# Solvency and Financial Condition Report

# 31 December 2019

SLF OF CANADA UK LIMITED GROUP OF COMPANIES IN THE EUROPEAN ECONOMIC AREA (THE "EEA GROUP")

INCORPORATING SUN LIFE ASSURANCE COMPANY OF CANADA (U.K.) LIMITED ("SLOC UK" OR "THE COMPANY")

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## Directors' statement

The directors are responsible for ensuring that the Solvency and Financial Condition Report has been properly prepared in all material respects in accordance with the Prudential Regulation Authority ("PRA") rules and Solvency II Regulations.

The directors are satisfied that, throughout the year, the EEA Group and SLOC UK have complied in all material respects with the applicable requirements of the PRA rules and Solvency II Regulations, and that it is reasonable to believe that compliance has continued since the reporting date and will continue in the future.

By order of the Board,

**Katherine Garner**

**Chief Executive Officer**

9 April 2020

# Report of the external independent auditor to the Directors of SLF of Canada UK Limited and to the Directors of Sun Life Assurance Company of Canada (U.K.) Limited ('the company') pursuant to rule 4.1 (2) of the external audit chapter of the PRA Rulebook applicable to Solvency II firms

**Report on the Audit of the relevant elements of the Solvency and Financial Condition Report ("SFCR")**

**Opinion**

Except as stated below, we have audited the following documents prepared by the company as at 31 December 2019:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the SFCR of the company as at 31 December 2019, ('the Narrative Disclosures subject to audit');
- Group templates S.02.01.02, S.23.01.22, S.25.01.22, S.32.01.22 ('the Templates subject to audit'); and
- Solo templates S.02.01.02, S.12.01.02, S.23.01.01, S.25.01.21, S.28.01.01 ('the Templates subject to audit').

The Narrative Disclosures subject to audit and the Templates subject to audit are collectively referred to as the 'relevant elements of the SFCR'.

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

- The 'Summary', 'Business and performance', 'System of governance' and 'Risk profile' elements of the SFCR;
- Group templates S.05.01.02 and S.05.02.01;
- Solo templates S.05.01.02 and S.05.02.01;
- The written acknowledgement by management of their responsibilities, including for the preparation of the SFCR ('the Responsibility Statement'); and
- Information which pertains to an undertaking that is not a Solvency II undertaking and has been prepared in accordance with PRA rules other than those implementing the Solvency II Directive or in accordance with a European Union ("EU") instrument other than the Solvency II regulations ('the sectoral information').

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

In our opinion, the information subject to audit in the relevant elements of the SFCR of the company as at 31 December 2019 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based, as modified by relevant supervisory modifications, and as supplemented by supervisory approvals and determinations.

**Basis for opinion**

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

**Emphasis of Matter – Basis of Accounting**

We draw attention to the 'Valuation for solvency purposes' and 'Capital management' sections of the SFCR, which describe the basis of accounting. The SFCR is prepared in compliance with the financial reporting provisions of the PRA Rules and Solvency II regulations, and therefore in accordance with a special purpose financial reporting framework. The SFCR is required to be published, and intended users include but are not limited to the PRA. As a result, the SFCR may not be suitable for another purpose. Our opinion is not modified in respect of these matters.

**Conclusions relating to going concern**

We are required by ISAs (UK) to report in respect of the following matters where:

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

We have nothing to report in relation to these matters.

**Other Information**

The Directors are responsible for the Other Information.

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

In connection with our audit of the SFCR, our responsibility is to read the Other Information and, in doing so, consider whether the Other Information is materially inconsistent with the relevant elements of the SFCR, or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the relevant elements of the SFCR or a material misstatement of the Other Information. If, based on the work we have performed, we conclude that there is a material misstatement of this Other Information, we are required to report that fact.

We have nothing to report in relation to these matters.

**Responsibilities of Directors for the Solvency and Financial Condition Report**

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

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

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

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

Our objectives are to obtain reasonable assurance about whether the relevant elements of the SFCR are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decision making or the judgement of the users taken on the basis of the SFCR.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: https://www.frc.org.uk/auditorsresponsibilities. The same responsibilities apply to the audit of the SFCR.

**Relevant elements of the SFCR that are not subject to audit**

The relevant elements of the SFCR that are not subject to audit comprise:

- Rows R0110 to R0130 of template S.12.01.02 – Amount of transitional measure on technical provision.

**Report on Other Legal and Regulatory Requirements**

**Sectoral information**

In our opinion, in accordance with Rule 4.2 of the External Audit Chapter of the PRA Rulebook, the sectoral information has been properly compiled in accordance with the PRA rules and EU instruments relating to that undertaking from information provided by members of the group and the relevant insurance group undertaking.

**Other information**

In accordance with Rule 4.1 (3) of the External Audit Chapter of the PRA Rulebook for Solvency II firms we are required to consider whether the Other Information is materially inconsistent with our knowledge obtained in the audit of the company's statutory financial statements. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in relation to this matter.

**Use of our Report**

This report is made solely to the Directors of the company in accordance with Rule 4.1 (2) of the External Audit Chapter of the PRA Rulebook for Solvency II firms. We acknowledge that our report will be provided to the PRA for the use of the PRA solely for the purposes set down by statute and the PRA's rules. Our audit work has been undertaken so that we might state to the Directors of SLF of Canada UK Limited and the Directors of the company matters we are required to state to them in an auditor's report on the relevant elements of the SFCR and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the PRA, for our audit work, for this report or for the opinions we have formed.

Paul Stephenson BA FCA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Statutory Auditor
London, UK
9 April 2020

# Summary

**Sun Life Financial of Canada business in the UK**

The EEA Group is a closed book life insurance business that has a portfolio of pension, life and annuity products. It is wholly owned by Sun Life Assurance Company of Canada ("SLACC") and the ultimate parent is Sun Life Financial Inc., both of which are Canadian companies. SLOC UK is the only regulated company within the EEA Group and is responsible for managing all insurance business. It gives rise to materially all risks and performance of the EEA Group.

SLOC UK profit after tax per the financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the EU for 2019: £41 million (2018: £14 million).

On 28 January 2019, the company paid an upfront charge of £23.9 million to enter an expense indemnity agreement with SLACC, effective for 30 years from 1 January 2019. The indemnity agreement sets a cap on the level of governance expenses per policy, increasing with inflation. Under the agreement, governance expenses above the cap are reimbursed to the company by SLACC. The indemnity agreement provides protection against expense shocks and diseconomies of scale.

The current Covid-19 pandemic has had a profound effect on markets. Given the extreme market conditions, the solvency position is being continuously monitored and remains in excess of risk appetite. *Section A.1.3 Covid-19* describes the operational response to the pandemic and the impact on the Risk Management System ("RMS") is described in *Section C.7.5 Covid-19*.

**Solvency and financial condition**

The Pillar 1 solvency ratio of SLOC UK as at 31 December 2019 was 186% (2018: 178%), with a Solvency Capital Requirement ("SCR") of £213.7 million (2018: £237.9 million) and eligible own funds to cover it of £397.5 million (2018: £424.3 million), all of which was tier 1 capital, the highest quality of capital in terms of permanence and ability to absorb losses should they arise. The total assets measured on a Solvency II basis were £14.0 billion (2018: £13.7 billion). Dividends paid in 2019 to SLF of Canada UK Limited, its parent, totalled £56.0 million and it is expected that a dividend of £66.0 million will be paid in 2020.

The EEA Group containing SLOC UK had a solvency ratio of 187% as at 31 December 2019 (2018: 179%) with an SCR of £213.7 million (2018: £237.9 million) and eligible own funds of £399.7 million (2018: £426.5 million) which, as for SLOC UK, was all tier 1 capital. The total assets on a Solvency II basis were £14.0 billion (2018: £13.7 billion). In 2019, a dividend of £56.0 million was paid to SLACC. It is expected that a dividend of £66.0 million will be paid in 2020.

The capital requirements of SLOC UK and the EEA Group are calculated using the Solvency II standard formula methodology and the own funds are measured using Solvency II valuation principles.

**System of governance**

A strong system of governance is in place with clear responsibilities, authorities and delegations to operate it and manage the business in a robust manner.

The business operates a 'Three Lines of Defence' governance model, where business functions are responsible for day-to-day operations, Compliance and Risk functions provide oversight and challenge and the Internal Audit function provides independent assurance.

The RMS has been developed in alignment with Solvency II guidelines and is actively used in managing the business. It enables management of the inherent risks in the business, supporting the achievement of business objectives. Therefore, its effective operation has benefits for both internal and external stakeholders.

**Own Risk and Solvency Assessment ("ORSA") results**

The 2019 ORSA process for the EEA Group and SLOC UK took into account all material risks of the business. The 2019 ORSA, approved by the Board in June 2019, showed that the company is expected to remain above its solvency risk appetite threshold and generate surplus throughout the five-year ORSA projection period. In respect of sensitivities and scenario analyses, SLOC UK is well placed to withstand shocks over the five-year ORSA period, remaining above regulatory solvency requirements and the internal risk appetite threshold, albeit with reduced dividend payments.

The 2019 ORSA showed that regulatory and other externally driven changes are considered to be the most significant risks facing the company. The top contributors to both Pillar 1 and Pillar 2 risk capital are lapse, equity and expense risk, all of which are closely monitored and managed. Lapse, equity and expense risk are within risk appetite and are expected to remain so for at least the five-year ORSA projection period. Under Pillar 2, credit spread risk capital is also significant because of the contribution of the staff pension scheme, however, Pillar 1 has the higher diversified capital requirement and on this basis, spread risk is less material.

The 2019 ORSA concludes that there are no material risks arising from the World-Wide Group of Sun Life Financial of Canada companies ("WWG") that are not mitigated by treaty, governance, contract or capital where applicable.

# A. Business and Performance

## A.1 Business

### A.1.1 Introduction

The SLOC UK business is a closed book life insurance business consisting of a portfolio of life, pension and annuity products all of which are in the UK, except for a small book of overseas business accounting for less than 1% of total premiums. SLOC UK most recently closed to new business from 2010, except for issuing annuity contracts arising from the vesting of individual pension plans already within the business, and the majority of this activity ceased in 2013. Management is therefore focused on managing the existing in-force business in a controlled way whilst ensuring high quality outcomes for customers.

