset in the income statement unless required or permitted by IFRS.

(i) Adoption of New or Amended Standards

The RL Group has adopted the following new standards and changes to existing standards which are relevant to the RL Group's operations, and became effective for financial years beginning on or after 1 January 2015. These amendments have all been endorsed by the EU.

IFRS 3 Business Combinations

IFRS 3 has been amended to clarify that IFRS 3 does not apply to the accounting for the formation of a joint arrangement under IFRS 11. The amendment also clarifies that the scope exemption only applies in the financial statements of the joint arrangement itself.

The standard has also been amended to clarify that an obligation to pay contingent consideration which meets the definition of a financial instrument is classified as a financial liability or as equity, on the basis of the definitions of IAS 32, 'Financial instruments: Presentation'. The standard is further amended to clarify that all non-equity contingent consideration, both financial and non-financial, is measured at fair value at each reporting date, with changes in fair value recognised in profit and loss. The amendments have no impact on the RL Group Financial Statements.

IFRS 13 Fair Value Measurement

The amendment clarifies that the portfolio exception in IFRS 13, which allows an entity to measure the fair value of a group of financial assets and financial liabilities on a net basis, applies to all contracts (including non-financial contracts) within the scope of IAS 39 or IFRS 9. The amendment has no impact on the RL Group Financial Statements.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(b) Basis of Preparation (continued)

(i) Adoption of New or Amended Standards (continued)

IAS 40 Investment Property

IAS 40 has been amended to clarify that IAS 40 and IFRS 3 are not mutually exclusive. The guidance in IAS 40 assists preparers to distinguish between investment property and owner occupied property. Preparers also need to refer to the guidance in IFRS 3 to determine whether the acquisition of an investment property is a business combination. The amendment has no impact on the RL Group Financial Statements.

IAS 19 Employee benefits

This amendment applies to plans that require employees or third parties to contribute towards the cost of benefits. The amendment does not affect the accounting for voluntary contributions. The amendment has no impact on the RL Group Financial Statements.

IFRS 2 Share based payment

This amendment clarifies the definition of a 'vesting condition' and separately defines 'performance condition' and 'service condition'. The amendment has no impact on the RL Group Financial Statements.

IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets

Both standards have been amended to clarify how the gross carrying amount and the accumulated depreciation are treated where an entity uses the revaluation model. The amendment has no impact on the RL Group Financial Statements.

IFRS 8 Operating Segments

The standard is amended to require disclosure of the judgements made by management in aggregating operating segments. This includes a description of the segments which have been aggregated and the economic indicators which have been assessed in determining that the aggregated segments share similar economic characteristics. The standard is further amended to require a reconciliation of segment assets to the entity's assets when segment assets are reported. The amendment has no impact on the RL Group Financial Statements, because all of the RL Group's business is in a single segment.

IAS 24 Related party disclosures

The standard is amended to include, as a related party, an entity that provides key management personnel services to the reporting entity or the parent of the reporting entity. The reporting entity is not required to disclose the compensation paid by the management entity to the management entity's employees or directors, but it is required to disclose the amounts charged to the reporting entity by the management entity for services provided. The amendment has no impact on the RL Group Financial Statements.

(ii) New or Revised Standard Not Yet Effective

The following new, revised standards, in issue, were not yet effective, or in some cases not yet endorsed by the EU. The RL Group has not early adopted any of these standards.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(b) Basis of Preparation (continued)

(ii) New or Revised Standard Not Yet Effective (continued)

IFRS 14 Regulatory deferral accounts

IFRS 14 has been issued, an interim standard on the accounting for certain balances that arise from rate-regulated activities. IFRS 14 is only applicable to entities that apply IFRS 1 as first-time adopters of IFRS. It permits such entities, on adoption of IFRS, to continue to apply their previous GAAP accounting policies for the recognition, measurement, impairment and de-recognition of regulatory deferral accounts. The RL Group does not expect the standard to impact on the RL Group Financial Statements.

IFRS 11 Joint arrangement

IFRS 11 provides specific guidance on accounting for the acquisition of an interest in a joint operation that is a business. The amendments address diversity in the practice related to the accounting for these transactions. The RL Group does not expect the standard to impact on the RL Group Financial Statements.

IAS 16 Property plant and equipment and IAS 38 Intangible Assets

Both IAS 16 and IAS 38 have been amended to clarify when a method of depreciation or amortisation based on revenue may be appropriate. The RL Group does not expect the amendment to impact on the RL Group Financial Statements.

IAS 27 Separate Financial Statements

The IASB has amended IAS 27 to restore the option to use the equity method to account for investments in subsidiaries, joint ventures and associates in an entity's separate financial statements. The RL Group does not expect the amendment to impact on the RL Group Financial Statements.

IFRS 10 Consolidated Financial Statements

Amendments were published to IFRS 10 to clarify the application of the consolidation exception for investment entities and their subsidiaries. The exception from preparing consolidated financial statements is available to intermediate parent entities which are subsidiaries of investment entities. The RL Group does not expect the amendment to impact on the RL Group Financial Statements.

IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates

The IASB published amendments to IFRS 10 and IAS 28 which clarify the accounting treatment for sales or contribution of assets between an investor and its associates or joint ventures. The RL Group does not expect the amendment to impact on the RL Group Financial Statements.

IAS 1 Presentation of Financial Statements

The amendments clarify guidance in IAS 1 on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies. The amendments form a part of the IASB's Disclosure Initiative, which explores how financial statement disclosures can be improved. The RL Group does not expect the amendment to have a material impact on the RL Group Financial Statements, except perhaps from a presentation perspective.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(b) Basis of Preparation (continued)

(ii) New or Revised Standards Not Yet Effective (continued)

IFRS 15 Revenue from Contracts with Customers

IFRS 15, as issued in May 2014, establishes a new five-step model that will apply to revenue earned from a contract with a customer, regardless of the type of revenue or industry. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue and will be applied using the following five steps:

1. Identify the contract(s) with a customer
2. Identify the performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to the performance obligations in the contract
5. Recognise revenue when (or as) the Company satisfies a performance obligation.

This new revenue standard, which is jointly issued by IASB and the United States Financial Accounting Standards Board (FASB), is applicable to all companies and will supersede the current revenue recognition requirements under IFRS.

IFRS 15 will be effective for IFRS reporters for the first interim period within annual reporting periods beginning on or after 1 January 2017 and will allow early adoption. The new standard will affect most entities that apply IFRS or US GAAP. The areas expected to provide the greatest impact are: transfer of control, variable consideration, licences, time value of money, contract costs and disclosures. The RL Group is still assessing the impact on the companies within the RL Group but note that insurance is specifically excluded.

IFRS 9 Financial instruments

The final version includes requirements on the classification and measurement of financial assets and liabilities. It also includes an expected credit losses model that replaces the incurred loss impairment model used currently. This version also includes the final hedging part of IFRS 9 that was issued in November 2013. The RL Group awaits further guidance before assessing the impact of the standard.

(iii) Annual Improvements 2012-2014 Cycle

These improvements are effective from 1 January 2016 and are not expected to have a material impact on the RL Group. They include: IFRS 5 Non-Current Assets held for sale and discontinued operations, IFRS 7 Financial Instruments: Disclosures, IAS 19 Employee Benefits and IAS 34 Interim Financial Reporting.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(c) Basis of Consolidation

The Consolidated Financial Statements comprise the Financial Statements of the RL Group as at 31 December each year.

RLL's subsidiaries are fully consolidated from the date of acquisition, being the date on which the RL Group obtains control, and continue to be consolidated until the date when such control ceases. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the Statement of Comprehensive Income from the date the RL Group gains control until the date the RL Group ceases to control the subsidiary. The Financial Statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions and dividends, are eliminated in full.

Control is achieved when the RL Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the RL Group controls an investee if and only if the RL Group has;

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee)
- Exposure, or rights, to variable returns from its involvement with the investee.
- The ability to use its power over the investee to affect its returns.

The RL Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control.

(d) Contract Classification

The RL Group has classified all its policyholder contracts as insurance contracts in accordance with IFRS 4 Insurance Contracts. Insurance contracts are contracts which transfer significant insurance risk to the insurer at the inception of the contract.

As permitted by IFRS 4 Insurance Contracts, the assets and liabilities of the RL Group's insurance contracts are accounted for using generally accepted accounting principles within the industry. The RL Group applies the modified statutory solvency basis ('MSSB') of reporting as set out in the revised Statement of Recommended Practise (SORP) issued by the Association of British Insurers (ABI) in November 2005 (amended in December 2006).

i) Premiums

The RL Group writes both single and regular premium business. Single (single payment of premium which covers the life of the policy) and regular premiums (payments of premium made regularly over the duration of the policy) are recognised when they fall due.

ii) Claims

Annuity payments are accounted for when they fall due for payment. Surrenders are accounted for when paid or, if earlier, on the date when the policy ceases to be included within the calculation of the long term business provision. Death claims and all other claims are accounted for when notified.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(d) Contract Classification

iii) Insurance Contract Liabilities

Insurance contract liabilities are determined by the RL Group's actuaries using methods and assumptions recommended by the actuarial function holder of RLL and prior to the Part VII transfer the actuarial function holder of Rothesay Assurance Limited ('RAL') and approved by the Board, and using recognised actuarial methods with due regard to the actuarial principles laid down in Directive 2002/83/EC. They are calculated using the statutory solvency basis required to comply with the reporting requirements under the Financial Services and Markets Act 2000 and in accordance with the SORP on Accounting for Insurance Business issued by the ABI in December 2005 and revised in December 2006. The RL Group seeks to make prudent assumptions relating to expected future experience based on current market conditions and recent experience. The assumptions used incorporate prudent margins to reflect the inherent uncertainty that actual experience may be less favourable than our best estimate.

Insurance Contract Liabilities have been determined using the gross premium method of valuation. They are calculated as the discounted value of projected future claim payments (as determined by reference to the contractual arrangements with policyholders at an individual member level) adjusted for future administration costs and investment management expenses determined using prudent assumptions less the present value of future premiums (a schedule of agreed, guaranteed payments) under the longevity swap arrangements. Projected future claim payments allow for the effects of mortality. Further details of valuation assumptions are produced in Note 20. The administration costs are reflective of recent costs and expenses budgeted for the future

In accordance with PRA valuation regulations set out in the Prudential Sourcebook for Insurers, the RL Group recognises negative mathematical reserves on its regular premium longevity risk transfer arrangements subject to the PRA's restrictions on the level of such reserves.

(e) Acquisition Costs

The costs of acquiring new business are expensed during the financial year in which they are incurred.

(f) Reinsurance

Long term business is ceded to reinsurers under contracts to transfer part or the insurance risk associated with the underlying insurance contracts. Such contracts are accounted for as insurance contracts provided the risk transfer is significant.

The amounts that will be recoverable from reinsurers are estimated based upon the gross provisions, having due regard to collectability. The recoverability of reinsurance recoveries is assessed having regard to market data on the financial strength of the reinsurance company. The reinsurers' share of claims incurred, in the profit and loss account, reflects the amounts received or receivable from reinsurers in respect of claims paid or incurred during the year. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised in the Consolidated Statement of Comprehensive Income as 'Premiums Ceded to Reinsurers' when due.

Collateral received on Reinsurance assets is accounted for in line with collateral received on Financial investments (see Note 1 (m)).

Reinsurance assets are reviewed for impairment at each reporting date, or more frequently when an indication of impairment arises during the financial reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the Reinsurance asset that the RL Group may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the RL Group will receive from the reinsurer. Any impairment loss is recorded in the Consolidated Statement of Comprehensive Income.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(g) Investment Return

Investment return comprises all interest income on financial investments at fair value through profit and loss, realised investment gains and losses and movements in unrealised gains and losses, as well as expenses directly related to investments executed during the year.

Dividends on money market securities held in collective investment schemes are included as investment income on the date the units are created. Interest is accounted for on an accruals basis.

Realised gains and losses on investments carried at fair value are calculated as the difference between net sales proceeds and purchase price. Movements in unrealised gains and losses on investments represent the difference between the fair value at the Consolidated Statement of Financial Position date and their cost.

(h) Finance Costs

Finance costs comprise finance costs and interest payable on financial liabilities. Expenses are accounted for on an accruals basis.

(i) Operating Leases

A lease is classified as an operating lease if it does not transfer substantially all the risk and rewards incidental to ownership.

Payments made under operating leases, net of any investments received from the lessor, are charged to profit and loss on a straight line basis over the term of the lease. When the lease includes a rent free period, the lessee recognises the aggregate benefit of the incentive as a reduction of rental expense over the lease term on a systematic basis.

(j) Investments in Subsidiary Undertakings

Investments in subsidiary undertakings are stated at cost less provision for impairment in the Company's Financial Statements.

(k) Property, Plant and Equipment

Equipment is stated at cost less accumulated depreciation and accumulated impairment losses. Depreciation is calculated on a straight basis over the useful life of the following classes of assets:

Computer Equipment: 3 years

Furniture and Fittings: 5 years

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(l) Financial Investments

Financial Investments are classified, at initial recognition, as financial investments at fair value through profit or loss, with the exception of receivables, cash and accrued interest which are carried at amortised cost.