The EEA Group is a group of UK companies as described in *Section A.1.2 Subsidiaries and branches*, which is wholly owned by SLACC, the Canadian immediate parent company. The EEA Group contains one regulated company: SLOC UK, a life insurance company. The performance and risks of the EEA Group are not materially different from those of SLOC UK. All other companies are holding companies or provide services ancillary to SLOC UK.

The EEA Group provides its parent with access to a mature market that generates capital, the surplus of which can be repatriated to SLACC and upwards to the ultimate parent Sun Life Financial Inc., subject to board approval and local regulatory constraints. In return, the business is supported operationally by, and is underpinned by, the solid foundation of the WWG although it is not the EEA Group's intention to rely on capital from its parent company.

The EEA Group operates an outsourced business model having outsourced its investment management in 2001 and the administration of its business in 2002. The company has recently entered an agreement to transition the financial reporting aspects of the in-house actuarial team to a specialist external provider, Towers Watson Limited, to complete June 2021.

### A.1.2 Subsidiaries and branches

The EEA Group consists of a number of wholly owned subsidiaries. SLF of Canada UK Limited is the top EEA Group holding company and is a wholly owned subsidiary of SLACC, which, in turn, is a wholly owned subsidiary of Sun Life Financial Inc.

The EEA Group consists of the following subsidiary undertakings:

| Name of subsidiary undertaking | Principal activity |
|---|---|
| SLF of Canada UK Limited | Top holding company of various wholly owned subsidiary undertakings in the EEA Group |
| Sun Life Assurance Company of Canada (U.K.) Limited | Insurance company which manages individual life, pension and annuity policies |
| Sun Life of Canada UK Holdings Limited | Intermediate holding company of various wholly owned subsidiary undertakings |
| SLFC Services Company (UK) Limited | Provision of management and administrative services to the EEA Group |
| Laurtrust Limited | Pension Trustee company |
| Barnwood Properties Limited | Property investment |

All companies in the EEA Group are limited by shares.

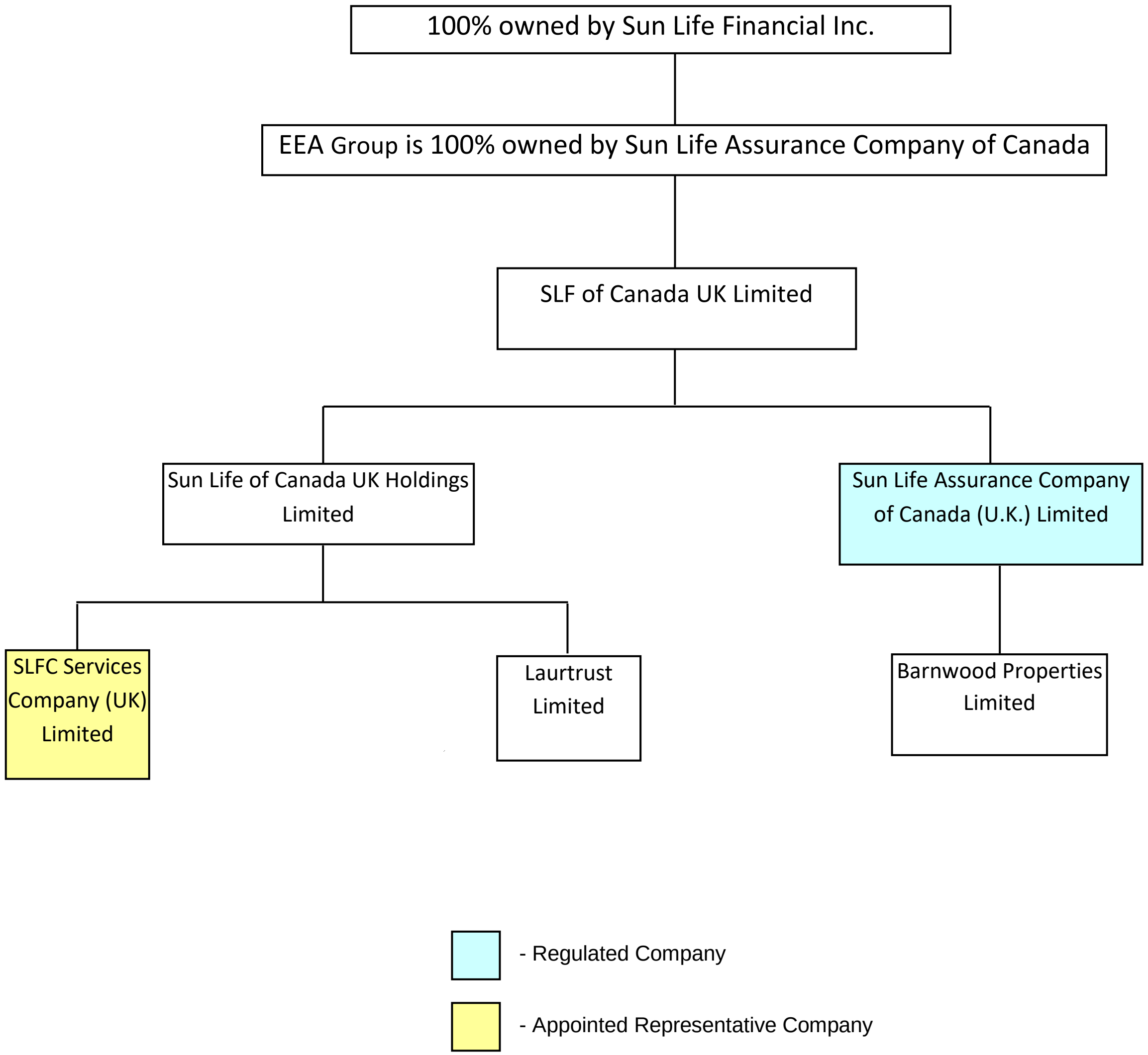
SLOC UK is authorised by the PRA, Threadneedle Street, London EC2R 8AH and regulated by the Financial Conduct Authority ("FCA"), 12 Endeavour Square, London E20 1JN and the PRA. The EEA Group is supervised by the PRA.

The auditor of all companies in the EEA Group that are subject to audit is Deloitte LLP, 1 New Street Square, London EC4A 3HQ.

No consolidated financial statements for the EEA Group are prepared on the basis of the exemption provided by Section 401 of the Companies Act 2006 and IFRS 10, Consolidated Financial Statements, paragraph 4(a). The EEA Group accounts are consolidated in the financial statements of SLACC and Sun Life Financial Inc.

During 2020, it is expected that a dividend of £66.0 million will be paid from SLOC UK to SLF of Canada UK Limited and that SLF of Canada UK Limited will pay a dividend of £66.0 million to SLACC.

## EEA GROUP STRUCTURE AND OWNERSHIP
## AS AT 31 DECEMBER 2019



**A.1.3 Covid-19**

The current Covid-19 pandemic has had a profound effect on markets. Given the extreme market conditions, the solvency position is being continuously monitored and remains in excess of risk appetite. The crisis management plan has been invoked. The business remains committed to delivering services to customers, working collaboratively with key outsourcers, focusing on ensuring payments out continue uninterrupted and with no loss of controls. The health and well-being of employees is of critical importance and, to that end, a predominantly working from home model has been adopted. Stress testing undertaken as part of the ORSA has included pandemic scenarios and demonstrates the business is financially strong, although the ultimate result of the Covid-19 pandemic is uncertain, and is likely to be for some time. The impact on the RMS is described further in *Section C.7.5 Covid-19*.

**A.1.4 Distributions to shareholders**

During 2019, SLOC UK paid a £56.0 million dividend to SLF of Canada UK Limited, its parent.

SLF of Canada UK Limited paid a dividend of £56.0 million to SLACC, its parent.

# A.2 Underwriting performance as per the financial statements

As a closed book life insurer, the underwriting performance as per the financial statements is described below in terms of premiums, claims and expenses.

Premiums, claims and benefits as per the financial statements, shown in the tables below, exclude premiums, claims and benefits on linked investment contracts. The premiums, claims and benefits shown in the quantitative reporting templates in the appendices include premiums, claims and benefits on linked investment contracts.

**Underwriting performance for the year ended 31 December 2019**

| **£ million** | **SLOC UK TOTAL** | Linked | With-profits | Non-linked, non-profit |
|---|---|---|---|---|
| *Earned premiums, net of reinsurance* | 50 | 43 | 6 | 1 |
| *Net claims and benefits paid* | (405) | (323) | (69) | (13) |
| *Administrative and other expenses (excluding investment management expenses)* | (73) | (61) | (3) | (9) |

The change in insurance and investment contract liabilities in the year was an increase of £603 million. Their value is sensitive to changes in market factors, policyholder activity and changes in the methodologies and assumptions used in their calculation.

**Underwriting performance for the year ended 31 December 2018**

| **£ million** | **SLOC UK TOTAL** | Linked | With-profits | Non-linked, non-profit |
|---|---|---|---|---|
| *Earned premiums, net of reinsurance* | 54 | 45 | 7 | 2 |
| *Net claims and benefits paid* | (412) | (328) | (74) | (10) |
| *Administrative and other expenses (excluding investment management expenses)* | (57) | (41) | (7) | (9) |

Premiums, claims and benefits in 2019 are lower than those in 2018, consistent with the reduction in existing business. Expenses are higher in 2019 than in 2018, predominantly due to the upfront charge paid in 2019 for entering into the expense indemnity agreement.

# A.3 Investment performance as per the financial statements

**Investment return net of reinsurance for the year ended 31 December 2019 by line of business**

| **£ million** | **SLOC UK TOTAL** | Linked | With-profits | Non-linked, non-profit |
|---|---|---|---|---|
| *Investment return, net of reinsurance* | 1,081 | 992 | 55 | 35 |
| *Investment management expenses* | (20) | (16) | (1) | (3) |

**Investment return gross of reinsurance for the year ended 31 December 2019 by asset class**

| **£ million** | **Income** | **Gains / (losses)** |
|---|---|---|
| **Asset Class** | | |
| *Bonds* | 133 | 222 |
| *Equities* | 176 | 823 |
| *Property* | 13 | (6) |
| *Other* | 13 | 67 |
| **TOTAL Investment Performance** | **335** | **1,106** |

**Investment return net of reinsurance for the year ended 31 December 2018 by line of business**

| **£ million** | **SLOC UK TOTAL** | Linked | With-profits | Non-linked, non-profit |
|---|---|---|---|---|
| *Investment return, net of reinsurance* | (418) | (415) | (5) | 2 |
| *Investment management expenses* | (20) | (17) | (1) | (2) |

**Investment return gross of reinsurance for the year ended 31 December 2018 by asset class**

| £ million | Income | Gains / (losses) |
|---|---|---|
| **Asset Class** | | |
| *Bonds* | 146 | (146) |
| *Equities* | 173 | (624) |
| *Property* | 12 | 10 |
| *Other* | 9 | (16) |
| **TOTAL Investment Performance** | **340** | **(776)** |

Investment income by asset class is similar in 2019 to 2018, reflecting the stability of the investment portfolios, which is consistent with the stability of the closed book of business. Gains and losses are driven by markets and the differences between gains and losses on bonds, equities and property in 2019 compared to those of 2018 reflect the performance of the bond, equities and property markets in 2019 and 2018.

**Securitisations**

SLOC UK's investment manager guidelines do not allow new purchases in securitisations. However, a small amount of legacy holdings (£84 million as at 31 December 2019) remains (£85 million at 31 December 2018). Trading is monitored for any breach of the guidelines.

## A.4 Performance of other activities as per the financial statements

**Tax**

In 2019 there was a tax charge of £36 million. This compares with a tax credit of £20 million in 2018. The large tax variance was primarily due to factors as follows:

- Significant gains arising on investments in 2019 compared to losses in 2018. This reflects the continued volatility in both UK and overseas investment markets; and
- Taxable pension business profits arising in the year compared to losses in 2018.

**Lease arrangements**

SLOC UK leases its premises from Threadneedle Pensions Limited and sublets part of the premises to a third party.

The rent paid by SLOC UK in 2019 was £0.4 million (2018: £0.4 million) and the rent received was £0.2 million (2018: £0.2 million).

A right of use asset and lease liability have been set up in 2019, in accordance with the new standard IFRS 16 'Leases'. The depreciation of the asset and reduction in liability broadly offset.

**Fees and commission income**

Fees from non-profit investment contracts, commissions and other income from arrangements with reinsurers and introduction fees from a third party annuity provider were £46 million (2018: £47 million).

## A.5 Any other information

**Related party transactions**

SLOC UK has an agreement with SLFC Services Company (UK) Ltd to pay any management and administration expenses incurred on its behalf on a monthly basis.

In 2019, the value of services provided by SLFC Services Company (UK) Ltd was £27 million (2018: £25 million). The outstanding balance at 31 December 2019 was £5 million (2018: £1 million).

# B. System of governance

## B.1 General information on the system of governance

### B.1.1 The Board and delegations of authority

The Board of Directors ("the Board") of SLOC UK has responsibility for oversight of operations to ensure, amongst other matters, competent and prudent management, sound planning, an adequate and effective system of risk management, an adequate and effective system of internal control, adequate accounting and other records and compliance with statutory and regulatory obligations. The system of governance is appropriate to the nature, scale and complexity of the business.

The Senior Management Regime component of the Senior Managers and Certification Regime was implemented during 2018 and the management and governance of SLOC UK is described extensively in the Management Responsibilities Map. This includes the attribution of senior manager functions and all prescribed responsibilities, and the categorisation of key functions, key function holders, material risk takers and certified functions.

The Board is authorised, pursuant to its Articles of Association, to delegate certain of its powers to either the Chief Executive Officer ("CEO") or to a Board Committee. The extent of the delegated authority is limited by:

- Matters on which the Board may not delegate authority as stipulated in the Terms of Reference of the Board, including the approval of material transactions;
- Matters where the Board has elected to designate specific authority to another individual or committee; and
- Any policies, standards or operating guidelines approved or adopted by the Board or a Policy Review Committee.

Currently the Board has delegated certain matters to the Risk Committee and the Audit and Compliance Committee ("ACC"). The Board also obtains advice on the with-profits business from its independent With-Profits Committee ("WPC"). The Board Committees perform the following tasks on its behalf:

- Risk Committee: The primary functions of the Risk Committee are to oversee, monitor and review, and advise the Board on current and potential risk exposures and future risk strategy. In particular, the Risk Committee ensures that major downside risks facing the business are identified, policies and controls are in place for management to ensure that those risks are effectively managed, and oversees compliance with risk management policies and controls.
- ACC: The primary functions of the ACC are to assist the Board with its oversight role in relation to the integrity of the financial statements, financial reporting processes and regulatory filings. There is particular focus on the adequacy and effectiveness of internal controls, Internal Audit plans and actions, compliance with regulatory requirements, and the relationship with, and the performance of, the external auditor.
- WPC: Provides independent advice to the Board in respect of matters that affect the with-profits business.

The Board delegates the day-to-day operational management to the CEO. In turn, the CEO delegates certain functional responsibilities to each direct report and this delegation is set out in each of their respective role profiles and Statements of Responsibility. Collectively these individuals and the Head of Legal and Company Secretary form the UK Management Committee, which meets fortnightly. Its main function is the oversight of the delegated functional responsibilities of the CEO's direct reports.

To assist the CEO's direct reports in discharging their functional and regulatory-prescribed responsibilities (pursuant to their Statements of Responsibility) the direct reports may onwards delegate a responsibility either through line management (to their direct reports) or to a group of individuals (a management committee), as described in the Management Responsibilities Map. The roles of the CEO and the CEO's direct reports are summarised below:

| **Role** | **Description** |
|---|---|
| CEO | To oversee the day-to-day management and associated risks of the business, to lead the development and delivery of strategy and business plans, and provide leadership to staff, ensuring that the desired culture is adopted and embedded throughout the organisation. Day-to-day operations include, but are not limited to, risk management, internal controls, accounting records, and compliance with statutory and regulatory obligations. The role is ultimately accountable for the day-to-day performance of all the identified Key Functions and Key Business Areas, as set out in the Management Responsibilities Map. |
| Chief Operating Officer ("COO") | To ensure that requirements set by the business and relevant statutory and regulatory obligations are met, the COO is empowered to:<br>• Be responsible for the management of the day-to-day operations within designated areas of functional responsibility, including the ownership of their risks and leadership of those functions;<br>• Serve as a director or trustee to certain EEA Group legal entities and pension schemes; and<br>• Act as the designated locum to the CEO. |
| Chief Financial Officer ("CFO") | To ensure that requirements set by the business and relevant statutory and regulatory obligations are met, and to ensure sound financial management, the CFO is responsible for:<br>• The management of the day-to-day operations within designated areas of functional responsibility including the ownership of their risks and leadership of those functions;<br>• The provision of a financial perspective and reporting to management, the Board and its committees;<br>• Liaison with the WWG corporate finance function and related business groups to integrate UK financial results with WWG financial statements and strategies, and the overall promotion of consistency in the development and use of accounting methods, standards and processes; and<br>• Serving as a director to certain EEA Group legal entities. |
| Chief Actuary | To ensure requirements set by the business, and relevant statutory and regulatory obligations are met, the Chief Actuary is responsible for:<br>• The management of the day-to-day operations within designated areas of functional responsibility including the ownership of their risks and leadership of those functions;<br>• The provision of actuarial perspective and reporting to management, the Board and its committees;<br>• Liaison with the WWG actuarial function and related business groups to promote consistency in the developments and use of actuarial methods, standards and processes; and<br>• Serving as a director of certain EEA Group legal entities. |

| Role | Description |
|---|---|
| Chief Risk Officer ("CRO") | To ensure requirements set by the business and relevant statutory and regulatory obligations are met, the CRO is responsible for:<br>• The management of the day-to-day operations of the 2nd line Risk and Compliance Function, including the ownership of their risks and leadership of those functions;<br>• The establishment of a RMS and assurance over its effective operation;<br>• The provision of risk perspectives and reporting to management, the Board and its committees; and<br>• Liaison with the WWG risk function and related business groups to integrate UK risk results with WWG risk assessments and strategies, and the overall promotion of consistency in the development and use of risk methods, standards and processes. |

These key roles are supported in exerting their mandates by six management committees.

The following table describes how individual responsibilities for Key Functions are allocated, demonstrating appropriate segregation and coverage of both regulatory and business requirements:

| **Key Function**<br>***mandatory as a Solvency II firm**<br>****regulator recommends for consideration**<br>*****discretionary inclusion** | **Responsible Senior Manager** | **Key Function Holder (if not allocated to a Senior Manager)** | **Individuals in support of Key Function who fall within the Certification Regime)** |
|---|---|---|---|
| Actuarial* | Chief Actuary | n/a | Head of Product Management<br>Head of Valuation<br>Head of Capital |
| Risk Management* | CRO | n/a | None |
| Compliance* | Head of Compliance & Money Laundering Reporting Officer | n/a | None |
| Internal Audit* | Head of Internal Audit & Controls Assurance | n/a | None |
| Finance** | CFO | n/a | Financial Controller |
| Tax** | CFO | n/a | Head of UK Tax Operations |
| Capital Management** | CFO | n/a | None |
| Liquidity Management** | CFO | n/a | None |
| Reinsurance** | Chief Actuary | n/a | Head of Product Management |
| Asset and Liability Management** | Chief Actuary | n/a | None |

| **Key Function**<br>***mandatory as a Solvency II firm**<br>****regulator recommends for consideration**<br>*****discretionary inclusion** | **Responsible Senior Manager** | **Key Function Holder (if not allocated to a Senior Manager)** | **Individuals in support of Key Function who fall within the Certification Regime)** |
|---|---|---|---|
| Investment Management** | COO | n/a | Head of Investments |
| Information Technology ("IT")** | COO | n/a | IT Manager |
| Operational Systems and Controls** | COO | n/a | Head of Operations |
| Data Protection*** | n/a | Data Protection Officer | None |

**B.1.2 Risk management**

The "Three Lines of Defence" governance model is adopted for risk management and is used to assign specific risk management responsibilities across the business. This is described further in *Section B.4 Internal control system*.

Each year the Board sets risk appetites within which the company is required to manage risk. Collectively the three lines of defence are responsible for identifying, measuring, managing, monitoring and reporting risk to the Risk and Compliance Management Committee ("RCMC"), Risk Committee and the Board so that it remains within these approved appetites.