Financial Investments at Fair Value Through Profit and Loss

Financial investments at fair value through profit or loss are both financial investments held for trading and financial investments designated upon initial recognition at fair value. Financial investments at fair value through profit or loss are carried in the Consolidated Statement of Financial Position at fair value with net changes in fair value presented in investment income. Financial investments include collective investment schemes, government and agency obligations, derivative assets, corporate debt, and collateralised agreements and financing.

Derecognition

A financial investment (or, where applicable, a part of a financial investment or part of a group of similar financial investments) is primarily derecognised (i.e. removed from the RL Group's Consolidated Statement of Financial Position) when:

- The rights to receive cashflows from the investment have expired; or
- The RL Group has transferred its rights to receive cashflows from the asset or has assumed an obligation to pay the received cashflows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the RL Group has transferred substantially all the risks and rewards of the asset, or (b) the RL Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the investment.

When the RL Group has transferred its rights to receive cashflows from an investment or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the investment, nor transferred control of the investment, the RL Group continues to recognise the transferred investment to the extent of the RL Group's continuing involvement. In that case, the RL Group also recognises an associated liability. The transferred investment and the associated liability are measured on a basis that reflects the rights and obligations that the RL Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the RL Group could be required to repay.

(m) Collateralised Agreements and Financing

Collateralised agreements (securities purchased under agreements to re-sell and deposits placed as collateral for stock borrowed) and collateralised financing (securities sold under agreements to repurchase and deposits received as collateral for stock loans) are treated as collateralised financing transactions and are carried at fair value through profit and loss under the fair value option. The collateral can be in the form of cash or securities. Cash collateral is recognised/derecognised when received/paid. Collateral posted by the RL Group in the form of securities is not derecognised from the Consolidated Statement of Financial Position, whilst collateral received in the form of securities is not recognised on the Consolidated Statement of Financial Position. If collateral received is subsequently sold, the obligation to return the collateral and the cash received are recognised in the Consolidated Statement of Financial Position.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(n) Fair Value

The fair value of a financial instrument is the amount that would be received on sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e. the exit price. Financial investments are marked to bid prices and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs. Fair value gains or losses are included in investment income.

The best evidence of fair value is a quoted price in an active market. If listed prices or quotations are not available, fair value is determined by reference to prices for similar instruments, quoted prices or recent transactions in less active markets, or internally developed models that primarily use, as inputs, market based or independently sourced parameters, including but not limited to interest rates, volatilities, equity or debt prices, foreign exchange rates, credit curves and funding rates. The fair value of certain financial investments and financial liabilities require valuation adjustments for counterparty credit quality, funding risk, transfer restrictions, illiquidity and bid/offer inputs.

Cash instruments such as corporate debt securities, covered bonds, government and agency obligations and certain money market instruments are valued by verifying to quoted prices, recent trading activity for identical or similar instruments, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations (e.g. indicative or firm) and the relationship of recent market activity to the prices provided from alternative pricing sources. Valuation adjustments are typically made (i) if the cash instrument is subject to regulatory or contractual transfer restrictions and/or (ii) for other premiums and discounts that a market participant would require to arrive at fair value. Valuation adjustments are generally based on market evidence.

Certain cash instruments, including collateralised agreements and financing have one or more significant valuation inputs that are not observable. Absent evidence to the contrary, these instruments are initially valued at transaction price, which is considered to be the best initial estimate of fair value. When a pricing model is used, the model is adjusted so that the model value of the cash instrument at inception equals the transaction price. Subsequently, the RL Group uses other methodologies to determine fair value, which vary based on the type of instrument. Valuation inputs and assumptions are changed when corroborated by substantive observable evidence, including values realised on sales.

The RL Group's derivative contracts consist primary of over the counter ('OTC') derivatives. OTC derivatives are generally valued using market transactions and other market evidence, including market based inputs to models, calibration to market clearing transactions, broker or dealer quotations or other alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations (e.g. indicative or firm) and the relationship of recent market activity to the prices provided from alternative pricing sources.

Where models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of and specific risks inherent in the instrument, as well as the availability of pricing information in the market. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates, loss severity rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, model selection does not involve significant management judgement because outputs of models can be calibrated to market clearing levels.

Certain OTC derivatives are valued using models which utilise inputs that can be observed in the market, as well as unobservable inputs. Unobservable inputs typically include certain correlations as well as credit spreads, that are long dated or derived from trading activity in inactive or less liquid markets. Subsequent to the initial valuation of such derivatives, the RL Group updates the observable inputs to reflect observable market changes. Unobservable inputs are changed when corroborated by evidence such as similar market transactions, third party pricing services and/or broker or dealer quotations or other empirical market data. In circumstances where the RL Group cannot verify the model value by reference to market transactions, it is possible that a different valuation model could produce a materially different estimate of fair value.

Further information on fair value can be found in Note 15.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(o) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method. Transaction costs are amortised over the period of the borrowings.

(p) Taxation

Current Income Tax

Income tax assets and liabilities for the current year and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities, or paid to or recovered from other group companies in respect of group relief surrendered or received. The tax rates and laws used to compute the amount are those that are enacted or substantively enacted by the financial statement date.

Deferred Income Tax

Deferred income tax is provided using the liability method on temporary differences at the financial statement date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax and liabilities are recognised for all taxable temporary differences except:

- When the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit or loss nor taxable profit or loss, and

- In respect of taxable temporary differences associated with investments in subsidiary undertakings, associates and interests in joint ventures, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which to offset them except:

- When the Deferred Income Tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit or loss or the taxable profit or loss; and

- The carrying amount of Deferred Income Tax assets is reviewed at each financial reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each financial reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the financial reporting date.

Deferred income tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred income tax relates to the same taxable entity and the same taxation authority.

Notes to the Financial Statements (continued)

Note 1 – Accounting Policies (continued)

(q) Foreign Currencies

Transactions denominated in foreign currencies are translated into sterling at rates of exchange ruling on the date the transaction occurred. Monetary assets and liabilities denominated in foreign currencies are translated into sterling at rates of exchange ruling at the Financial Statement date. Gains and losses on exchange are recognised in Operating Expenses.

(r) Dividends

Final dividends are recognised in the year that they are approved by the shareholders. Interim dividends are recognised in the year that they are paid. These dividends are debited directly to equity.

Note 2 – Segmental Analysis

All of the RL Group's business risks and returns are within one business segment (i.e. long term insurance business). The RL Group's operations are materially within the United Kingdom. The split between regular premiums (payments of premium made regularly over the duration of the policy) and single premiums (single payment of premium which covers the life of the policy) is disclosed below:

	Regular premiums		Single premiums	
	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Group pension bulk annuities	272,093	273,567	2,334,972	1,405,768
Assumed reinsurance premiums	-	-	1,156,565	-
Total Gross Premiums Written	**272,093**	**273,567**	**3,491,537**	**1,405,768**

During 2015 premiums from three bulk annuity and reinsurance customers each made up more than 10% of the RL Group's total gross written premium (2014: four bulk annuity customers), generating premiums of £3,437.4m (2014: £1,109.7m).

Note 3 – Company Profit

The profit for the financial year of the Company was £279.7m (2014: £28.2m). As permitted by section 408 of the Companies Act 2006, the Company's Statement of Comprehensive Income has not been included in these Financial Statements.

Notes to the Financial Statements (continued)

Note 4 – Investment Return

The RL Group's Investment return includes fair value gains and losses. Interest is included on an accrual basis.

RL Group	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Interest income on financial investments at fair value through profit and loss	350,968	270,321
Unrealised (losses)/gains on financial investments	(924,697)	895,260
Realised gains on financial investments	462,593	564,189
Investment expenses	(3,496)	(7,247)
Gain on acquisition of subsidiary undertaking	-	56,413
Total Investment Return	**(114,632)**	**1,778,936**

Note 5 – Net Claims Incurred and Change in Insurance Contract Liabilities

RL Group	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Claims Paid		
Gross claims paid	(1,056,425)	(700,560)
Reinsurance recoveries	531,244	408,607
Change in the provision for claims outstanding	253	680
	(524,928)	**(291,273)**
Change in Insurance Contract Liabilities		
Gross change in Insurance contract liabilities	(2,143,355)	(2,528,646)
Reinsurance recoveries	26,232	124,575
	(2,117,123)	**(2,404,071)**
Net Claims and Change in Insurance Contract Liabilities	**(2,642,051)**	**(2,695,344)**

Claims paid has increased in 2015 reflecting the growth of the in force book and a partial surrender which arose as a result of restructuring one of our in force contracts to improve its treatment under Solvency II.

Notes to the Financial Statements (continued)

Note 6 – Operating Expenses

The note gives further details of items included in the Operating Expenses section of the Consolidated Statement of Comprehensive Income which have been included in arriving at the profit before tax:

RL Group	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Acquisition costs	52,030	37,960
Administration expenses - recurring	9,763	8,585
Administration expenses - other	15,089	14,776
	76,882	**61,321**

The following items have been included in Administration expenses – other

	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Costs relating to separation project	8,503	4,558
Solvency II expenses	1,703	781
Part VII project	975	577
Reinsurance fees	3,908	7,728
Acquisition of RAL	-	1,132
	15,089	**14,776**

The following items have been included in operating expenses:	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Depreciation	474	-
Operating lease rental expense for office premises	945	420
	1,419	**420**

Notes to the Financial Statements (continued)

Note 7 – Finance Costs

RL Group	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Interest payable on collateral	3,612	1,511
Interest payable on overnight loans	1	23
Interest payable on overdraft	5	-
Interest payable on borrowings	3,353	-
Interest payable on borrowings from affiliates	4,956	4,909
Net Finance Costs	**11,927**	**6,443**

Debt issuance expenses associated with the issue of subordinated loan notes will be recognised over the term of the loan.

Note 8 – Employee Information

All person's involved in the RL Group's operations are employed by a wider group undertaking, RPML. The charges made by RPML for all the services provided (personnel and other) to the RL Group are included in the management fees charged by group undertakings.

Directors' emoluments in respect of qualifying services to the RL Group were as follows:

RL Group	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Directors' Remuneration		
Aggregate emoluments	1,789	1,430
Company pension contributions to money purchase schemes	7	21
	1,796	**1,451**
Highest Paid Director		
Total amount of emoluments	1,295	1,051
Company pension contributions to money purchase schemes	7	6
	1,302	**1,057**

In accordance with the Companies Act 2006, Directors' emoluments above represent the proportion of total emoluments paid or payable in respect of qualifying services. This total does not include the value of equity awards in accordance with the provisions of Schedule 5 of SI 2008/410.

During 2015 Directors also received emoluments for non-qualifying services which were not required to be disclosed.

No Directors have been granted shares in respect of long term incentive schemes. No Directors have exercised options during the year.

Notes to the Financial Statements (continued)

Note 9 – Auditors' Remuneration

Fees paid and payable to the RL Group's auditors are as follows:

RL Group	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Remuneration receivable by the RL Group's auditors for the audit of the consolidated and company financial statements	296	298
Remuneration receivable by the RL Group's auditors for the audit of the financial statements of the Company's subsidiary	110	121
Audit related assurance services	67	147
Total Audit	**473**	**566**
Other assurance services	567	-
Total Fees	**1,040**	**566**

Other assurance services provided in 2015 include assurance in relation to the RL Group's Solvency II balance sheet, a review of the RL Group's internal credit rating function and assurance over the debt prospectus. These services are all in compliance with applicable independence rules and were approved by the Audit Committee.

Note 10 – Taxation

The major components of the income tax expense for the years ended 31 December 2015 and 2014 are:

(a) Tax charged in the income statement

RL Group	Year ended 31 December 2015 £000s	Year ended 31December 2014 £000s
Current income tax:		
UK corporation tax	71,685	57,479
Adjustments in respect of prior years	(6)	-
Total Current Income Tax	**71,679**	**57,479**
Deferred tax:		
Origination and reversal of temporary differences	(437)	(394)
Impact of changes in tax laws and rates	(200)	-
Total Deferred Tax	**(637)**	**(394)**
Total Expense in the Income Statement	**71,042**	**57,085**

Notes to the Financial Statements (continued)

Note 10 – Taxation (continued)

(b) Reconciliation of the total tax charge

The tax expense in the Consolidated Statement of Comprehensive Income for the year and the standard rate of corporation tax in the UK of 20.25% (2014: 21.49%) is reconciled below:

	Year ended 31 December 2015 £000s	Year ended 31 December 2014 £000s
Profit before tax	355,992	259,984
Tax calculated at UK standard rate of corporation tax of 20.25% (2014: 21.49%)	72,088	55,870
Adjustment in respect of prior years	(6)	207
Expenses not deductible for tax purposes	114	14,303
Income not subject to corporation tax	-	(12,115)
Timing differences	(196)	(13)
Impact of changes in tax laws and rates	(212)	-
Utilisation of losses surrendered by group undertakings	(746)	(1,167)
Total Tax Expense Reported in the Consolidated Statement of Comprehensive Income	**71,042**	**57,085**

Note 11 – Investment in Unconsolidated Structured Entities

The RL Group has interests in investments which are classified under IFRS as unconsolidated structured entities. A structured entity is an entity that has been designed so that voting or similar rights are not the dominating factor in deciding who controls the entity, such as when voting rights might relate to administrative tasks only and the relevant activities are directed by means of contractual arrangement. Structured entities include those entities that have restricted activities or a narrow and well-defined objective. These structured entities have not been consolidated as the RL Group does not have the power to affect their returns.

As at 31 December 2015 our total interest in such entities, reflected on the RL Group's Consolidated Statement of Financial Position and classified as financial investments held at fair value through profit or loss, was £2,892m (2014: £1,156m) and for the Company it was £2,892m (2014: £1,156m). The increase in the balance has been driven by increased investment in highly collateralised ground rent loans.

Notes to the Financial Statements (continued)

Note 12 – Investment in Subsidiaries

Subsidiaries

The Financial Statements include the Financial Statements of RLL and the subsidiary listed in the following table:

Group Undertakings	Country of Incorporation	Primary business operation	Held at lower of cost or net realisable value £'000	2015 % equity interest	2014 % equity interest
Rothesay Assurance Limited (Formerly known as MetLife Assurance Limited)	UK	Life insurance	2,669	100%	100%
LT Mortgage Financing Limited	UK	Service Company	-	100%	-

The above subsidiaries are registered in England and Wales.

During the prior year, RLL acquired MetLife Assurance Limited, the UK bulk annuity business of MetLife Inc. MetLife Assurance Limited is now wholly owned by RLL. MetLife Assurance Limited was renamed Rothesay Assurance Limited on 23 June 2014.

On 17 February 2015 LT Mortgage Financing Limited was incorporated as a wholly owned subsidiary of Rothesay Life Limited with 0.01 pence share capital. This Company has remained dormant during 2015.

Note 13 – Property, Plant and Equipment

RL Group and Company

	Computer Equipment £000s	Furniture and Fittings £000s	Total £000s
Cost			
As at 1 January 2015	-	1,524	1,524
Additions	229	709	938
As at 31 December 2015	**229**	**2,233**	**2,462**
Accumulated Depreciation			
As at 1 January 2015	-	-	-
Charge for the year	52	422	474
As at 31 December 2015	**52**	**422**	**474**
Net Book Value			
As at 31 December 2015	**177**	**1,811**	**1,988**
As at 31 December 2014	-	1,524	1,524

As part of the development of fully independent infrastructure and computer systems the RL Group moved into new premises during early 2015. Both Furniture and Fittings and Computer Equipment additions reflect the build out of the office.

Notes to the Financial Statements (continued)

Note 14 – Financial Investments

The RL Group's Financial Investments are grouped in a single category:

	31 December 2015 £000s	31 December 2014 £000s
Financial Investments	24,591,613	20,989,390

This is made up of:

	Current Value	
	31 December 2015 £000s	31 December 2014 £000s
Collective investment schemes	470,388	726,307
Government and agency obligations	6,137,079	5,855,467
Corporate debt	5,792,876	5,076,291
Derivative assets	6,936,656	5,801,994
Collateralised agreements and financing	5,134,880	3,400,828
Certificates of deposit	119,734	128,503
	24,591,613	**20,989,390**

The Company's Financial Investments are grouped in a single category:

	31 December 2015 £000s	31 December 2014 £000s
Financial Investments	24,588,952	18,338,666

This is made up of:

	Current Value	
	31 December 2015 £000s	31 December 2014 £000s
Collective investment schemes	467,727	628,257
Government and agency obligations	6,137,079	4,151,886
Corporate debt	5,792,876	3,596,702
Derivative assets	6,936,656	6,432,490
Collateralised agreements and financing	5,134,880	3,400,828
Certificates of deposit	119,734	128,503
	24,588,952	**18,338,666**

Notes to the Financial Statements (continued)

Note 15 – Fair Value

Determination of Fair Value and Fair Values Hierarchy

The RL Group uses the following hierarchy for determining and disclosing the fair value of Financial Instruments by valuation technique:

- Level 1: inputs are unadjusted quoted prices in active markets to which the RL Group had access at the measurement date for identical unrestricted assets and liabilities,
- Level 2: inputs to valuation techniques are observable either directly or indirectly,
- Level 3: one or more inputs to valuation techniques are significant and unobservable.

Financial Investments and liabilities are measured using valuation techniques based on assumptions that are supported by prices from observable current market transactions and pricing obtained via pricing services. Where prices have not been determined in an active market, the fair values are based on broker quotes and the RL Group's own models whereby the majority of assumptions are market observable.

The following tables shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy for 2015 and 2014:

RL Group 31 December 2015

	Level 1 £000s	Level 2 £000s	Level 3 £000s	Total £000s
Financial investments:				
Collective investment scheme	470,388	-	-	470,388
Government and agency obligations	3,240,711	2,896,368	-	6,137,079
Corporate debt	-	5,610,310	182,566	5,792,876
Derivative assets	-	6,933,679	2,977	6,936,656
Collateralised agreements and financing	-	3,196,132	1,938,748	5,134,880
Certificate of deposits	-	119,734	-	119,734
Total Financial Investments at Fair Value	**3,711,099**	**18,756,223**	**2,124,291**	**24,591,613**
Financial liabilities:				
Derivative financial instrument	-	6,906,402	11,197	6,917,599
Collateralised financing agreements	-	1,886,099	-	1,886,099
Total Financial Liabilities at Fair Value	**-**	**8,792,501**	**11,197**	**8,803,698**

Notes to the Financial Statements (continued)

Note 15 – Fair Value (continued)

RL Group 31 December 2014

	Level 1 £000s	Level 2 £000s	Level 3 £000s	Total £000s
Financial investments:				
Collective investment scheme	726,307	-	-	726,307
Government and agency obligations	3,390,645	2,464,822	-	5,855,467
Corporate debt	-	4,827,882	248,409	5,076,291
Derivative assets	-	5,800,209	1,785	5,801,994
Collateralised agreements and financing	-	3,400,828	-	3,400,828
Certificate of deposits	-	128,503	-	128,503
Total Financial Investments at Fair Value	**4,116,952**	**16,622,244**	**250,194**	**20,989,390**
Financial liabilities:				
Derivative financial instrument	-	5,544,495	6,654	5,551,149
Collateralised financing agreements	-	2,022,430	-	2,022,430
Total Financial Liabilities at Fair Value	**-**	**7,566,925**	**6,654**	**7,573,579**

Company 31 December 2015

	Level 1 £000s	Level 2 £000s	Level 3 £000s	Total £000s
Financial investments:				
Collective investment scheme	467,727	-	-	467,727
Government and agency obligations	3,240,711	2,896,368	-	6,137,079
Corporate debt	-	5,610,310	182,566	5,792,876
Derivative assets	-	6,933,679	2,977	6,936,656
Collateralised agreements and financing	-	3,196,132	1,938,748	5,134,880
Certificate of deposits	-	119,734	-	119,734
Total Financial Investments at Fair Value	**3,708,438**	**18,756,223**	**2,124,291**	**24,588,952**
Financial liabilities:				
Derivative financial instrument	-	6,906,402	11,197	6,917,599
Collateralised financing agreements	-	1,886,099	-	1,886,099
Total Financial Liabilities at Fair Value	**-**	**8,792,501**	**11,197**	**8,803,698**

Notes to the Financial Statements (continued)

Note 15 – Fair Value (continued)

Company 31 December 2014

	Level 1 £000s	Level 2 £000s	Level 3 £000s	Total £000s
Financial investments:				
Collective investment scheme	628,257	-	-	628,257
Government and agency obligations	2,295,129	1,856,757	-	4,151,886
Corporate debt	-	3,348,293	248,409	3,596,702
Derivative assets	-	6,430,705	1,785	6,432,490
Collateralised agreements and financing	-	3,400,828	-	3,400,828
Certificate of deposits	-	128,503	-	128,503
Total Financial Investments at Fair Value	**2,923,386**	**15,165,086**	**250,194**	**18,338,666**
Financial liabilities:				
Derivative financial instrument	-	6,233,604	6,654	6,240,258
Collateralised financing agreements	-	2,022,430	-	2,022,430
Total Financial Liabilities at Fair Value	**-**	**8,256,034**	**6,654**	**8,262,688**

Approximately 9% (2014: 1%) of the total financial assets recorded at fair value are based on estimates and recorded as Level 3 investments. Where estimates are used, these are based on a combination of independent third-party evidence and internally developed models, calibrated to market observable data where possible.

Notes to the Financial Statements (continued)

Note 15 – Fair Value (continued)

The following table shows a reconciliation of the opening and closing recorded amounts in relation to the Level 3 financial instruments recorded at fair value:

RL Group

	Corporate debt £000s	Collateralised agreements £000s	Derivatives £000s	Total £000s
At 1 January 2015	**248,409**	**-**	**(4,869)**	**243,540**
Total gains in the Statement of Comprehensive Income:				
Unrealised gains/(losses)	2,350	-	(3,351)	(1,001)
Realised gains	411	-	-	411
Transfer into Level 3	75	455,754	-	455,829
Transfer out of Level 3	(136,622)	-	-	(136,622)
Purchases/additions/(sales)/(disposals)	67,943	1,482,994	-	1,550,937
At 31 December 2015	**182,566**	**1,938,748**	**(8,220)**	**2,113,094**
At 1 January 2014	**961,890**	**552,767**	**(14,719)**	**1,499,938**
Acquisition at market value	6,942	-	7,474	14,416
Total gains in the Statement of Comprehensive Income:				
Unrealised gains	25,693	-	9,850	35,543
Transfer into Level 3	24,511	-	-	24,511
Transfer out of Level 3	(812,535)	(552,767)	(7,474)	(1,372,776)
Purchases/additions/(sales)/(disposals)	41,908	-	-	41,908
At 31 December 2014	**248,409**	**-**	**(4,869)**	**243,540**

Notes to the Financial Statements (continued)

Note 15 – Fair Value (continued)

Company	Corporate debt £000s	Collateralised agreements £000s	Derivatives £000s	Total £000s
At 1 January 2015	**248,409**	**-**	**(4,869)**	**243,540**
Total gains in the Statement of Comprehensive Income:				
Unrealised gains/(losses)	2,350	-	(3,351)	(1,001)
Realised gains	411	-	-	411
Transfer into level 3	75	455,754	-	455,829
Transfer out of level 3	(136,622)	-	-	(136,622)
Purchases/additions/(sales)/(disposals)	67,943	1,482,994	-	1,550,937
At 31 December 2015	**182,566**	**1,938,748**	**(8,220)**	**2,113,094**
At 1 January 2014	**961,890**	**552,767**	**(14,719)**	**1,499,938**
Total gains in the Statement of Comprehensive Income:				
Unrealised gains	25,693	-	9,850	35,543
Transfer into level 3	24,511	-	-	24,511
Transfer out of level 3	(812,535)	(552,767)		(1,365,302)
Purchases/additions/(sales)/(disposals)	48,850	-	-	48,850
At 31 December 2014	**248,409**	**-**	**(4,869)**	**243,540**

There have been no transfers between Level 1 and Level 2 during the year.

The increase in the amount of assets allocated to Level 3 of the fair value hierarchy when compared to 2014 has been driven by £1,482.9m of ground rent loans executed during 2015 which have been classified as Level 3, in addition, £455.8m of such loans were transferred from Level 2 to Level 3 due to the unavailability of recent external market levels.

Notes to the Financial Statements (continued)

Note 15 – Fair Value (continued)

Sensitivity of Level 3 Financial Instruments Measured at Fair Value to Changes in Key Assumptions

The following table shows the impact on the fair value of Level 3 instruments of using reasonably possible alternative assumptions by class of instrument. Since part of any spread movement is likely to be included in the derivation of the liability discount rate, changes in fair value of assets also impact liabilities. The table below shows the potential impact on profit before tax of the same alternative assumptions:

RL Group and Company

Impact on Financial Assets, Liabilities and PBT	Main Assumptions	Sensitivity	Current FV £000s	2015 Increase/(Decrease) in FV £000s	Increase/(Decrease) in PBT £000s
Financial Assets					
Corporate debt	Discount rate	+50bps interest rate	182,566	(21,808)	(5,596)
		-50bps interest rate	182,566	24,250	6,211
Collateralised financing agreements	Discount rate	+25bps interest rate	1,938,748	(143,669)	(14,248)
		-25bps interest rate	1,938,748	159,653	(15,826)
Derivative assets	Expected defaults	+50bps credit default spread	2,977	1,435	1,435
		-50bps credit default spread	2,977	(1,435)	(1,435)
Financial Liabilities					
Derivative liabilities	Expected defaults	+50bps credit default spread	(11,197)	3,087	3,087
		-50bps credit default spread	(11,197)	(3,087)	(3,087)

Impact on Financial Assets, Liabilities and PBT	Main Assumptions	Sensitivity	Current FV £000s	2014 Increase/(Decrease) in FV £000s	Increase/(Decrease) in PBT £000s
Financial Assets					
Corporate debt	Discount rate	+50bps interest rate	248,409	(23,733)	(7,509)
		-50bps interest rate	248,409	23,733	7,509
Derivative assets	Expected defaults	+50bps credit default spread	1,785	472	472
		-50bps credit default spread	1,785	(472)	(472)
Financial Liabilities					
Derivative liabilities	Expected defaults	+50bps credit default spread	(6,654)	1,099	1,099
		-50bps credit default spread	(6,654)	(1,099)	(1,099)

The fair value of certain debt securities classified as Level 3 instruments is determined using inputs that are not based on observable market data. The valuation model discounts the future cash flows using interest rate swap curves in addition to a spread to reflect the associated credit and liquidity risk. The sensitivities shown above assume all other pricing inputs remain constant.