The RMS is discussed further in *Section B.3 Risk management system including the own risk and solvency assessment.*

**B.1.3 Internal Audit**

The Board and the WWG Chief Auditor delegate authority to the Head of Internal Audit to carry out the internal audit function.

The Board is ultimately responsible for the system of internal controls and reviewing its effectiveness. Acting as the 3rd line of defence, the Internal Audit function provides assurance over the operation of the system of internal controls and that the risk management, governance and internal control processes are operating effectively.

The Internal Audit function operates under the WWG Chief Internal Auditor's mandate that is reviewed and approved annually and provides independent assurance to the ACC, the Board and to Sun Life Financial Inc. as to the effectiveness and adequacy of the internal control system. It is responsible for assessing whether an effective and adequate internal control framework is adopted by management. In carrying out its mandate, the Internal Audit function has the authority to audit and investigate any activity, with unrestricted access to records, information and personnel throughout the organisation relevant to the performance of the Internal Audit function.

Independence of the Internal Audit function is further assured by features of the role of Head of Internal Audit including:

- The role profile and statement of responsibility for the Head of Internal Audit must be approved by the ACC; and
- The Head of Internal Audit has unrestricted access to the Chair of the Board, to the Chair of the ACC and to the ACC itself with, and without, the presence of executive management.

**B.1.4 Compliance**

Compliance is a 2nd line of defence function that is responsible for ensuring regulatory requirements are understood and implemented within the business (including where these requirements are fulfilled on behalf of SLOC UK by outsourced service providers), and for conducting a risk-based compliance monitoring programme. This includes the management of regulatory relationships, the provision of some regulatory reporting (a responsibility shared with the CFO), the provision of compliance advice, and the performance of compliance monitoring to assess and report on the effectiveness of the measures in place to detect and minimise compliance risk. The Compliance function is described in more detail in *Section B.4.2 The Compliance function*.

The Head of Compliance is a regulatory-approved Senior Manager. The appointment has the following additional features provided within the SLOC UK system of governance:

- The role profile and statement of responsibility for the Head of Compliance must be approved by the ACC; and
- The Head of Compliance has unrestricted access to the Chair of the Board, the Chair and members of the ACC both with, and without, the presence of executive management.

**B.1.5 Governance across the EEA Group**

Governance, risk management and internal control is applied to each legal entity in the EEA Group proportionately in accordance with the activities of each entity.

The system of governance is periodically reviewed both internally and externally to ensure that it remains fit for purpose. Such reviews take into account the current strategy to ensure that the governance is proportionate to the strategy and the risks identified with that strategy.

**B.1.6 Remuneration**

The primary compensation objectives are to align employee interests with the interests of customers and the shareholder while attracting, retaining and rewarding employees. The compensation model rewards employees for achieving business goals and individual performance.

For employees below CEO level, each element of compensation is generally targeted at the median pay level of peer companies, with the variable compensation amount adjusted based on achievement of both business and individual performance goals. This philosophy ensures superior performance drives reward that is above target, while poor performance results in reward that is below target.

For employees below CEO level, salary ranges for each job band are designed so the middle of the range aligns with median competitive salaries for similar roles at peer companies. Individual salaries are determined by the appropriate manager within these ranges based on an assessment of the scope and mandate of the role and the individual's experience and performance.

For employees below CEO level, annual incentive and long-term incentive target award levels are based on median competitive practice. Based on plan design, the actual pay-out of incentives varies above and below target based on business results, including an overall measure of risk, and individual performance.

For the CEO, remuneration is considered at a total compensation level. Total compensation is benchmarked to market median. Total compensation is split into salary, annual incentive and long-term incentive awards.

#### B.1.6.1 Pay mix

The mix of salary, annual incentives and long-term incentives is set annually by the WWG Board, is adopted by the UK Board and provides executive compensation frameworks for executive level positions.

Below executive level, the mix of compensation is based on salary structures, target Annual Incentive Plan ("AIP") levels, Long-term Incentive Plan participation rates and target award levels.

The executive compensation frameworks outline the portion of variable and deferred incentive compensation by position level based on target performance. More senior roles have more compensation that is at-risk, with greater weight placed on long-term incentives which are awarded in various share-based instruments, and promote effective risk management by incentivising sound decision making that is in the interests of the long-term health of the organisation.

#### B.1.6.2 Pay for performance

Compensation programmes are designed to ensure positive customer outcomes, reflect our financial performance and do not encourage excessive risk taking. All incentive compensation plans are performance based and include appropriate measures of performance over different time horizons for different employee levels.

The AIP measures performance on an annual basis and reflects success in executing against annual financial and non-financial measures aligned to the annual business plan approved by the Board.

Long-term incentives reflect various mid- and long-term performance measures and ensure a substantial portion of compensation is deferred over at least a three-year period. Additional performance vesting criteria are used for more senior executives to align compensation with other measures of long-term value creation and to achieve a wider range of pay outcomes tied to performance.

The proportion of variable pay that is deferred for three years or more is greater for more senior roles.

## B.2 Fitness and propriety requirements

#### B.2.1 Fitness and propriety

Nominated individuals in the business, by virtue of their regulatory designation as a Senior Manager or Certified Function, are deemed to satisfy fitness and propriety requirements on an ongoing basis through the following processes:

- Prior to the taking up of a new appointment, all Senior Managers and Certified Functions are subject to a criminal record check and a regulatory reference check from financial services firms covering the previous six years of employment, including those in overseas jurisdictions;

- Prior to their approval, Senior Managers may be interviewed by one or more of the regulators in order to determine their fitness to perform the role for which they are applying;
- Prior to appointment as Certified Functions, these individuals are subject to an appropriate selection process, led by Human Resources ("HR"), which determines their fitness to perform the role for which they are applying;
- All Senior Managers and Certified Functions are subject to an annual re-assessment of their fitness and propriety. This involves a self-assessment and declaration of their honesty, integrity and financial soundness, followed by a review and sign-off by the respective Heads of Compliance and HR; and
- In the event a non-executive director ("NED") is not also an approved Senior Manager ('a notified NED'), they will still be subject to the company's pre-appointment checks and post-appointment annual re-assessment of their fitness and propriety.

#### B.2.2 Role requirements

Throughout the organisation, each role has a documented role profile outlining the purpose and key accountabilities of the role and the levels of knowledge, skill and competence required to perform the role, along with any professional examination requirements. Those roles designated as Senior Managers have a Statement of Responsibility that includes their role profile as well as their regulatory designations, their prescribed responsibilities and their delegations.

Any knowledge, skills or examination shortfalls, required to achieve competency for the role must be made clear to the individual at offer and appointment stage. Evidence that this has been actioned is retained in the employee file as appropriate. All offers to Senior Managers are subject to regulatory pre-approval. Development needs may also need to be provided to the regulators as part of the Senior Manager's approval process.

#### B.2.3 Performance management

For all employees, on-going competency is evidenced through the annual performance review process and recorded on a performance management system. For each job level, there is a set of competency descriptors.

The Terms of Reference of the Board require that the contributions, effectiveness and performance of each Director, including the Chair of the Board, the Chair of each Board Committee, the Chair of the WPC and the With-Profits Actuary are reviewed annually.

#### B.2.4 Competencies

During the recruitment process, evidence of the competencies considered critical for the particular role is assessed, in addition to functional knowledge, experience and skill. The robust recruitment process also aims to ensure that there is a good cultural fit between the candidate and the business.

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

The RMS is an integral element of the system of governance and is consistent with WWG's approach to risk management.

### B.3.1 RMS and its components

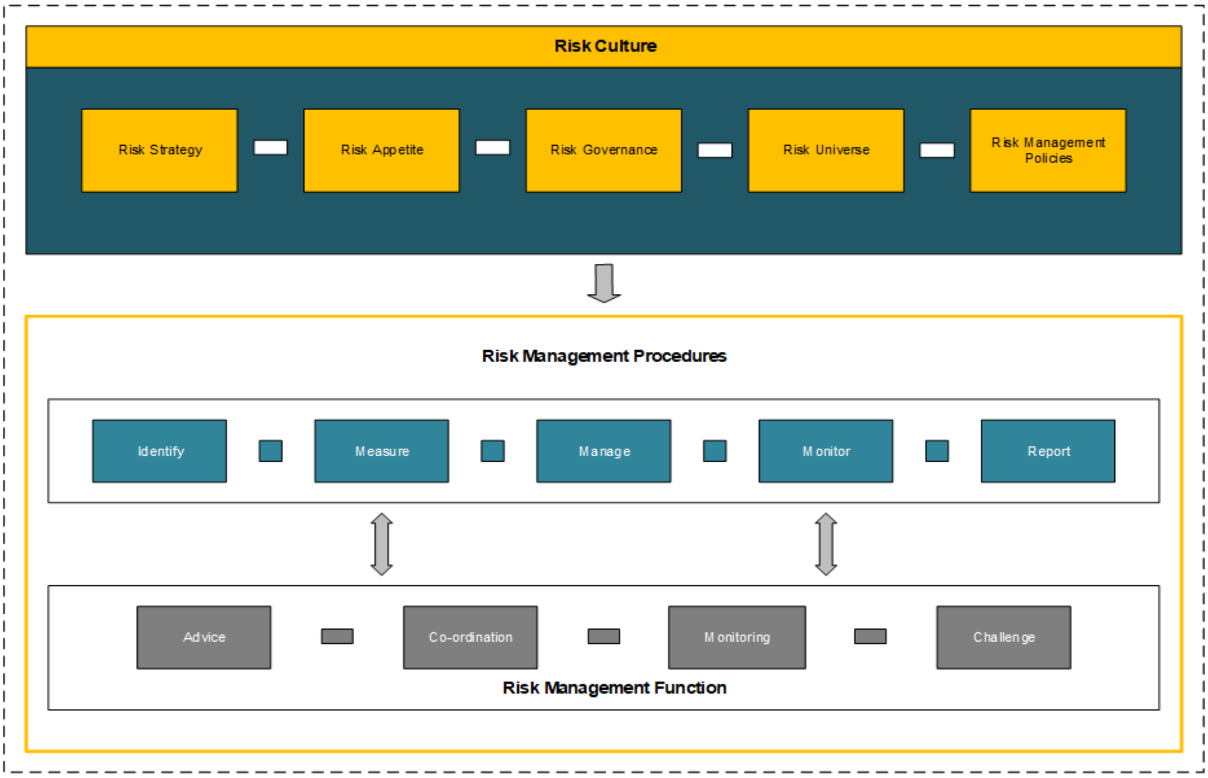
SLOC UK uses the RMS to quantify and manage risks and to ensure an appropriate forward-looking focus on emerging risks. The RMS uses Solvency II methodology and, under this methodology, SLOC UK continues to be defined as a standard formula firm. The components of the RMS are:

- Risk strategy;
- Risk appetite;
- Risk governance;
- A defined risk universe; and
- Risk management policies.

These are described in more detail in *Section B.3.2 Risk culture*.

Operation of the RMS is the responsibility of the CEO and the UK Management Committee. Monitoring the application of the RMS is the responsibility of the CRO.

The RMS consists of the components shown in the diagram below.




### B.3.2 Risk culture

The RMS components exist under an overarching risk culture supported by risk management procedures.

The risk culture is a set of shared attitudes, values and practices that characterise how the company deals with risk in its day-to-day activities. This culture is carefully aligned with the other components of the RMS.

#### B.3.2.1 Risk strategy

SLOC UK accepts selected risks provided there is an appropriate level of return. In accepting those strategically inherent risks, the company seeks to ensure that appropriate and sufficient skills and capabilities are retained to manage them. The risk strategy is approved by the Board and is consistent with the objectives articulated within the Plan.

#### B.3.2.2 Risk appetite

Risk appetite is defined as the type and level of risk that a firm is willing to accept in pursuit of its business objectives. Risk appetite demonstrates a clear link between risk and our business decisions. It sets out the amount of risk we can accept while still achieving earnings and capital targets, as well as other strategic objectives.

The company has a prudent appetite towards risk. This informs, and is complementary to, the business strategy. Risks are accepted under the following scenarios:

- Where the risk is core and inherent in the business, such as equity risk;
- Where the company receives a suitable reward for accepting the risk; and
- Where the company has proven expertise to manage the risk, such as outsourcing arrangements.

Core risks can lend themselves to an individual appetite being set or may be consolidated as part of an aggregated portfolio view.

The company seeks to remove, reduce or not take risk under the following scenarios:

- Where the risk is non-core;
- Where the company does not receive suitable reward for accepting the risk; and
- Where the company does not have sufficient expertise to manage the risk, such as annuity pricing risk.

By definition, the risk appetite for non-core risks will be very low but will lend itself to expression qualitatively. Conduct and cyber risk are examples, as are most operational risks.

The management of both core and non-core risk is subject to the cost / efficiency of doing so.

#### B.3.2.3 Risk governance

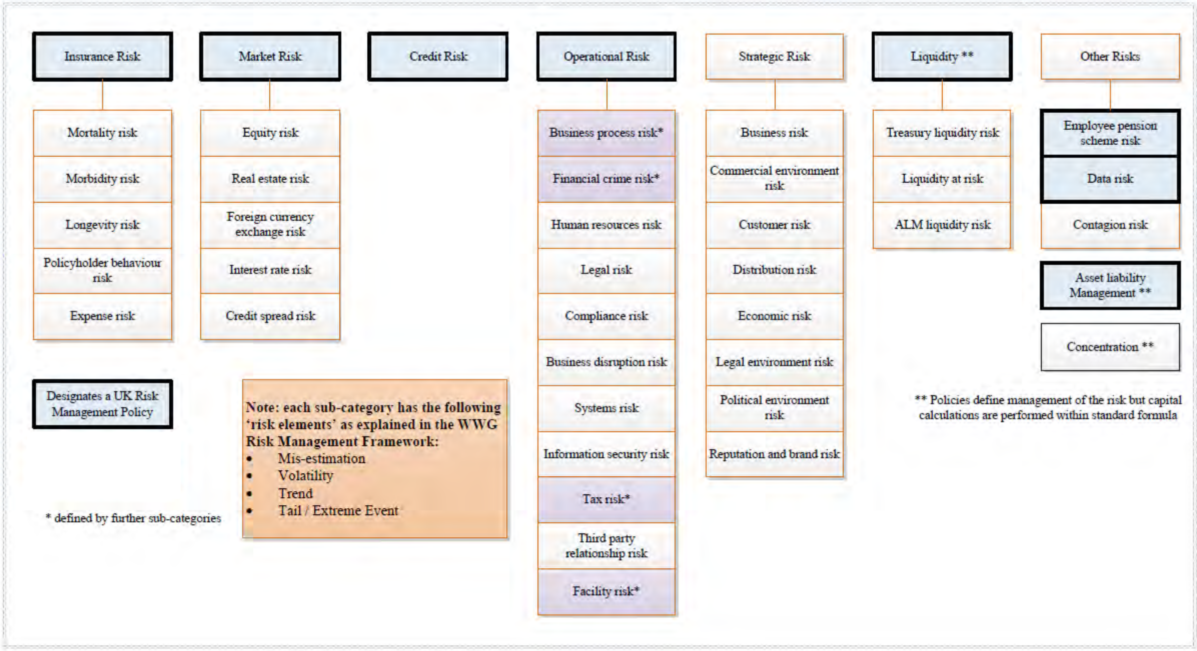
The RMS uses a 'Three Lines of Defence' model described in *Section B.4.1 Three Lines of Defence*. The risk universe provides a structure and common terminology for grouping and reporting on risk.

#### B.3.2.4 Risk universe

In the application of the RMS, risks are considered under the categories set out below. These risks are discussed further in *Section C. Risk profile.* The Identify, Measure, Manage, Monitor and Report ("IMMMR") concepts, as defined in *Section B.3.3 Risk management procedures,* are applied to this risk universe.

Within operational risk, some categories of risk are further analysed in order to ensure risks are defined and managed at the correct level of granularity. These are identified as purple boxes in the diagram below.

The management of the risks within the risk universe is defined by the application of a suite of risk management policies.




### B.3.2.5 Risk management policies

As part of the operation of the RMS, the Risk function defines individual risk policies. The principles and governance of these is set out within an overarching Risk Management Policy. The Board adopts, on the recommendation of the Board sub committees, or in a limited number of cases executive committees, policies that govern the activity of the business.

The risk policies of the business are aligned to the risk universe described in *Section B.3.2.4 Risk universe*. Policies are supported by operating guidelines as required and detailed processes as necessary. Outside of the risk management policies, other policies exist (for example, policies on internal control, internal audit and remuneration).

### B.3.3 Risk management procedures

The RMS sets out a risk management cycle that consists of five stages and operates continuously, involving business management and the Risk and Compliance functions:

- ***Identify*** – business management is primarily responsible for identifying current and emerging risks and opportunities that could impact the business.
- ***Measure*** – each identified risk is assessed by business management for its likelihood of occurrence and potential impact on the business measured in financial or non-financial terms. The Risk function reviews and challenges the risk assessment, including the assessment methodologies and tools used, such as models, stress testing and scenario analysis.
- ***Manage*** – There are four options: avoid, transfer, control or accept. The first three require action to be taken, for example to improve a process control that requires improvement so it better mitigates a risk and keeps the business within its risk appetite.
- ***Monitor*** – having assessed and responded to risks, the risk and the actions being taken are monitored, as are possible "key risk indicators" that a risk may crystallise.

- ***Report*** – reporting is the final step in the risk management process. Accurate, clear and timely reporting of current and emerging risks is presented to those who need to know about them in the organisation. Sufficient detail is provided to allow users to make risk-informed decisions.

Collectively, this is known as the IMMMR process.

**B.3.4 Prudent Person Principle in relation to investments**

The investment strategy is approved by the Board. The risk management aspect of the strategy is operationalised through application of the Prudent Person Principle. The Principle requires, among other things, SLOC UK to demonstrate that it identifies, measures, monitors, manages, controls and reports on the risks arising from investments, as well as ensuring that assets are invested in a manner that is appropriate given the nature and duration of the liabilities.

SLOC UK has a number of investment policies in place, which contain details of the risk appetite requirements relevant to the investment portfolios. Measurement against key risks is undertaken quarterly as part of the risk control self-assessment process. Using this process, the business (Line 1 functions) ranks itself against key risks. This ranking is then challenged by Line 2 functions. See *Section B.4.1 Three Lines of Defence* for descriptions of Line 1 and Line 2.

To ensure the appropriate skill is used to manage the investments, day-to-day management is performed by specialist fund managers. Fund managers are appointed following a rigorous selection process, which is detailed in the Outsourcing Policy, see *Section B.4.6 Operational control*. This includes establishing the regulatory compliance regime that the fund manager has put in place, their "Senior Managers" structure, and their competencies framework that ensures staff are fully qualified for the roles they are executing.

An Investment Management Agreement ("IMA") is in place with each fund manager and these agreements reflect SLOC UK's strategy and risk appetite requirements.

Formal operational meetings take place with the fund manager at regular intervals as part of a rolling, continuous, programme of oversight. The oversight framework includes criteria to define and remediate issues with investment managers, including contract termination, if necessary.

All investments must meet the requirements of the investment guidelines contained within the IMA. These guidelines include a range of investment restrictions covering all aspects of investment including permitted asset classes, single name, and industry and rating band limits, designed to ensure diversification, as well as benchmarks and performance targets.

Where the use of derivatives is permitted, it is restricted to efficient portfolio management and risk management.

Any investments that result in one or more of the investment guidelines not being met are reported as a breach.

The Investment Management Committee ("IMC") and the Asset Liability Management Committee ("ALMC"), which form part of the governance framework, are responsible for reporting and remediating any breach relating to their respective areas of responsibility.

All Investment Managers are required to maintain a policy on conflicts of interest to ensure the following:

- The interests of SLOC UK will not take precedence over the interests of SLOC UK customers in making decisions;
- Managers ensure their staff's interests do not conflict with that of SLOC UK or its customers; and
- The interests of other clients of Managers do not take precedence over the interests of SLOC UK.

**B.3.5 ORSA**

The ORSA is the process of assessing all risks inherent in the business of SLOC UK, the EEA Group and the material and relevant risks arising from membership of the WWG, refining or amending the strategy accordingly and determining the corresponding capital requirements on a Solvency II Pillar 2 basis.