Notes to the Financial Statements (continued)

Note 16 – Reinsurance Assets

The reinsurers' share of the Insurance Contract Liabilities is as follows:

	RL Group		Company	
	31 December 2015 £000s	31 December 2014 £000s	31 December 2015 £000s	31 December 2014 £000s
Reinsurance of insurance contract liabilities	273,632	288,654	273,632	234,052

Under the outward reinsurance contracts, the RL Group has committed to pay fixed cash flows to the reinsurer for each policy covered. In exchange, the reinsurers will pay cashflows that are linked to the actual longevity of the underlying policies. The contracts are collateralised for changes in longevity expectations and movements in market rates.

An analysis of the movement in Reinsurance of Insurance Contract Liabilities is included in Note 20.

At 31 December 2015 the RL Group conducted an impairment review of the reinsurance assets and found no impairment necessary.

Note 17 – Accrued Interest and Prepayments

	RL Group		Company	
	31 December 2015 £000s	31 December 2014 £000s	31 December 2015 £000s	31 December 2014 £000s
Accrued interest	138,178	117,744	138,178	88,992
Prepaid expenses	26,802	13,072	26,802	6,596
	164,980	**130,816**	**164,980**	**95,588**

Notes to the Financial Statements (continued)

Note 18 – Receivables

RL Group	31 December 2015 £000s	31 December 2014 £000s
Deposits pledged as collateral to third parties	377,651	349,273
Amounts due from group undertakings	11,262	5,570
Amounts due from undertakings with participating interest	-	1,979
Tax receivable	-	16
Other receivables	3,585	895
	392,498	**357,733**

All receivables are due within one year. The fair value of receivables is £392.5m (2014: £357.7m).

The net exposure to certain OTC derivatives is collateralised through cash posted, as per the terms of the OTC contracts. At 31 December 2015, the total cash collateral posted was £377.7m (2014: £349.3m). Further details of the full extent of collateral usage can be found in the credit risk disclosure in Note 28.

Company	31 December 2015 £000s	31 December 2014 £000s
Deposits pledged as collateral to third parties	377,651	317,703
Amounts due from group undertakings	11,262	5,771
Amounts due from undertakings with participating interest	-	1,979
Tax receivable	-	16
Other debtors	3,585	895
	392,498	**326,364**

All receivables are due within one year. The fair value of receivables is £392.5m (2014: £326.4m).

The net exposure to certain OTC derivatives is collateralised through cash, as per the terms of the OTC contracts. At 31 December 2015, the total cash collateral was £377.7m (2014: £317.7m). Further details of the full extent of collateral usage can be found in the credit risk disclosure in Note 28.

Notes to the Financial Statements (continued)

Note 19 – Cash and Cash Equivalents

The cash at bank and in hand of the RL Group and Company at the year end is as follows:

	RL Group		Company	
	31 December 2015 £000s	31 December 2014 £000s	31 December 2015 £000s	31 December 2014 £000s
Cash at bank and in hand	83,582	106,711	83,574	86,631
	83,582	**106,711**	**83,574**	**86,631**

Note 20 – Insurance Contract Liabilities

Key Valuation Assumptions

This note details the assumptions with the greatest impact on the RL Group's insurance contract liability valuations. Note that Insurance contract liabilities include reinsurance inwards, i.e. where the Group has reinsured a third party insurer.

(a) Mortality Assumptions

Mortality bases have been determined separately for each insurance contract. The resulting assumptions are equivalent to using the base mortality and improvement assumptions set out in the table below:

RL Group

	31 December 2015		31 December 2014	
	Males	Females	Males	Females
Base mortality	97.2% S2PMA	97.2% S2PFA	101.8% S1PMA	101.8% S1PFA
Mortality improvements	CMI_2014_M[2.7%]	CMI_2014_F[2.2%]	CMI_2012_M[2.7%]	CMI_2012_F[2.2%]

Company

	31 December 2015		31 December 2014	
	Males	Females	Males	Females
Base mortality	97.2% S2PMA	97.2% S2PFA	103.7% S1PMA	103.7% S1PFA
Mortality improvements	CMI_2014_M[2.7%]	CMI_2014_F[2.2%]	CMI_2012_M[2.7%]	CMI_2012_F[2.2%]

Notes to the Financial Statements (continued)

Note 20 – Insurance Contract Liabilities (continued)

Key Valuation Assumptions (continued)

(a) Mortality Assumptions (continued)

Ultimate mortality has been used in all cases and mortality improvements are applied from 2007 (2014: from 2002).

Recent mortality experience was analysed for each pension scheme (individually or grouped) at the end of 2015 and, where the data was considered statistically credible, the best estimate base mortality assumptions used in the valuation are based on this actual mortality experience. Where the data is not statistically credible, the RL Group has taken into account reinsurance prices and external and proprietary socio demographic models, based on postcode and other factors.

Mortality assumptions are set with reference to standard tables drawn up by the Continuous Mortality Investigation Bureau ('CMIB') of the Institute and Faculty of Actuaries. These tables are based on industry-wide experience. During 2015 base mortality tables were updated to use the CMI S2 series of mortality tables. The update was made to better reflect the shape of mortality and to update the base date from 2002 to 2007.

During 2015 the RL Group transacted funded reinsurance over a block of in payment Zurich Assurance annuities. The lives reinsured are reserved using the CMI 08 series of annuitant mortality tables rather than the S2 series of mortality tables used to value all other pension liabilities as the former is expected to better reflect the shape of mortality for an insured block.

Allowance is made for future improvements in annuitant mortality with reference to statistical analysis of historic rates of mortality improvements, expert judgement of future changes in mortality improvements, industry benchmarking and reinsurance pricing.

Prudent margins are then applied to the demographic basis to reflect the fact that future experience for the schemes may differ from that assumed.

(b) Valuation Rate of Interest

The valuation rate of interest used to discount the cash flows for the purpose of valuing insurance contract liabilities is based on the PRA Pillar 1 regulatory requirements, as modified by a waiver granted by the PRA in 2008 and renewed in 2013 to allow the RL Group to reflect the yield (internal rate of return) on the combined matching assets rather than an average yield based on market value weighted durations. The rate of interest is determined based on the yield obtainable on the basket of assets matching the PRA Pillar 1 mathematical reserves at 31 December 2015.

The result is equivalent to using the valuation discount rate set out in the table below:

	RL Group		Company	
	31 December 2015	31 December 2014	31 December 2015	31 December 2014
Equivalent valuation discount rate	3.21%pa	2.90%pa	3.21%pa	2.93%pa

Notes to the Financial Statements (continued)

Note 20 – Insurance Contract Liabilities (continued)

Key Valuation Assumptions (continued)

(b) Valuation Rate of Interest (continued)

This rate reflects both the prescribed PRA 2.5% prudential margin applied to the risk adjusted internal rate of return obtained on the basket of matching assets and an allowance for investment management expenses of 3bps p.a. (2014: 3bps p.a).

The asset yield used to calculate the valuation discount rate has been reduced to reflect counterparty default risk; where applicable adjusted for the prudent expected recoveries in the event of default. This reduction in yield is determined separately for each individual asset reflecting the risk to the return being achieved on the asset.

The table below shows the average yield deduction at 31 December 2015 and 31 December 2014 by asset category:

Asset Class	RL Group Average yield reduction		Company Average yield reduction	
	2015	2014	2015	2014
UK Government approved securities	0 bps	0 bps	0 bps	0bps
Corporate bonds after allowance for covering credit default swaps	0 bps	0 bps	0 bps	0bps
Secured Lending	6 bps	6 bps	6 bps	6bps
Supranational/Other Sovereign	15 bps	18 bps	15 bps	16bps
Secured Residential Lending	24 bps	33 bps	24 bps	29bps
Infrastructure	83 bps	82 bps	83 bps	80bps
Other	56 bps	31 bps	56 bps	36bps
Overall	**18bps**	**18bps**	**18bps**	**16bps**

Overall, the deduction for counterparty default risk on the assets held by the RL Group is generally lower than the corresponding credit default deduction on a typical unsecured credit portfolio. This is due to either a low probability of default due to government guarantees or expectation of higher recovery in the event of default through collateralisation, recourse to specific assets, credit default swap protection.

Notes to the Financial Statements (continued)

Note 20 – Insurance Contract Liabilities (continued)

Key Valuation Assumptions (continued)

(c) Expenses

An allowance is made for future overhead maintenance expenses following an investigation into the total costs incurred by the RL Group during 2015 and the projected 2016 expenses. As part of this investigation, these costs have been split between acquisition and maintenance expenses. The long term business provisions include an allowance to provide for the expenses payable under the Third Party Administration agreements ('TPA') together with the long term business overhead expenses expressed as an amount per policy. An additional short term maintenance expense overrun provision has been established to provide for expected project costs.

Within these expense provisions, an allowance for future expense inflation has been provided to cover the impact of both salary and price inflation. The future rate of expense inflation is assumed to be RPI (as implied by the RPI swap curve) plus an addition at each duration of 0.25% p.a. (2014: 0.25% p.a.) for the overhead maintenance expenses and an addition at each duration of either 0.25% or 1.00% p.a. (2014: 1.00% p.a.) for the TPA expenses depending on TPA provider.

Other Assumptions

An important actuarial assumption relates to the future rate of escalation of certain benefits, but as the RL Group is holding appropriate matching assets (such as index-linked bonds and inflation-linked swaps with associated caps and floors), the impact on the overall financial position of the RL Group of actual or assumed changes in these rates is relatively small.

A number of other, less financially significant, actuarial assumptions are made in determining the provisions. These assumptions include, inter alia, the proportion of deferred and immediate annuitants assumed to have a dependant eligible for contingent benefits, dependant's age difference and the proportion of deferred annuitants opting to take a proportion or all of their benefit as a lump sum. When deferred annuitants have passed the scheme normal retirement date and have been subject to in depth tracing exercises and yet remain untraced, a prudent allowance has been made for the probability of them retiring in the future. All other individuals who have passed the scheme normal retirement date are assumed to retire immediately.

(d) Movements in Insurance Contract Liabilities

	31 December 2015			31 December 2014		
RL Group	**Insurance Liabilities**	**Reinsurance Assets**	**Net Liabilities**	**Insurance Liabilities**	**Reinsurance Assets**	**Net Liabilities**
	£000s	**£000s**	**£000s**	**£000s**	**£000s**	**£000s**
Carrying amount at 1 January	12,105,682	288,654	**11,817,028**	6,953,306	164,325	**6,788,981**
RAL value at acquisition	-	-	-	2,623,545	-	**2,623,545**
Increase in respect of new business	3,320,026	8,777	**3,311,249**	1,282,942	56,225	**1,226,717**
Release of liabilities/liabilities discharged	(616,908)	1,852	**(618,760)**	(404,416)	20,099	**(424,515)**
Effect of non-economic assumption changes	(82,888)	(102,750)	**19,862**	30,708	(27,058)	**57,766**
Effect of economic assumption changes	(519,771)	77,099	**(596,870)**	1,629,421	75,063	**1,554,358**
Other	1,334	-	**1,334**	(9,824)	-	**(9,824)**
Closing Balance at 31 December	**14,207,475**	**273,632**	**13,933,843**	**12,105,682**	**288,654**	**11,817,028**

Notes to the Financial Statements (continued)

Note 20 – Insurance Contract Liabilities (continued)

Key Valuation Assumptions (continued)

(d) Movements in Insurance Contract Liabilities (continued)

	31 December 2015			31 December 2014		
Company	Insurance Liabilities £000s	Reinsurance Assets £000s	Net Liabilities £000s	Insurance Liabilities £000s	Reinsurance Assets £000s	Net Liabilities £000s
Carrying amount at 1 January	9,341,887	234,052	9,107,835	6,953,306	164,325	6,788,981
Increase in respect of new business	3,320,026	8,777	3,311,249	1,282,942	22,723	1,260,219
Transferred on Part VII	2,696,912	68,406	2,628,506	-	-	-
Release of liabilities/liabilities discharged	(531,412)	805	(532,217)	(341,795)	17,680	(359,475)
Effect of non-economic assumption changes	(79,614)	(99,989)	20,375	3,298	(25,989)	29,287
Effect of economic assumption changes	(543,425)	61,581	(605,006)	1,444,068	55,313	1,388,755
Other	3,101	-	3,101	68	-	68
Closing Balance at 31 December	**14,207,475**	**273,632**	**13,933,843**	**9,341,887**	**234,052**	**9,107,835**

The tables above details the change in the gross and net insurance liabilities over the year. The table below provides a further split of the net impact of the most significant assumption changes.