To achieve this, the SLOC UK Board requires the CRO to maintain adequate, robust processes for assessing, monitoring and measuring the risks and the overall solvency needs of SLOC UK and the wider EEA Group, while ensuring that the output from the assessment is embedded into decision making processes. Conducting an assessment of the overall solvency requires input from all areas of the business.

The ORSA is produced at the level of the EEA Group. SLOC UK, as the regulated entity of the EEA Group, is where the material risk exposure exists.

The ORSA must consider and document the approach taken to all risks considered within the EEA Group and must also consider and document any material and relevant risks that arise for the EEA Group from membership of the WWG.

As part of the ORSA, the Board will review and assess the overall ORSA Report and recommendations provided by the Risk function. The Board will comment on the suitability of the assessment, considering the manner in which the assessment of overall solvency needs reflects the management of risks through overall capital requirements or other mitigation techniques. This takes into consideration the risk profile, approved risk appetite and business and risk strategies.

The ORSA Capital Measure ("OCM") is distinct from the regulatory capital requirements. This assessment includes a comparison of SLOC UK's risk profile to the assumptions underlying the calculation of the regulatory capital requirement, whereby differences are highlighted, quantified and explained.

Based on the forward looking perspective of the operating environment, own funds and capital requirements are projected under both expected and stressed conditions. Through this projection, the ORSA provides an assessment of SLOC UK's ability to execute its Long Term Business Plan while maintaining sufficient funds to cover both its regulatory capital requirements and its OCM. Exposure against risk appetite statements and tolerances is also assessed as part of these projections.

The Board has reviewed and approved the ORSA process ensuring that techniques for assessing its overall solvency needs are commensurate with the nature, scale and complexity of the risks inherent in the business. The ORSA Report is reviewed by the Risk Committee and recommended for approval by the Board annually. During the year, should an internal or external event occur that significantly changes the risk profile of the firm as detailed within the last annual ORSA Report, then the requirement to produce an updated ORSA report will be considered. In the event that it is deemed appropriate, an updated ORSA Report will be produced and reviewed by the Board for approval outside of the annual process.

The operation of the ORSA process provides the Board with a key tool for monitoring and keeping the business within risk appetite, through the operation of robust and transparent risk and capital management practices.

The extent and sophistication of the ORSA is proportionate to the nature, scale and complexity of the business.

## B.4 Internal control system

It is the responsibility of every staff member to identify and manage risk. Our governance arrangements strengthen this principle by adding challenge, oversight and independent assurance of risk management in all our business operations. In addition to local regulatory obligations, staff must comply with the WWG corporate governance requirements.

The internal control requirements are set out in the Internal Controls Policy. The functions in scope for this policy are as follows:

- Risk and Compliance;
- Actuarial;
- Finance;
- Operations; and
- Internal Audit.

The Internal Audit function is also governed by the Internal Audit Policy.

### B.4.1 Three Lines of Defence

A 'Three Lines of Defence' governance model is adopted for risk management, providing a consistent, transparent and clearly documented allocation of accountability and segregation of functional responsibilities. It separates the organisation into three lines of defence against risk:


- 1st Line of Defence ("Line 1") – responsible for managing risk in day-to-day business operations. Line 1 comprises Actuarial, Finance, Tax, HR, Communications, IT, Legal and Outsource Management.
- 2nd Line of Defence ("Line 2") – comprises the Compliance and Risk functions. The Compliance function oversees regulatory compliance. A summary of the Risk function's

responsibilities are set out in *Section B.4.3 The Risk function.* Line 2 functions are represented on all committees and on all material projects.

- 3rd Line of Defence ("Line 3") – independent assurance in respect of risk management controls is provided by Internal Audit. The Internal Audit function is described in *Section B.5 Internal Audit function.*

**B.4.2 The Compliance function**

The Compliance function is responsible for the following:

- Ensuring the company takes reasonable steps to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the UK regulatory system;
- Operating a system that is adequately resourced and has unrestricted access to the company's and EEA Group's relevant records, as well as ultimate recourse to the company's Board;
- Maintain compliance with the WWG Corporate Compliance Risk Management Policy; and
- Maintaining compliance with its Fraud Risk Management Operating Guideline.

**B.4.3 The Risk function**

The Risk function sets the system within which risks are identified and reported.

The Risk function is responsible for the following:

- Reporting to the Risk Committee;
- Risk identification methodology;
- Operational risk framework;
- 2nd line of defence challenge of risk controls;
- Data protection responsibilities;
- The outsourcing framework;
- Appropriate reporting procedures and feedback loops that ensure that information on the RMS is actively monitored and managed by all relevant staff, the Risk Committee and the Board;
- Reports that are submitted to the Risk Committee and Board by the Risk function on the material risks faced by the EEA Group and on the effectiveness of the RMS; and
- An appropriate ORSA process.

The Risk function will provide detailed reporting on risk exposures and advice on risk management matters including strategy, mergers and acquisitions, major projects and investments.

**B.4.4 Internal Controls over Financial Reporting ("ICFR")**

The ICFR programme is a fully developed set of procedures for identifying, monitoring and reporting internal controls within the financial reporting process. It supports the attestations that the UK CEO and UK CFO must provide for reporting to the WWG.

### B.4.5 Ownership of processes

SLOC UK has processes and procedures for undertaking the required prudential solvency assessment (including regulatory reporting) and for financial reporting purposes. This includes a description and definition of roles and responsibilities of the people involved and the relevant models.

The Finance function, with support from the Actuarial and Tax functions, takes ownership of the processes and procedures needed to undertake financial reporting. The valuation of assets and liabilities for solvency reporting purposes is owned by the Actuarial function supported by the Finance and Tax functions.

### B.4.6 Operational control

Operational controls cover a number of areas including Investments, Outsource Management, IT, HR and Legal.

The controls around the investments processes are documented in the investment related policies covering credit risk management, liquidity risk management, asset liability management and market risk management. The management of operational risk is governed by the Operational Risk Management Policy.

The SLOC UK business model places significant reliance on outsourcing and therefore the outsourcing processes and the governance and control of outsourcing risks are key components of the internal control system.

The Outsourcing Policy details the activity to be undertaken prior to entering into an agreement, and the oversight and control activities required during the lifetime of an outsourcing arrangement. This dictates that SLOC UK must establish a contractual right to information about the outsourced activities and a contractual right to issue instructions concerning the outsourced activities.

Key outsourcing arrangements are described in *Section B.7 Outsourcing*.

### B.4.7 System and data control

SLOC UK's systems take account of applicable data requirements, provide for appropriate security controls and define requirements in respect of access to hardware, systems and data, so as to maintain the integrity of records and information and thereby protect the interests of all stakeholders. This includes planning and controls designed to maintain business continuity.

System and data controls are addressed in the Data Governance Policy and the Operational Risk Policy.

### B.4.8 Control activities

Control activities are the policies and procedures that set out the rules, principles and requirements of the organisation. Control activities occur throughout the organisation, at all levels and in all functions.

The control activities in SLOC UK include approvals, authorisations, verifications, reconciliations, management reviews, appropriate measurements applicable to each business area, physical controls, checking for compliance with agreed exposure limits and operating guidelines and follow-ups on identified areas of non-compliance. The control activities are proportionate to the risks identified from the controlled activities and processes. Different levels of approval or authorisation are required for various business activities; these are documented in the procedures and guidelines covering each function or activity.

The internal control system ensures that any areas of potential conflicts of interest are identified and managed appropriately.

## B.5 Internal Audit function

### B.5.1 Internal Audit implementation

The UK Internal Audit function is part of the WWG Internal Audit function and operates in accordance with the Statement of Mandate, Responsibility and Authority approved by the WWG Audit Committee. The mandate is reviewed and approved by the Audit Committee on an annual basis.

An Internal Audit Policy is established for the UK, annually reviewed, and approved by the Board. This incorporates the WWG mandate and specifically references the role and responsibilities, independence and scope of work of the UK Internal Audit function.

The Internal Audit function operates in accordance with the Institute of Internal Audit's internationally recognised professional standards. The UK Internal Audit function also observes the Chartered Institute of Internal Audit (UK)'s code of practice for internal audit in financial services.

A WWG audit manual governs the day to day working practices and methodology applied within Internal Audit supported by a centralised professional practices group.

### B.5.2 Internal Audit independence

The independence of the UK Internal Audit function is achieved through organisational structure and reporting lines. The Head of Internal Audit reports to the Chair of the ACC (functionally) and to the WWG Chief Auditor (administratively).

### B.5.3 Controls assurance

A Controls Assurance Team ("CAT") is established to work alongside the Internal Audit function, reporting into the Head of Internal Audit acting as the Head of Controls Assurance. The CAT utilises audit methodology, alongside compliance expertise, to undertake independent compliance monitoring reviews based on an annual plan prepared by the Head of Compliance. The CAT also completes the annual ICFR programme based on a plan agreed with Corporate Finance.

## B.6 Actuarial function

During the reporting period, the Actuarial function coordinated the calculation of technical provisions and capital requirements on both Pillar 1 and Pillar 2 bases. Various mechanisms were employed to ensure these were determined appropriately:

- A Model and End User Computing Risk Management Policy was followed under which material models are independently reviewed periodically to ensure both the appropriateness of the methodologies and assumptions used and the accuracy of the calculations. More frequent reviews are carried out for models of greater materiality. Additionally, the material methodologies used in the determination of technical provisions by the Actuarial function are reviewed by a cross-functional technical management group prior to their use. The Actuarial function conducted appropriate experience investigations to develop proposals for non-economic assumptions, which are subject to Board approval. The models used for these experience investigations are also subject to the Model and End User Risk Management Policy described above. The Actuarial function has applied appropriate methodologies and assumptions by line of business.

- The Data Governance Policy was followed to ensure the data used to calculate technical provisions and capital requirements is materially appropriate, complete and accurate. For each quarterly Pillar 1 valuation, the policy data used by the actuarial models were reconciled to data extracts from the policy administration systems. Periodic checks of sample data have been carried out to verify the accuracy of data held by the policy administration systems and the policy data used by the actuarial models.
- Assumptions used in each quarterly Pillar 1 valuation and each Pillar 2 valuation were documented and appropriate checks were carried out to ensure these assumptions were correctly entered into the actuarial models.
- An analysis of change exercise was carried out at each quarterly Pillar 1 valuation and each Pillar 2 valuation to identify the sources of movements. Additionally, this exercise provided a further check on the accuracy of the calculations and the appropriateness of the assumptions and methodology used.