The release of liabilities line reflects claims paid, release of prudent margins and unwind of discounting over the year.

Effect of Changes in Assumptions and Estimates During the Year

The following table shows the impact on the Insurance Contract Liabilities of changes in the assumptions used:

Change in assumptions used	RL Group Net (Decrease)/ Increase in liabilities £000s	Company Net (Decrease)/ Increase in liabilities £000s
Valuation interest rates	(440,514)	(462,493)
Inflation	(156,357)	(142,514)
Demographics	(23,733)	(23,219)
Expenses	43,594	43,594
	(577,010)	**(584,632)**

As shown previously the valuation interest rate increased by 0.3% over the year which led to the £440.5m movement in RL Group liability shown and £462.5m movement in the Company liability shown. This was due to asset portfolio optimisation and widening in illiquidity premium of asset spreads. This was offset slightly by the change in interest rates for example a benchmark 30 year swap fell 0.1% in the period.

The movement in the demographic assumptions shown reflects the changes to base mortality, mortality improvement and dependants assumptions applied during the year leading to a £23.7m decrease in liabilities in RL Group and £23.2m decrease in liabilities in the Company.

Notes to the Financial Statements (continued)

Note 20 – Insurance Contract Liabilities (continued)

Key Valuation Assumptions (continued)

(e) Sensitivity Analysis

The schedule below provides an analysis of the reasonably possible movements in key assumptions that would have a material impact on liabilities, profit before tax, and equity. The analysis is based on a change in a single assumption whilst holding all other assumptions constant.

RL Group and Company 2015	Change in Assumptions	Increase/ (decrease) on liabilities £000s	Increase/ (decrease) on PBT £000s	Impact on Equity £000s
Annuitant mortality	+5% qx	(85,777)	85,777	68,408
Annuitant mortality	-5% qx	89,904	(89,904)	(71,698)
Interest rate	+100bps	(1,933,535)	28,881	23,032
Interest rate	-100bps	2,473,647	64,761	51,647
Inflation	+100bps	912,436	10,703	8,535
Inflation	-100bps	(845,382)	58,806	46,897
Long term credit default assumption	+10bps	918	(52,953)	(42,230)
Long term credit default assumption	-10bps	(918)	54,162	43,194
Expenses	+10%	28,788	(28,788)	(22,958)

The sensitivities shown above capture non-linearity effects, which may be significant following large market movements. The risk management strategy adopted can result in the RL Group being immunised to market movements in either direction.

The credit default assumption sensitivity has been calculated assuming a change in the credit spreads on non risk free assets with no associated change in valuation interest rate.

The table below shows the impact of the reinsurance is to reduce the sensitivity to mortality risk, a reduction of 77%.

RL and Company Group 2015	Change in Assumptions	(Decrease)/ increase on Insurance Liability £000s	Increase/ (decrease) on Reinsurance Asset £000s	Net (Decrease)/ increase on liabilities £000s
Annuitant mortality	+5% qx	(378,023)	292,246	(85,777)
Annuitant mortality	-5% qx	403,644	(313,740)	89,904

The annuitant mortality sensitivity is defined in terms of a qx stress where qx represents the probability of a life dying during the year. As such in the annuitant mortality stress it is assumed that in each year 5% more or fewer people survive to the end of each year than had previously been assumed.

Notes to the Financial Statements (continued)

Note 20 – Insurance Contract Liabilities (continued)

Key Valuation Assumptions (continued)

(f) Timing of Cashflows

The table below shows the discounted insurance liability cash flows, which are expected to arise during each year:

	31 December 2015			
RL Group and Company	**Less than 1 year £000s**	**1 to 5 years £000s**	**Over 5 years £000s**	**Total £000s**
Insurance liability cashflows	629,812	2,392,963	11,184,700	14,207,475
Reinsurance asset cashflows	31,520	112,711	(417,863)	(273,632)
	661,332	**2,505,674**	**10,766,837**	**13,933,843**

	31 December 2014			
RL Group	**Less than 1 year £000s**	**1 to 5 years £000s**	**Over 5 years £000s**	**Total £000s**
Insurance liability cashflows	486,363	1,850,609	9,768,710	12,105,682
Reinsurance asset cashflows	24,659	89,618	(402,931)	(288,654)
	511,022	**1,940,227**	**9,365,779**	**11,817,028**

	31 December 2014			
Company	**Less than 1 year £000s**	**1 to 5 years £000s**	**Over 5 years £000s**	**Total £000s**
Insurance liability cashflows	388,834	1,465,015	7,488,038	9,341,887
Reinsurance asset cashflows	20,950	75,636	(330,638)	(234,052)
	409,784	**1,540,651**	**7,157,400**	**9,107,835**

Notes to the Financial Statements (continued)

Note 21 – Payables and Financial Liabilities

	RL Group		Company	
	31 December 2015 £000s	31 December 2014 £000s	31 December 2015 £000s	31 December 2014 £000s
Derivative financial instruments	6,917,599	5,551,149	6,917,599	6,240,258
Collateralised financing agreements	1,886,099	2,022,430	1,886,099	2,022,430
Deposits received as collateral for derivatives from other group undertakings	-	-	-	120,160
Deposits received as collateral from third parties	752,587	640,953	752,587	450,969
Deposits received as collateral for derivatives from participating interest	227,273	464,506	227,273	464,506
Amounts due to group undertakings	20,506	13,704	20,506	13,644
Current tax payable	51,887	47,031	51,887	-
Other payables	22,388	3,993	22,388	2,485
	9,878,339	**8,743,766**	**9,878,339**	**9,314,452**

Payables and financial liabilities of £1,204.7m (2014: £1,606.8m) for the RL Group and £1,204.7m (2014: £1,487.2m) for the Company are all due within one year.

The net exposures to certain OTC derivatives are collateralised through cash. As at 31 December 2015, the total cash collateral received for RL Group was £979.9m (2014: £1,105.5m) and Company £979.9m (2014: £1,035.6m). Other OTC contracts are collateralised with fixed income securities which are not recognised on the Consolidated Statement of Financial Position.

Note 22 – Borrowings

The RL Group and Company borrowings are as follows:

	31 December 2015 £000s	31 December 2014 £000s
Affiliate subordinated loan	100,000	100,000
Subordinated loan notes	248,770	-
	348,770	**100,000**

The amounts outstanding at 31 December 2015 include £100m of floating rate perpetual callable loan notes and £250m unsecured, subordinated loan notes.

The £100m of floating rate perpetual callable loan notes are callable at par on 21 December 2017 and every six months thereafter. They carry deferrable interest at six month sterling LIBOR plus 425bps per annum. The notes are unsecured and classified as qualifying dated Tier 2 securities for the purpose of the RL Group's regulatory capital requirements under the current regime and under Solvency II. The notes are issued to an affiliate. The notes have a carrying value of £100m and a fair value of £100m (2014: £100m).

Notes to the Financial Statements (continued)

Note 22 – Borrowings (continued)

On 22 October 2015, RLL issued £250m subordinated loan notes maturing in 2025 with a fixed 8% coupon paid annually in arrears. The notes are unsecured and classified as qualifying dated Tier 2 securities for the purpose of the RL Group's regulatory capital requirements under the current regime and under Solvency II. The notes were issued and initially recognised at fair value of £248.7m being issue proceeds of £250m less capitalised issue costs of £1.3m.

At 31 December 2015 the notes have a carrying value of £248.8m which is calculated on an amortised cost basis, and a fair value of £257.5m, as determined by traded levels. The notes are issued through the public debt markets.

Part of the proceeds from the subordinated loan notes (£130m) was paid to RHUK as a dividend in order that the £125m term loan agreement held in RHUK could be repaid.

For the year ended 31 December 2015, an interest expense of £3.3m was recognised in the Consolidated Statement of comprehensive income in respect of these subordinated loan notes.

Note 23– Deferred Tax liabilities

	RL Group		Company	
Deferred tax balances comprise:	31 December 2015 £000s	31 December 2014 £000s	31 December 2015 £000s	31 December 2014 £000s
Temporary differences between the financial statements and the tax deductions for insurance liabilities	(2,792)	(3,429)	(2,792)	(2,690)
	(2,792)	**(3,429)**	**(2,792)**	**(2,690)**

The movements in the deferred tax balances were as follows:

	RL Group		Company	
	31 December 2015 £000s	31 December 2014 £000s	31 December 2015 £000s	31 December 2014 £000s
At 1 January	(3,429)	(2,914)	(2,690)	(2,914)
Impact of tax rate change on opening balance	200	-	152	-
Part VII transfer	-	-	(609)	-
Consolidation adjustment	-	(909)	-	-
Capital allowances	11	(58)	21	(121)
Transitional adjustments	426	452	334	345
At 31 December	**(2,792)**	**(3,429)**	**(2,792)**	**(2,690)**

Deferred tax assets are only recognised to the extent that based on management's assessment, they are regarded as recoverable.

Notes to the Financial Statements (continued)

Note 24 – Share Capital

At 31 December 2015 and 31 December 2014 share capital comprised:

	31 December 2015		31 December 2014	
Company	**No.**	**£000s**	**No.**	**£000s**
Authorised share capital (ordinary shares of £1 each)	183,900,840	183,901	183,900,840	183,901

On 16 May 2014 the Company allotted 28,779,840 shares of £1.00 each to RHUK, the ultimate parent of RLL. The total cash consideration received was £116.3m, reflecting share premium of £87.5m.

Note 25 – Share Premium Account and Reserve

RL Group	**Share premium £000s**	**Retained earnings £000s**
At 1 January 2015	199,854	504,862
Profit for the financial year	-	284,950
Dividends paid	-	(130,000)
At 31 December 2015	**199,854**	**659,812**

Company	**Share premium £000s**	**Retained earnings £000s**
At 1 January 2015	199,854	330,122
Profit for the financial year	-	279,690
Dividends received	-	180,000
Dividends paid	-	(130,000)
At 31 December 2015	**199,854**	**659,812**

Note 26 – Dividends

	31 December 2015 £000s	**31 December 2014 £000s**
Interim Ordinary Share Dividends (£0.71 per £1.00 ordinary share)	130,000	-
	130,000	-

On 2 November the Directors recommended and paid an ordinary dividend of £130m (2014:£nil).

The Directors have recommended that no final ordinary dividend in respect of the year be paid. (2014:£nil).

Notes to the Financial Statements (continued)

Note 27 – Derivatives

The RL Group utilises derivative financial instruments as part of its asset/liability risk management. It enters into derivative contracts to match the Insurance Contract Liabilities arising on the insurance and reinsurance contracts that it issues.

The following table shows the fair value of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying assets, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are indicative of neither the market risk nor the credit risk.

	31 December 2015			31 December 2014		
RL Group	**Assets £000s**	**Liabilities £000s**	**Notional Amount £000s**	**Assets £000s**	**Liabilities £000s**	**Notional Amount £000s**
Derivatives Held for Risk Management:						
Interest rate swap	5,477,847	(5,255,524)	90,688,417	4,641,488	(4,267,001)	75,617,910
Inflation swap	1,321,260	(1,405,014)	27,814,298	1,039,317	(1,077,421)	24,609,061
Currency swap	113,914	(206,378)	10,231,929	109,165	(120,689)	8,159,240
Credit derivative	22,056	(44,236)	1,813,635	11,923	(76,133)	3,449,834
Foreign currency forwards	1,579	(6,447)	291,506	101	(9,905)	946,626
	6,936,656	**(6,917,599)**	**130,839,785**	**5,801,994**	**(5,551,149)**	**112,782,671**

	31 December 2015			31 December 2014		
Company	**Assets £000s**	**Liabilities £000s**	**Notional Amount £000s**	**Assets £000s**	**Liabilities £000s**	**Notional Amount £000s**
Derivatives Held for Risk Management:						
Interest rate swap	5,477,847	(5,255,524)	90,688,417	5,088,055	(4,788,053)	71,611,982
Inflation swap	1,321,260	(1,405,014)	27,814,298	1,201,261	(1,239,365)	26,399,961
Currency swap	113,914	(206,378)	10,231,929	114,318	(126,837)	8,148,629
Credit derivative	22,056	(44,236)	1,813,635	28,759	(76,098)	3,449,834
Foreign currency forwards	1,579	(6,447)	291,506	97	(9,905)	946,626
	6,936,656	**(6,917,599)**	**130,839,785**	**6,432,490**	**(6,240,258)**	**110,557,032**

Notes to the Financial Statements (continued)

Note 27 – Derivatives (continued)

Derivatives are used solely for risk management purposes, allowing market risks to be hedged in line with our risk appetite. The notional amount shown reflects the gross notional of derivative contracts and under IFRS, we are not permitted to offset assets and liabilities. Hence multiple derivative contracts which generate offsetting risk positions inflate the size of the notional amount reported, but do not increase our risk exposure. As such, the notional amount should not be considered as an indicator of the market risk exposure generated by the derivative portfolio.