The Actuarial function has monitoring systems in place to estimate the Pillar 1 and Pillar 2 coverage in the intermediate period between full valuations. Various reporting and stress-testing exercises were also carried out on IFRS, Canadian Life Insurance Capital Adequacy Test and Embedded Value bases.

The Actuarial function is responsible for the measurement and monitoring of insurance and market risks. Data is captured at least quarterly as part of the risk measurement process and draws upon the valuation and capital assessments described above. Additionally the operational risks inherent within the Actuarial function are assessed on a quarterly basis as part of the same process.

To support the Actuarial function's responsibility to contribute to effective risk management, the function also carried out the following activities over the reporting period:

- Developing recommendations for bonus rates on the with-profits business, as well as other aspects of with-profits management;
- Investigations into the asset and liability matching position and other areas of investment risk such as credit exposure and concentration risk to help ensure investment risk exposures remained within defined risk appetite limits;
- Investigations into expenses, demographics and operational risk; and
- Investigations into the reinsurance exposures to assess the adequacy of the reinsurance arrangements.

## B.7 Outsourcing

**B.7.1 The outsourcing model**

Certain activities are outsourced where customer or business needs can be better met, or provide improved financial results, without exposure to unnecessary risk.

With this primary objective in mind, outsourcing will be considered for reasons such as these listed below:

- To realise cost savings and allow better control of costs by converting fixed costs into variable costs;
- To enable management to concentrate on core activities;
- To allow management to concentrate on service (quality and cost) rather than the management of resources delivering the service;
- To provide access to the wider expertise and / or specialist knowledge of a service provider;
- To increase flexibility where there are fluctuations in demand, or the service is required on an irregular basis; and
- To enable better access to technology without capital investment.

The Outsourcing Policy is described in *Section B.4.6 Operational control*.

### B.7.2 Fund administration and global custody

Fund administration and global custody are primarily outsourced to State Street Bank & Trust Company ("State Street"). The fund administration for a small block of business, the private funds, is outsourced to Capita Life and Pensions Regulated Services Limited ("Capita") and property fund administration is outsourced to Aberdeen Standard Investments. These outsourcers are located in the UK.

### B.7.3 Life, pension and annuity servicing outsourcing

All life and pensions servicing, plus the support services and facilities required to perform the services are outsourced to Diligenta Life and Pensions Limited ("Diligenta") and Capita, with annuity servicing outsourced to Equiniti, Paymaster (1836) Limited ("Equiniti"). These outsourcers are located in the UK.

### B.7.4 Asset liability management services provided by the WWG

Asset liability management services are categorised as outsourcing arrangements as these services are sourced under a formal contract with SLACC, Canada. This includes service requirements, reporting requirements, and oversight and exit provisions. The service is provided partially by UK based personnel who report to the WWG Asset Liability Management function and are supported by additional WWG personnel within the WWG Asset Liability Management function. The agreement stipulates that the UK regulatory regime will be complied with. The ultimate responsibility for asset liability management is retained by the Chief Actuary of SLOC UK.

## B.8 Any other information

In addition to our principal outsourcing arrangements discussed above, and in common with other WWG business groups, the EEA Group receives some centralised services from its corporate parent, defined as 'intra-group service provisions'. These arrangements are typically central 'decision to supply' IT services consistent across the WWG, creating economies of scale and subject to corporate-wide risk management procedures that may not always be achievable through outsourced arrangements with other providers. A charge back for each itemised intra-group service provision is made to the EEA group, and the service standards are set according to WWG policy that is appropriately modified to meet the local requirements of the EEA Group where necessary.

Under this arrangement, the WWG IT team standardises all IT global infrastructure for all businesses within the WWG in line with WWG IT policies and standards. On a simplified basis, the model works, from the centre out, as follows:

- The WWG contracts with various third party suppliers for provision of core IT services being distributed to the UK office. The WWG centrally owns, manages and maintains these contracts. As an example, the WWG IT team has contracted with Microsoft for the management, support and maintenance of the Global email platform, which is a core service.
- Distribution to the UK of applications and software is undertaken by centrally managed distribution software and technology. Licensing to the UK is undertaken by a WWG centralised licensing team.
- Charges for the provision of IT services are charged to the UK based on volume, utilisation and licensing requirements.

These centrally distributed IT services are significant and therefore SLOC UK also retains a UK based IT team. This team is led by an IT manager of senior grade and is responsible for:

- all UK based services;
- the business continuity programme, including disaster recovery arrangements; and
- oversight of third party outsourced IT arrangements.

# C. Risk profile

The risk profile of the EEA Group is not materially different from that of SLOC UK.

## C.1 Underwriting risk

For Solvency II Pillar 1, the undiversified capital requirement for life underwriting risk as at 31 December 2019 was £144 million (2018: £191 million). The most significant underwriting risks contributing to this are lapse risk and expense risk making up £82 million and £43 million respectively (2018: £107 million and £63 million).

### C.1.1 Lapse risk

Lapse risk arises for profitable contracts because higher than anticipated lapses will result in reduced future expected profit. Lapse risk also arises on non-profitable contracts, e.g. contracts with options and guarantees where lower than anticipated lapses lead to a higher take up rate resulting in reduced profit. Expense diseconomies of scale arising from the risk of increased lapses has been partially mitigated by an expense indemnity agreement as described in *Section C.1.5 Material underwriting risk mitigation techniques.*

**Control and monitoring of lapse risk**

Lapse experience is monitored regularly across the business, as are other metrics that could be considered early warning signals for a potential change in lapse rates, e.g. customer service metrics.

### C.1.2 Expense risk

Expense risk arises because any future increased costs of policy administration (either outsourcer costs or internal governance expenses) or investment management expenses immediately increases technical provisions. This is mitigated by the portion of expenses that can be met by with-profits business or charged to policyholders. From 1 January 2019, internal governance expense risk has been partially mitigated by an expense indemnity agreement as described in *Section C.1.5 Material underwriting risk mitigation techniques*.

**Control and monitoring of expense risk**

Internal governance expenses are carefully managed and expenses relating to outsourcing arrangements are set under the contractual arrangements in place. Expense variances against plan are monitored on a monthly basis.

Management and the Board are cognisant of the potential for increases in unit expenses over time when measured on a per in-force policy basis, particularly given the decision to exit new business and the resulting reduction of in-force policy count that will occur over time. The outsourcing contracts provide protection against this risk as they are variable in line with policy count, with an allowance for inflation, or assets under management as appropriate. Expense management is a key area of management attention.

### C.1.3 Longevity risk

Longevity risk on the annuity and Guaranteed Annuity Option ("GAO") business is reinsured as described in *Section C.1.5 Material underwriting risk mitigation techniques*. Longevity risk is retained in relation to the staff pension scheme and pension policies with GAOs that are not covered by a reinsurance treaty.

**Control and monitoring of longevity risk**

Following the reinsurance of the annuity and GAO business, longevity risk is much reduced. However, trends in longevity are regularly monitored in order to understand this risk before reinsurance and the value of the reinsurance.

**C.1.4 Concentrations of underwriting risk**

Underwriting risk comes from a wide variety of industry standard product types, which originated from several different insurance companies acquired in the past e.g. Lincoln National UK and Confederation Life Insurance Company ("CLIC"). These operated in several geographical areas and sold through different sales channels leading to a diverse underwriting risk portfolio.

Therefore, the populations covered are relatively diverse and there is little concentration of underwriting risk.

**C.1.5 Material underwriting risk mitigation techniques**

**Material reinsurance treaties**

There is an annuity treaty with the Bermuda Branch of SLACC ("Sun Life Bermuda"), which transfers all risks other than expense risk. The SLOC UK business incepted prior to 31 December 2008 is subject to a cap on payments, which is covered by a stop loss treaty with SLACC.

A third treaty covers the GAOs of SLOC UK arising from unit-linked pensions policies originally written by CLIC and is with Sun Life Bermuda.

**Other reinsurance treaties**

There are a total of 55 treaties with other reinsurers.

These treaties cover mortality, longevity, income protection, critical illness and various other smaller benefits.

The continued effectiveness of the reinsurance programme is ensured through the risk management activities described in *Section B.3.4 Risk management processes*, whereby retained risks (i.e. those not reinsured) are identified, measured, managed, monitored and reported.

**Staff pension scheme insurance buy-in**

During 2018, the trustees of the defined benefit staff pension scheme agreed a £200m buy-in contract with Pension Insurance Corporation insuring the majority of pensions in payment. This was an initial step in reducing risk within the scheme. It left £300m of uninsured liabilities, primarily for deferred members.

**Expense indemnity agreement**

On 28 January 2019, the company paid an upfront charge of £23.9 million to enter an expense indemnity agreement with SLACC, effective for 30 years from 1 January 2019. The indemnity agreement sets a cap on the level of governance expenses per policy, increasing with inflation. Under the agreement, governance expenses above the cap are reimbursed to the company by SLACC. The indemnity agreement provides protection against expense shocks and diseconomies of scale.

### C.1.6 Underwriting risk stresses

The standard formula approach is used for assessing all underwriting risks. The risks are quantified by stressing the liabilities for each stress. Lapse risk is assessed as the most onerous of (i) allowing for lapses and surrenders to be 50% higher or 50% lower than the best estimate assumptions, and (ii) allowing for a mass lapse event. The mass lapse result is currently the most onerous.

For with-profits business, provided there are sufficiently large future discretionary benefits, it is assumed reductions in surplus from stresses will be offset by reductions in future discretionary bonuses (with no allowance for any timing effects from the delay in acting to reduce bonuses). This means that the stress net of management actions for with-profits business has minimal impact on the company.