The RL Group's exposure under derivative contracts is closely monitored as part of the overall management of the RL Group's market risk (see also Note 28). As of 31 December 2015, the RL Group had material positions in the following types of derivatives:

Interest rate swaps

Interest rate swaps are contractual agreements between two parties to exchange movements in interest rates. Typically, for an interest rate swap, a floating rate interest stream will be exchanged for a fixed rate or vice versa. The payment flows are usually netted against each other, with the difference being paid by one party to the other.

Inflation swaps

The RL Group uses inflation swaps and options to hedge the inflation linked benefits on the pension liabilities of the UK insurance business.

Currency swaps

In a currency swap, the RL Group pays a specified amount in one currency and receives a specified amount in another currency. Currency swaps are mostly gross–settled.

Credit derivatives

The RL Group uses credit derivatives to hedge counterparty risk of some of its assets in the event of default of corporate or sovereign bonds.

Forwards and futures

Forwards and futures contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customised contracts traded in the over-the-counter market. Futures contracts are transacted in standardised amounts on regulated exchanges and are subject to daily cash margin requirements. The main differences in the risk associated with forward and futures contracts are credit risk and liquidity risk. The RL Group has credit exposure to the counterparties of forward contracts. The credit risk related to future contracts is considered minimal because the cash margin requirements of the exchange help ensure that these contracts are always honoured. Forward contracts are settled gross and are, therefore, considered to bear a higher liquidity risk than the futures contracts which are settled on a net basis. Both types of contracts result in market risk exposure.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management

The RL Group is exposed to financial risk through its financial assets, financial liabilities and Insurance Contract Liabilities. These risks, described below, are managed in accordance with risk management policies and procedures established by the RL Group.

The Board Risk Committee advises and makes recommendations to the Board of Directors to assist it in providing leadership, direction and oversight of the RL Group's risk appetite, risk strategy and risk management framework and of the risk aspects of major investments and corporate transactions. The Board Risk Committee has oversight of the Working Level Risk Committee, which is an executive committee and is assigned responsibility for the on-going monitoring and control of the financial and insurance risks associated with the activities of the RL Group.

In addition to the committees, independent functions such as Compliance, Finance (including Risk Management), Legal, Internal Audit and Operations, perform risk management functions, which include assessing, monitoring, reporting and evaluating risk.

Market Risk

Market risk is the risk of changes in the value of the RL Group's net asset position due to changes in market prices. Financial investments are accounted for at fair value and, therefore, fluctuate on a daily basis. Categories of market risk include the following:

- Interest rate risk arises from discounting cash flow mismatches across all future dates. Profits and losses are generated through changes in the level, slope and curvature of interest rate curves. The risk is hedged using interest rate swaps.

- Inflation rate risks results from mismatches in the index linkage of annuities and assets. Profits and losses are generated through changes to the level, slope and curvature of inflation curves. The risk is hedged using inflation swaps.

- Currency rate risk results from mismatches in the denomination of annuities and assets. Profits and losses are generated due to changes in the level of foreign exchange rates. The risk is hedged using spot foreign exchange and cross currency swaps.

The RL Group manages market risk by diversifying exposures, controlling position sizes and establishing economic hedges in related securities, derivatives and insurance liabilities.

The RL Group's Chief Risk Officer and the Risk Function, which is independent of management and reports to the Chief Executive Officer, has responsibility for assessing, monitoring and managing market risk. Risks are monitored and controlled through strong oversight and independent control and support functions across the business.

Market risk limits are set by the Board Risk Committee and the Risk Function monitors exposures against those.

Senior management is responsible and accountable for managing market risks daily within prescribed limits. They have in depth knowledge of their positions, markets and the instruments available to hedge their exposures.

In addition to applying business judgement, management uses a number of quantitative tools to manage the exposure to market risk for 'Financial Investments' in the Financial Statements. These tools include scenario analyses, stress test and other analytical tools that measure the potential effects on the net revenues of various market events, including, but not limited to, a large widening of credit spreads, as well as volatility in interest, inflation and mortality rates.

Management and the Risk Function discuss market information, positions and estimated risk and loss scenarios on an ongoing basis.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Market Risk (continued)

Interest Rate Risk Sensitivity Analysis

RL Group Change in Variables	31 December 2015 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	318	254
(-) 1 basis point	(318)	(254)

RL Group Change in Variables	31 December 2014 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	125	98
(-) 1 basis point	(125)	(98)

Company Change in Variables	31 December 2015 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	318	254
(-) 1 basis point	(318)	(254)

Company Change in Variables	31 December 2014 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	102	80
(-) 1 basis point	(102)	(80)

There was no change in the method used for deriving sensitivity information and significant variables during the year.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Market Risk (continued)

Inflation rate risk sensitivity analysis

RL Group Change in Variables	31 December 2015 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	(373)	(297)
(-) 1 basis point	373	297

RL Group Change in Variables	31 December 2014 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	(357)	(280)
(-) 1 basis point	357	280

Company Change in Variables	31 December 2015 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	(373)	(297)
(-) 1 basis point	373	297

Company Change in Variables	31 December 2014 Impact on PBT £000s	Impact on Equity Up to a Year £000s
(+) 1 basis point	(219)	(172)
(-) 1 basis point	219	172

Credit Risk

Credit risk represents the potential for loss due to the default or deterioration in credit quality of a counterparty, e.g. an OTC derivatives counterparty or an issuer of corporate debt instruments. Credit risk also comes from cash placed with banks and collateralised financing transactions, (i.e. resale and repurchase agreements) and receivables from customers and counterparties.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

The Board Risk Committee establishes and reviews credit policies and parameters. Policies authorised by the Board Risk Committee prescribe the level of formal approval required to assure credit exposure to a counterparty across all product areas is in line with the risk taking capacity and strategy, taking into account any enforceable netting provisions, collateral or other credit risk mitigants.

The Chief Credit Officer, who is independent of management and reports to the Chief Risk Officer, has responsibility for assessing and monitoring credit risk. Risks are monitored and controlled through strong oversight and independent control and support functions across the business.

Senior management is responsible and accountable for managing credit risks within prescribed limits. They have in depth knowledge of the credit positions, underlying models and the instruments available to hedge the credit exposures.

Effective management of credit risk requires accurate and timely information, strong collateral management, a high level of communication and knowledge of customers, countries, industries and products. The process for managing credit risk includes:

- Establishing counterparty risk and concentration limits;
- Use of collateral and other risk mitigants to reduce credit losses in the event of default;
- Assessing the likelihood that counterparty will default on its payment obligations;
- Measuring and modelling the Group's current and potential credit exposures and losses resulting from counterparty defaults;
- Approving credit risk generated by transactions and investments;
- Monitoring and communicating the utilisation of and compliance with established credit exposure limits;
- Identifying, monitoring and managing potential problem credits;
- Performing adequate stress tests to assess the Group's vulnerability to certain scenarios and risk concentrations; reporting and where necessary, escalating of credit exposures to senior management, the Working Level Risk Committee, the Board Risk Committee, and possibly the Board of Directors and regulators; and
- Communicating and collaborating with other independent control and support functions such as Operations, Legal and Compliance.

Risk Mitigants

To reduce the credit exposures on derivatives and collateralised agreement transactions, the RL Group enters into netting agreements with counterparties that permit it to offset receivables and payables with such counterparties that enable it to obtain collateral from them on an upfront or contingent basis and/or terminate transactions if the counterparty's credit rating falls below a specified level.

When the RL Group does not have sufficient visibility into a counterparty's financial strength or when it believes a counterparty requires support from its parent company, the RL Group may obtain third party guarantees of the counterparty's obligations. The RL Group also mitigates its credit risk using credit derivatives.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

Credit Exposures

The RL Group's credit exposures are described further below.

Cash and Cash Equivalents. Cash and cash equivalents include both interest bearing and non-interest bearing deposits. To mitigate the risk of credit loss, the RL Group places its deposits with banks typically assigned minimum ratings in the single A rating category and central banks. Cash deposits with banks rated lower than the single A category are subject to approval by the Board Risk Committee, in line with RL Group's liquidity policy.

OTC Derivatives. Derivatives are reported at fair value on a gross by counterparty basis in the RL Group's Financial Statements unless the RL Group has current legal rights of set off and also intends to settle on a net basis. OTC derivatives are risk managed using the risk processes, measures and limits described above.

A waiver to INSPRU 3.2.5R(3) was granted in July 2010 and renewed in July 2013. This allowed the RL Group to treat a derivative contract with a pension scheme as an admissible asset. The purpose of the derivative contract is to provide a hedge for a specific pension scheme against market risk. The RL Group has hedged this risk with a derivative contract with an approved counterparty.

Collateralised Agreements. The RL Group bears credit risk related to re-sale agreement and securities borrowed only to the extent that cash advanced to the counterparty exceeds the value of the collateral received. Therefore, the RL Group's credit exposure on the transactions is significantly lower than the amounts recorded on the balance sheet (which represents fair values or contractual value before consideration of collateral received). The RL Group also has credit exposure on repurchase agreements and securities loaned, which are liabilities on its Consolidated Statement of Financial Position, to the extent that the collateral pledged for these transactions exceeds the amount of cash received.

Other Credit Exposures. The RL Group is exposed to credit risk from its receivables from customers and counterparties. Receivables from counterparties are generally comprised of collateralised receivables related to customer securities transactions and have minimal credit risk due to the value of the collateral received. In addition, the RL Group invests in highly rated assets or assets where there is underlying structural security in the event of a default. These assets include supranational sovereign bonds, sub-sovereign bonds, covered bonds, higher education bonds, infrastructure assets and secured residential lending.

Reinsurance. Long term business is ceded to reinsurers under contracts to transfer part of the insurance risk associated with the underlying insurance contracts. The amounts that will be recoverable from reinsurers is estimated based upon the gross provisions, having due regard to collectability. The recoverability of reinsurance recoveries is assessed having regard to market data on the financial strength of the reinsurance company.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

The following table identifies the amounts covered by enforceable netting arrangements (netting under master netting agreements, cash collateral and security collateral) but do not qualify for netting under IAS32.

	31 December 2015				
		Related amounts not offset			
RL Group	Net amounts of financial assets presented in the statement of financial position £000s	Netting under master netting agreements £000s	Cash collateral £000s	Security collateral and charges £000s	Net credit exposures £000s
Exposure to Credit Risk by Class					
Property, plant and equipment	1,988	-	-	-	1,988
Collective investment schemes	470,388	-	-	-	470,388
Government and agency obligations	6,137,079	-	-	-	6,137,079
Corporate debt	5,792,876	-	-	-	5,792,876
Derivative assets	6,936,656	(4,752,518)	(494,564)	(1,689,574)	-
Collateralised agreements and financing	5,134,880	-	(152,159)	(4,982,721)	-
Certificate of deposits	119,734	-	-	-	119,734
Reinsurance assets	273,632	-	-	-	273,632
Accrued income and prepayments	164,980	-	-	-	164,980
Receivables	392,498	-	-	-	392,498
Cash and cash equivalents	83,582	-	-	-	83,582
	25,508,293	(4,752,518)	(646,723)	(6,672,295)	13,436,757

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

	31 December 2014				
		Related amounts not offset			
RL Group	Net amounts of financial assets presented in the statement of financial position £000s	Netting under master netting agreements £000s	Cash collateral £000s	Security collateral £000s	Net credit exposures £000s
Exposure to Credit Risk by Class					
Property, plant and equipment	1,524	-	-	-	1,524
Collective investment schemes	726,307	-	-	-	726,307
Government and agency obligations	5,855,467	-	-	-	5,855,467
Corporate debt	5,076,291	-	-	-	5,076,291
Derivative assets	5,801,994	(3,723,156)	(546,694)	(1,532,144)	-
Collateralised agreements and financing	3,400,828	-	(101,112)	(3,299,716)	-
Certificate of deposits	128,503	-	-	-	128,503
Reinsurance assets	288,654	-	-	-	288,654
Accrued income and prepayments	130,816	-	-	-	130,816
Receivables	357,733	-	-	-	357,733
Cash and cash equivalents	106,711	-	-	-	106,711
	21,874,828	(3,723,156)	(647,806)	(4,831,860)	12,672,006

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

	31 December 2015				
		Related amounts not offset			
Company	Net amounts of financial assets presented in the statement of financial position £000s	Netting under master netting agreements £000s	Cash collateral £000s	Security collateral and charges £000s	Net credit exposures £000s
Exposure to Credit Risk by Class					
Investment in subsidiary	2,669	-	-	-	2,669
Property, plant and equipment	1,988	-	-	-	1,988
Collective investment schemes	467,727	-	-	-	467,727
Government and agency obligations	6,137,079	-	-	-	6,137,079
Corporate debt	5,792,876	-	-	-	5,792,876
Derivative assets	6,936,656	(4,752,518)	(494,564)	(1,689,574)	-
Collateralised agreements and financing	5,134,880	-	(152,159)	(4,982,721)	-
Certificate of deposits	119,734	-	-	-	119,734
Reinsurance assets	273,632	-	-	-	273,632
Accrued income and prepayments	164,980	-	-	-	164,980
Receivables	392,498	-	-	-	392,498
Cash and cash equivalents	83,574	-	-	-	83,574
	25,508,293	(4,752,518)	(646,723)	(6,672,295)	13,436,757

Within the above table derivative liabilities are only included to the extent they net against derivative assets. Therefore, the amount of derivative assets shown after offsetting netting arrangements does not represent our overall derivative exposure. Our overall exposure can be seen in Note 27 Derivatives.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

	31 December 2014				
		Related amounts not offset			
Company	Net amounts of financial assets presented in the statement of financial position £000s	Netting under master netting agreements £000s	Cash collateral £000s	Security collateral £000s	Net credit exposures £000s
Exposure to Credit Risk by Class					
Investment in subsidiary	421,381	-	-	-	421,381
Property, plant and equipment	1,524	-	-	-	1,524
Collective investment schemes	628,257	-	-	-	628,257
Government and agency obligations	4,151,886	-	-	-	4,151,886
Corporate debt	3,596,702	-	-	-	3,596,702
Derivative assets	6,432,490	(4,439,708)	(356,710)	(1,636,072)	-
Collateralised agreements and financing	3,400,828	-	(101,112)	(3,299,716)	-
Certificate of deposits	128,503	-	-	-	128,503
Reinsurance assets	234,052	-	-	-	234,052
Accrued income and prepayments	95,588	-	-	-	95,588
Receivables	326,364	-	-	-	326,364
Cash and cash equivalents	86,631	-	-	-	86,631
	19,504,206	(4,439,708)	(457,822)	(4,935,788)	9,670,888

Right of Offset

As described in the risk mitigants section of this note, the RL Group has the right of offset for certain financial assets and liabilities.

Netting under master netting agreements of £4,753m (2014: £3,723m), Company £4,753m (2014: £4,440m) reflects the offsetting of derivative assets with liabilities for which the RL Group has a right to set off in the event of default. Cash and security collateral have been offset to the extent there are credit exposures on the balance sheet.

The RL Group has received total security collateral and charges of £8,868.9m (2014: £5,179.8m) of which £6,672.3m (2014: £4,831.9m) has been applied against net exposure, leaving excess of £2,196.6m (2014: £347.9m). The Company has received total security collateral and charges of £8,868.9.m (2014: £5,164.8m) of which £6,672.3m (2014: £4,935.8m) has been applied against net exposure, leaving excess of £2,196.6m (2014: £229m). Security collateral exposes the RL Group and Company to further market and credit risk. This is mitigated through the use of haircuts and over collateralisation.

Credit default swaps and total return swaps (which contain credit protection) have been purchased to protect the RL Group from default on corporate bonds. The table above does not reflect the protection provided. The RL Group calls margins, receivable in cash, against this exposure and other derivative positions.

In a distressed situation the value of collateral may vary depending on credit quality and interest rates. The effectiveness of collateral as a credit risk mitigant will depend on the operational expertise of the collateral manager and the ability to seize the collateral in a distressed scenario.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

The table below shows the RL Group's gross and net credit exposure based on external ratings (lowest of Standard & Poor's, Moody's and Fitch ratings). In line with industry standards, Stability Ratings are used to rate the Money Market funds in which the RL Group invests £328m (2014: £296.4m) of the total net credit exposure relates to bonds held within negative basis packages, for which maturity, currency and reference obligation matched credit default swap protection is held.

Net credit exposure is primarily in 'AAA' and 'AA' bonds. AAA assets include supranational bonds, sub-sovereigns, covered bonds, US not-for-profit private universities and certificates of deposit. 'AA' assets include Gilts. Other net credit exposures rated 'A' and 'BBB' include investments in regulated infrastructure assets and English social housing bonds, which are secured on property assets.

Net credit exposures rated non-investment grade are mitigated by the use of collateral or credit default swap.

As of current and prior year end there were no financial assets past due or impaired.

	31 December 2015				
		Related amounts not offset			
	Net amounts of financial assets presented in the statement of financial position	Netting under master netting agreements	Cash collateral	Security collateral	Net credit exposures
RL Group	£000s	£000s	£000s	£000s	£000s
Exposure to Credit Risk by Rating					
AAA	3,180,655	-	-	-	3,180,655
AA	8,686,942	(182,416)	-	(1,642,680)	6,861,846
A	8,546,533	(3,810,753)	(401,531)	(2,485,046)	1,849,203
BBB	2,296,754	(759,307)	(244,436)	(225,257)	1,067,754
BB	53,547	-	-	-	53,547
B	103,471	-	(756)	(76,342)	26,373
Unrated	2,640,391	(42)	-	(2,242,970)	397,379
	25,508,293	(4,752,518)	(646,723)	(6,672,295)	13,436,757

The unrated financial assets of £2,640.4m (2014:£1,260.0m) reflect investments in issuers and issues that are not externally rated. During the year, the RL Group invested in unrated financial assets which are highly secured and subject to very low credit risk. These include notably £1,483m of ground rent loans executed during 2015.

For the purpose of Solvency II, unrated assets are internally rated by the RL Group's independent credit risk function under a framework which has been externally reviewed.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

	31 December 2014				
		Related amounts not offset			
RL Group	Net amounts of financial assets presented in the statement of financial position £000s	Netting under master netting agreements £000s	Cash collateral £000s	Security collateral £000s	Net credit exposures £000s
Exposure to Credit Risk by Rating					
AAA	2,448,404	(46,272)	-	-	2,402,132
AA	8,155,173	(146,946)	-	(1,454,676)	6,553,551
A	7,403,971	(2,509,646)	(238,164)	(2,688,844)	1,967,317
BBB	2,416,223	(971,863)	(291,853)	(442,349)	710,158
BB	191,026	-	(1,600)	(106,018)	83,408
Unrated	1,260,031	(48,429)	(116,189)	(139,973)	955,440
	21,874,828	**(3,723,156)**	**(647,806)**	**(4,831,860)**	**12,672,006**

	31 December 2015				
		Related amounts not offset			
Company	Net amounts of financial assets presented in the statement of financial position £000s	Netting under master netting agreements £000s	Cash collateral £000s	Security Collateral and charges £000s	Net credit exposures £000s
Exposure to Credit Risk by Rating					
AAA	3,177,993	-	-	-	3,177,993
AA	8,686,935	(182,416)	-	(1,642,680)	6,861,839
A	8,546,533	(3,810,753)	(401,531)	(2,485,046)	1,849,203
BBB	2,296,754	(759,307)	(244,436)	(225,257)	1,067,754
BB	53,547	-	-	-	53,547
B	103,471	-	(756)	(76,342)	26,373
Unrated	2,643,060	(42)	-	(2,242,970)	400,048
	25,508,293	**(4,752,518)**	**(646,723)**	**(6,672,295)**	**13,436,757**

The unrated financial assets of £2,643.1m (2014: £2,626.5m) reflect investments in issuers and issues that are not externally rated. During the year, the Company invested in unrated financial assets which are subject to very low credit risk. These include notably £1,483m of ground rent loans executed during 2015.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Credit Risk (continued)

	31 December 2014				
		Related amounts not offset			
	Net amounts of financial assets presented in the statement of financial position	Netting under master netting agreements	Cash collateral	Security collateral	Net credit exposures
Company	£000s	£000s	£000s	£000s	£000s
Exposure to Credit Risk by Rating					
AAA	1,717,173	-	-	-	1,717,173
AA	6,161,880	(133,771)	-	(1,445,363)	4,582,746
A	6,741,209	(2,505,603)	(165,269)	(2,683,159)	1,387,178
BBB	2,066,457	(965,201)	(174,764)	(442,349)	484,143
BB	191,026	-	(1,600)	(106,018)	83,408
Unrated	2,626,461	(835,133)	(116,189)	(258,899)	1,416,240
	19,504,206	(4,439,708)	(457,822)	(4,935,788)	9,670,888

Liquidity Risk

Liquidity risk arises where timing differences and/or uncertainties occur between cash inflows and cash outflows. The objective of liquidity management is to ensure that the RL Group is capable of honouring all cash flow commitments on both an on-going basis and in a stressed scenario, without incurring significant cost or business disruption. The RL Group liquidity and funding policy is designed to ensure the availability of sufficient funds to meet cash flow requirements on a timely basis via:

- Maintenance of substantial excess liquidity. The RL Group seeks to enter into long term, illiquid investments that match its liabilities in order to maximise the value of the illiquidity premium. To mitigate residual liquidity risk the RL Group maintains substantial excess liquidity to meet a broad range of potential cash outflows in a stressed environment including financing obligations.

- Conservative asset/liability management. The RL Group seeks to maintain funding sources that are sufficiently long term in order to withstand a prolonged or severe liquidity-stressed environment without having to rely on asset sales.

The Risk function which is independent of management and reports to the Chief Risk Officer, who reports to the Chief Executive Officer has primary responsibility for assessing, monitoring and managing liquidity risk. Risks are monitored and controlled through strong oversight and independent control and support functions across the business.

Senior management is responsible and accountable for managing liquidity risks within prescribed limits that are set by the Board and are overseen by the Board Risk Committee.

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Liquidity Risk (continued)

The following table details the RL Group's and Company's financial liabilities and assets by contractual maturity including interest that was accrued where the RL Group is entitled to repay the liability before its maturity. Financial Assets and Liabilities are presented at their fair value as this is consistent with the values used in the liquidity risk management of these instruments. The table excludes insurance liability cash flows and reinsurance asset cash flows which are included in Note 20.

	31 December 2015			
RL Group	**Less than 1 year £000s**	**1 to 5 years £000s**	**Over 5 years £000s**	**Total £000s**
Financial Assets				
Financial investments	787,136	3,016,378	20,788,099	24,591,613
Accrued income and prepayments	134,455	12,600	17,925	164,980
Receivables	392,498	-	-	392,498
Cash and cash equivalents	83,582	-	-	83,582
	1,397,671	**3,028,978**	**20,806,024**	**25,232,673**
Financial Liabilities				
Payables and financial liabilities	1,204,697	2,105,114	6,568,528	9,878,339
Borrowings	-	-	348,770	348,770
Deferred tax liabilities	-	-	2,792	2,792
Accruals and deferred income	23,179	4,110	61	27,350
	1,227,876	**2,109,224**	**6,920,151**	**10,257,251**
Net	**169,795**	**919,754**	**13,885,873**	**14,975,422**

	31 December 2014			
RL Group	**Less than 1 year £000s**	**1 to 5 years £000s**	**Over 5 years £000s**	**Total £000s**
Financial Assets				
Financial investments	1,058,333	2,789,071	17,141,986	20,989,390
Accrued income and prepayments	130,816	-	-	130,816
Receivables	357,733	-	-	357,733
Cash and cash equivalents	106,711	-	-	106,711
	1,653,593	**2,789,071**	**17,141,986**	**21,584,650**
Financial Liabilities				
Payables and financial liabilities	1,606,841	1,388,232	5,748,693	8,743,766
Borrowings	-	-	100,000	100,000
Deferred tax liabilities	39	3,090	300	3,429
Accruals and deferred income	33,334	-	-	33,334
	1,640,214	**1,391,322**	**5,848,993**	**8,880,529**
Net	**13,379**	**1,397,749**	**11,292,993**	**12,704,121**

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Liquidity Risk (continued)

Company	31 December 2015			
	Less than 1 year £000s	1 to 5 years £000s	Over 5 years £000s	Total £000s
Financial Assets				
Financial investments	784,475	3,016,378	20,788,099	24,588,952
Accrued income and prepayments	134,455	12,600	17,925	164,980
Receivables	392,498	-	-	392,498
Cash and cash equivalents	83,574	-	-	83,574
	1,395,002	**3,028,978**	**20,806,024**	**25,230,004**
Financial Liabilities				
Payables and financial liabilities	1,204,697	2,105,114	6,568,528	9,878,339
Borrowings	-	-	348,770	348,770
Deferred tax liabilities	-	-	2,792	2,792
Accruals and deferred income	23,179	4,110	61	27,350
	1,227,876	**2,109,224**	**6,920,151**	**10,257,251**
Net	**167,126**	**919,754**	**13,885,873**	**14,972,753**

Company	31 December 2014			
	Less than 1 year £000s	1 to 5 years £000s	Over 5 years £000s	Total £000s
Financial Assets				
Financial investments	959,529	2,778,085	14,601,052	18,338,666
Accrued income and prepayments	95,588	-	-	95,588
Receivables	326,364	-	-	326,364
Cash and cash equivalents	86,631	-	-	86,631
	1,468,112	**2,778,085**	**14,601,052**	**18,847,249**
Financial Liabilities				
Payables and financial liabilities	1,487,179	1,379,037	6,448,236	9,314,452
Borrowings	-	-	100,000	100,000
Deferred tax liabilities	-	2,690	-	2,690
Accruals and deferred income	31,300	-	-	31,300
	1,518,479	**1,381,727**	**6,548,236**	**9,448,442**
Net	**(50,367)**	**1,396,358**	**8,052,816**	**9,398,807**

Notes to the Financial Statements (continued)

Note 28 – Financial Risk Management (continued)

Collateralised Agreements

RL Group and Company

Assets are transferred under repurchase and securities lending agreements with other financial institutions. The nature and carrying amounts of the assets (all carried at fair value) subject to repurchase and securities lending agreements as well as their related liabilities are as follows:

	31 December 2015		31 December 2014	
	Asset £000s	Related Liability £000s	Asset £000s	Related Liability £000s
Government and agency obligations	2,005,394	1,836,922	2,273,450	1,973,732
Corporate debt	53,688	49,177	56,092	48,698
	2,059,082	**1,886,099**	**2,329,542**	**2,022,430**

As the substance of these transactions is secured borrowings and repurchase agreements the asset collateral continues to be recognised in full and the related liability reflecting the RL Group's obligations to repurchase the transferred assets at a future date is recognised in other liabilities. The RL Group remains exposed to interest rate risk and credit risk on these pledged instruments. The counterparty's recourse is not limited to the transferred assets.

The RL Group net exposures to certain OTC derivatives are collateralised through cash. As at 31 December 2015, the total cash collateral received was £979.9m (2014: £1,105.5m). The Company total cash collateral received was £979.9m (2014: £1,035.6m). Other OTC contracts are collateralised with fixed income securities which are not recognised on the balance sheet of the RL Group.

Note 29 – Capital Management

The RL Group's capital resources are of critical importance. The RL Group's risk management procedures and governance and regulatory environment are described in the Strategic Report. The objectives in managing its capital are

- To satisfy the requirements of its policyholders and regulators;
- To match the profile of its assets and liabilities, taking account of the risk inherent in the business;
- To maintain financial strength and allocate capital efficiently to support new business growth; and
- To retain financial flexibility by maintaining strong liquidity;

Solvency I

As at 31 December 2015 the Group had sufficient capital available to meet its regulatory capital requirements. The RL Group holds both debt and equity to optimise its capital structure and improve shareholder return.

Under the Solvency I regime, the Group was required to hold sufficient capital to meet the PRA's capital requirements calculated on the Solvency I statutory basis, which is based on EU Directives. As was required with all regulated insurance businesses, the RL Group also monitored its Individual Capital Assessment ('ICA') which considers certain business risks not reflected in the statutory basis.

Notes to the Financial Statements (continued)

Note 29 – Capital Management (continued)

The available capital was subject to certain restrictions as to its availability to meet capital requirements. In particular, no transfers from the long term fund could take place without an up to date actuarial valuation.

The capital held within the shareholders' fund was generally available to meet any requirements. It remains the intention of management to ensure that there is adequate capital to exceed the RL Group's regulatory requirements.

Total available capital resources at 31 December 2015 are £1,369.5m (2014: £970.9m) of which:

At 31 December 2015 Group and Company	Long Term Fund £000s	Shareholders' Funds £000s	Total £000s
Shareholders' funds outside long term fund	-	400,951	400,951
Shareholders' funds held in long term fund	642,616	-	642,616
Total shareholders' funds	642,616	400,951	1,043,567
Adjustments onto regulatory basis	(249,666)	575,574	325,908
Total Available Capital Resources	**392,950**	**976,525**	**1,369,475**

At 31 December 2014 Group and Company	Long Term Fund £000s	Shareholders' Funds £000s	Total £000s
Shareholders' funds outside long term fund	-	385,715	385,715
Shareholders' funds held in long term fund	328,162	-	328,162
Total shareholders' funds	328,162	385,715	713,877
Adjustments onto regulatory basis	(241,991)	498,984	256,993
Total Available Capital Resources	**86,171**	**884,699**	**970,870**

Note that under Solvency II the distinction between the long term fund and shareholders' fund disappears.

The RL Group does not write any with profits business. The RL Group has written an immaterial volume of unit linked business which is wholly reinsured.

The RL Group was required to hold sufficient capital to meet the Insurance Groups Directive ('IGD'). It is also required to ensure that its insurance company subsidiaries meet the higher of the Capital Resource Requirement ('CRR') determined in accordance with the PRA's regulatory rules and the ICA.

Under Solvency I management maintained surplus capital in its insurance company subsidiaries in excess of the higher of the CRR and ICA to meet the PRA's total requirements, and to maintain an appropriate additional margin over this to absorb changes in capital requirements.

At 31 December 2015 the IGD cover was 244% (2014: 204%) of the capital requirement of £560.7m (2014: £477.1m).

Notes to the Financial Statements (continued)

Note 29 – Capital Management (continued)

Movements in Capital Resources under Solvency I

	31 December 2015 £000s	31 December 2014 £000s
Opening Balance	**970,870**	**654,128**
New business	173,639	60,800
Acquisition of RAL	-	210,203
Management of in force book	258,737	50,836
Expenses	(61,793)	(46,521)
Demographic experience variance	10,180	11,739
Other	1,049	(7,633)
Operating Surplus	**1,352,682**	**933,552**
Economic profits	(5,516)	(610)
Non recurring expenses	(15,089)	(14,800)
Finance costs	(11,560)	(6,443)
Tax	(71,042)	(57,084)
Debt Issuance	250,000	-
Issue of ordinary share	-	116,255
Dividend payment	(130,000)	-
Closing Balance	**1,369,475**	**970,870**

Capital Resource Sensitivities

The capital position is sensitive to changes in market conditions, due to changes in the value of the assets and the effect that changes in investment conditions may have on the value of the liabilities. The RL Group seeks to mitigate these risks through the use of derivative hedges and reinsurance. Management monitor these assumptions and market conditions and take appropriate action if relevant.

Management monitors markets conditions and emerging longevity experience on a regular basis. As these conditions change, management will take remedial action such as adjustment of hedging strategies if appropriate.

Financial risk management is discussed in Note 28.

Solvency II

From 1 January 2016, the RL Group is required to operate under the new Solvency II regime. This is discussed on pages 7 and 8 of the Strategic Report.

Notes to the Financial Statements (continued)

Note 30 – Related Parties Disclosures

Ultimate Holding Company

At the Financial Statement date, the immediate and ultimate parent company was RHUK, which is incorporated in the United Kingdom. Company Financial Statements are prepared for RHUK, copies of which can be obtained from the Company Secretary, Level 25, The Leadenhall Building, 122 Leadenhall Street, London, EC3V 4AB.

Related Party Transactions

The RL Group entered into various transactions with fellow participating interests which are subject to common control from the same source, including Goldman Sachs International, Goldman Sachs and Co, The Goldman Sachs Group Inc., Goldman Sachs Asset Management International, and Rothesay Life (Cayman) Limited.

Details of transactions and balances in respect of these transactions are as follows:

	RL Group		Company	
	31 December 2015	31 December 2014	31 December 2015	31 December 2014
RL Group	**£000s**	**£000s**	**£000s**	**£000s**
Statement of Comprehensive Income				
Realised/Unrealised losses on financial assets and liabilities	(133,878)	(563,639)	(133,878)	(563,639)
Interest income on bank deposits	-	36	-	39
Income from money market securities held in collective investment schemes	3,478	2,889	2,966	2,006
Interest on collateralised agreements and financing	37,363	31,786	37,363	31,786
Service fee charges	(2,900)	(4,161)	(2,900)	(3,979)
Investment management and charges	(6,458)	(7,077)	(6,458)	(7,077)
Finance costs	(582)	-	(582)	-
Statement of Financial Position				
Derivative financial assets and liabilities	(1,355,115)	(1,119,032)	(1,355,115)	(1,119,032)
Collateralised agreements and financing	913,752	1,440,880	913,752	1,440,880
Collective investments schemes	470,388	708,519	467,727	610,469
Accrued interest and prepayments	10,307	241	10,306	189
Amounts payable to related party	(227,273)	(890)	(227,273)	(890)

During the year £4m (2014: £4m) of bonus payments were borne by a fellow participating interest, as part of a long term incentive arrangement. The RL Group will not be charged for this expense.

The notional value of derivatives contracts outstanding with related parties in RL Group and the Company as at 31 December 2015 was £36,424.6m (2014: £40,964.3m).

The RL Group continues to develop fully independent infrastructure and computer systems. As of 1 September 2015 the RL Group fully migrated its middle office and back office functions to an independent third party. Any services/support which remains provided by Goldman Sachs are provided on an arms-length basis under a Transition Services Agreement ('TSA').

Notes to the Financial Statements (continued)

Note 30 – Related Parties Disclosures (continued)

Transactions with key management personnel

Key management personnel comprise the Directors of the Company, Directors of subsidiary undertakings, Directors of RHUK and certain members of senior management.

There are no material transactions between the RL Group and its key management personnel other than transactions discussed below:

	31 December 2015 £000s	31 December 2014 £000s
Salaries, bonus and other employee benefits	8,973	7,800
Pension costs	163	151
	9,136	**7,951**

The tables below represents transactions between RL and its subsidiary RAL, its parent RHUK and other group company RPML.

Transactions with Rothesay Pensions Management Limited

	31 December 2015 £000s	31December 2014 £000s
Statement of Comprehensive Income		
Cost transfer	(33,651)	(25,627)
Statement of Financial Position		
Other payables	20,476	13,090

Notes to the Financial Statements (continued)

Note 30 – Related Parties Disclosures (continued)

Transactions with Rothesay Assurance Limited

	31 December 2015 £000s	31December 2014 £000s
Statement of Comprehensive Income		
Interest income on bank deposits	-	12
Investment management charges	-	(26)
Interest on collateral	(642)	-
Realised/Unrealised gains on financial assets and liabilities	134,775	-
Cost transfer	762	2,186
Statement of Financial Position		
Investment in subsidiary undertaking	2,669	421,381
Derivative financial instruments	-	116,223
Other receivables	-	201
Other payables	-	(120,160)
Capital		
Dividends	180,000	-

Transactions with Rothesay Holdco UK Limited

	31 December 2015 £000s	31December 2014 £000s
Statement of Comprehensive Income		
Interest on collateralised agreements and financing	213	60
Cost transfer	3	284
Statement of Financial Position		
Other payables	32	-
Other receivables	11,263	5,015
Capital	**383,754**	**383,754**
Dividends	(130,000)	-

Notes to the Financial Statements (continued)

Note 31 – Financial Commitments and Contingencies

Operating Lease Commitment

Operating lease rentals commitments arise where the RL Group company is the lessee in respect of non-cancellable operating lease agreements. Payments made under operating leases (net of any incentives received from the lessor) are charged to the profit and loss on a straight line basis over the period of the lease. The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

RL Group and Company	31 December 2015 £000s	31 December 2014 £000s
Not later than one year	945	420
Later than one year and no later than five years	2,834	3,358
Later than five years	3,359	3,779
Total Minimum Lease Payments	**7,138**	**7,557**

Other Commitments

During the previous years the RL Group executed transactions to purchase partly funded bonds. The RL Group expects to pay a further £197m within the next 5 years (2014: £197m), £24m of this being due within 12 months of the financial reporting date (2014: £nil).

RL Group and Company	31 December 2015 £000s	31 December 2014 £000s
Not later than one year	24,000	-
Later than one year and no later than five years	173,000	197,000
Later than five years	-	-
Other Commitments	**197,000**	**197,000**

Notes to the Financial Statements (continued)

Note 32 – Part VII Transfer

On 1 December 2015, the board approved the transfer of the long-term business of RAL to RLL, the immediate parent company. The transfer was effective from 1 December 2015. All the assets, liabilities and reserves, with the exception of the issued share capital, within RAL's shareholder fund were transferred to the shareholder fund of RLL on the transfer date.

Financial assets and liabilities were transferred at fair value which equates to the carrying value in the Statement of Financial Position. The transfer was for nil consideration in accordance with the scheme of transfer pursuant to Part VII of the Financial Services and Markets Act 2000. The value of the assets transferred was £4,927m at that date.

The following table summarises the assets and liabilities transferred into RLL at the transfer date.

Effect on the Statement of Financial Position:

	Transferred at 1 December 2015 £000s	At 31 December 2015 £000s
Assets		
Investment in subsidiary undertaking	-	2,669
Property, plant and equipment	-	1,988
Financial investments	4,598,898	24,588,952
Reinsurance assets	68,406	273,632
Accrued interest and prepayments	33,415	164,980
Receivables	166,282	392,498
Cash and cash equivalents	59,949	83,574
Total Assets	**4,926,950**	**25,508,293**
Equity and Liabilities		
Share capital	-	183,901
Share premium	-	199,854
Retained earnings	422,202	659,812
Total Equity	**422,202**	**1,043,567**
Liabilities		
Insurance contract liabilities	2,696,912	14,207,475
Payables and financial liabilities	1,804,424	9,878,339
Borrowings	-	348,770
Deferred tax liabilities	609	2,792
Accruals and deferred income	2,803	27,350
Total Equity and Liabilities	**4,926,950**	**25,508,293**