The underwriting risk stresses are as follows:

| £ million | Net SCR (including the loss-absorbing capacity of technical provisions) | Gross SCR (excluding the loss-absorbing capacity of technical provisions) |
|---|---|---|
| Mortality risk | 9 | 13 |
| Longevity risk | - | 5 |
| Disability-morbidity risk | 9 | 9 |
| Life-expense risk | 43 | 50 |
| Lapse risk | 82 | 82 |
| Life catastrophe risk | 1 | 2 |
| Diversification within module | (30) | (37) |
| **Total capital requirement for underwriting risk** | **114** | **124** |

## C.2 Market risk

### C.2.1 Background

Market risk arises from fluctuations in values of, or income from, assets, interest rates and exchange rates. The investment strategy, covered in *Sections C.2.2 Equity risk to C.2.6 Concentration risk*, mitigates this risk and is approved by the Board and implemented by the ALMC.

Investment mandates are outsourced to third parties in order to realise cost savings and access the wider expertise and specialist knowledge of service providers. The asset managers are required to comply with the detailed investment guidelines and policies as defined in their respective IMAs. See *Section B.7 Outsourcing* for more details of the outsourcing arrangements.

### C.2.2 Equity risk

A material proportion of income is derived from fee income from unit-linked funds (primarily invested in equities). Although risks and rewards of equity performance in unit-linked funds are passed through to the customer, a change in value of equity markets will cause proportionate changes in fee income because it is linked to the value of assets under management, which also affects the cost of providing GAO guarantees and loyalty bonus units.

The SLOC With-Profits fund holds equities in order to increase policyholder returns.

### C.2.3 Interest rate risk

Interest rate risk arises mainly from mismatches between the non-linked liabilities and the assets used to match those liabilities. Where possible, attempts are made to minimise this risk by matching the duration of liabilities as closely as possible across the interest rate curve. A range of matching approaches is used depending on the product and the size of liabilities.

The IMA's investment guidelines detail tolerances across the term structure of the liability profile that the manager is required to match. The investment guidelines comply with internal policies and operating guidelines and are reviewed annually.

GAO liabilities are a significant source of interest rate risk; however, the majority of this has been reinsured to Sun Life Bermuda as described in *Section C.1.5 Material underwriting risk mitigation techniques.* The derivatives strategy is managed on behalf of the reinsurers.

### C.2.4 Currency risk

Where non-sterling assets are bought, their cash flows are hedged back into sterling within the non-linked business but not necessarily within the with-profits or unit-linked funds. Currency movements will cause proportionate changes in fee income because it is linked to the value of assets under management, which also affect the cost of providing GAO guarantees and loyalty bonus units.

### C.2.5 Property risk

A small proportion of the unit-linked funds invest in property, so fee income is exposed to fluctuations in the valuation of underlying properties. This is not material.

A proportion of the assets backing with-profits business is invested in property.

### C.2.6 Concentration of risks

The largest market risks arise from risks to fee income from unit-linked funds. Unit-linked products are invested in a variety of funds within different sectors, geographical areas and managers. This diversification means it is believed there are no material concentrations of equity risk, apart from having exposure to the overall asset class.

Suitable diversification limits are maintained in investment guidelines and operating guidelines to ensure minimal concentration risk arising from single name, sector, issue proportion and / or rating exposure. A market risk concentration stress is performed and the low value for this confirms that there is no concentration to particular counterparties.

### C.2.7 Market risk stress tests and scenario analysis

The standard formula approach is used for assessing market risk.

For with-profits business, provided there are sufficiently large future discretionary benefits to cover this, it is assumed reductions in surplus from stresses will be offset by reductions in future discretionary bonuses (with no allowance for any timing effects from the delay in acting to reduce bonuses). This means that the stress net of management actions for with-profits business has minimal impact on the company.

The projection of liabilities takes into account the change in asset values relevant to the scenario or stress being tested.

The market risk stresses are as follows:

| £ million | Net SCR (including the loss-absorbing capacity of technical provisions) | Gross SCR (excluding the loss-absorbing capacity of technical provisions) |
|---|---|---|
| Interest rate risk | | |
| interest rate up shock | 41 | 41 |
| Equity risk | | |
| type 1 equities | 67 | 112 |
| type 2 equities | 11 | 11 |
| Property risk | 3 | 12 |
| Spread risk | | |
| bonds and loans | 20 | 35 |
| Market risk concentrations | 2 | 2 |
| Currency risk | 27 | 33 |
| Diversification within module | (57) | (65) |
| **Total capital requirement for market risk** | **114** | **181** |

**Interest rate risk**

Interest rate shocks are specified by the standard formula.

Analytic data from each bond (such as duration and convexity) is used to capture the response of the market value of the security to the underlying market variable of the stress.

The stressed yield / discount rate curves and, where relevant, post-shock unit prices are used to calculate the stressed value of assets.

Products modelled stochastically are revalued using an Economic Scenario Generator ("ESG") recalibrated to the stressed conditions.

For non-linked business modelled using the conventional models, flat yields are used for valuation. The stressed liabilities for these products are calculated by increasing (or decreasing) the base flat rate.

The interest rate stresses are calculated as the change in own funds.

**Equity risk**

Equity stresses are specified by the standard formula. The equity stress is calculated by aggregating together stresses on two types of equities.

Type 1 equities are equities listed in regulated markets in the countries which are members of the EEA or the Organisation for Economic Co-operation and Development ("OECD").

Type 2 equities are equities listed in stock exchanges in countries which are not members of the EEA or the OECD, equities which are not listed, private equities, hedge funds, commodities and other alternative investments.

As a simplification, the type 2 equity stress is also applied to all investments where a look-through approach is not possible and information is not available as to what stress should apply to the asset. For significant holdings in external collective investment funds, the investment mandates are used to derive the asset stresses.

Shocks are applied separately for the two types of equity. The value is calculated for the assets in both the non-linked and the unit-linked funds in the event of each shock.

The type 1 and type 2 equity stresses are calculated as the change in own funds. They are aggregated together using the standard formula's equity correlation matrix.

**Property risk**

A 25% shock is applied to the value of all property investments in both the non-linked and the unit-linked funds.

The property stress is calculated as the change in own funds.

**Concentration risk**

Concentration risk stress amounts are calculated using asset data only and, to avoid double counting, excludes assets covered by the counterparty default risk calculation.

A simplification is used for collective investment schemes where look-through is not possible. These are treated as a single counterparty in this calculation. The calculation follows the standard formula in summing the value of assets in excess of a threshold multiplied by a risk factor.

**Currency risk**

Currency stresses are specified by the standard formula.

The currency risk stress applied depends on the exposure to the foreign currency. The exposure of a foreign currency is equal to the market value of the assets denominated in the foreign currency less the best estimate of the liabilities denominated in the same foreign currency.

The main risk is due to the capitalised effect of lost management fees on policyholder unit funds invested in overseas currency. The business also has Euro-denominated liabilities and it has been calculated that overall solvency would be more adversely affected by a rise than a fall in the value of the Euro.

A 25% decrease in the value of assets is applied to the value of all investments in currencies other than sterling.

Stresses to be applied to unit prices for the unit-linked funds (applying look-through as far as possible) are calculated and are used with the standard assumptions in order to calculate stressed values for the liabilities.

The currency stress is calculated as the change in own funds.

## C.3 Credit risk

**Credit risk profile**

Credit risk includes the risk of losses arising from credit migrations, changes in credit spreads or default of counterparties. The key credit risk exposures are as follows:

- Fixed income securities - exposure to losses from credit migrations, changes in credit spreads or defaults;

- Derivative trades - default of trade counterparties partially mitigated through collateral and margin arrangements; and
- Reinsurance arrangements - default of reinsurance counterparties.

The management of credit risk is governed by internal policies such as the Asset Liability Management and Market Risk Management Policy and the Credit Risk Management Policy. The ALMC is responsible for overseeing and managing credit risk and credit exposures facing the company and ensuring that credit risk management policies and controls are in place. The ALMC meets at least four times a year.

**Management of credit risk – fixed income securities**

In order to benefit from their experience, resources and knowledge a number of investment managers are employed to invest in fixed income securities. As at 31 December 2019, £3.8 billion of fixed income securities were held in the non-linked business (2018: £3.9 billion).

The appetite for credit risk and how it will be managed is articulated to the Investment Manager via the contractually binding investment guidelines attached to the IMAs. Investment guidelines are reviewed annually before being approved by the IMC for unit-linked business or the ALMC for non-linked business and, if appropriate, the reinsurer. The appropriate level of credit risk for each type of product will vary depending upon the risk appetite and the nature of the product (e.g. with-profits, annuities).

The investment guidelines include the following restrictions relating to the following:

- The average credit rating of the portfolios;
- Exposures to lower rated credit exposures;
- Exposures to single counterparties, associated counterparty groupings and sectors:
- The proportion of an issue that can be bought; and
- The origin of issuers.

Investment Managers are required to provide detailed reports and attestations at least quarterly to demonstrate compliance with the investment guidelines. These detailed reports are reviewed at regular operational governance meetings with the Investment Managers.

In order to identify and mitigate potential credit losses, the ALMC also records and reviews specific securities that are identified by bond analysts as having a higher risk of default on a credits causing concern list.

As described in *Section C.1.5 Material underwriting risk mitigation techniques*, the reinsurance treaties with SLACC cover all risks other than expense risk. As described below in the *Section Management of reinsurance counterparty default risk*, the reinsurer is required to deposit back assets in respect of these treaties. £2.9 billion, or 75% (2018: £2.9 billion, or 75%), of the total fixed income securities relate to assets deposited back and therefore, for these securities, the only exposure is to default by the reinsurance counterparty.

**Management of credit risk – derivative trades**

SLOC UK has a derivative portfolio to hedge material economic risks, such as those relating to GAOs. Where business is reinsured with other companies in the WWG, the derivative performance is passed on to the reinsurer. As at 31 December 2019, the derivatives in SLOC UK's non-linked business had a total market value of £122.1 million (2018: £82.4 million) and a total notional value of £1.6 billion (2018: £2.0 billion).

£121.8 million (2018: £87.7 million) of the total market value is for derivatives cleared through a central clearing counterparty ("cleared derivatives"). As at 31 December 2019, SLOC UK's non-linked business posted initial margin of £25.6 million (2018: £24.1 million) in respect of these cleared derivatives, all of which was gilts.

For uncleared derivatives, SLOC UK is exposed to losses from the default of the derivative counterparty if the derivative is in the money. In order to mitigate this risk, SLOC UK exchanges collateral on a daily basis. The exchange of collateral is governed by market standard International Swaps and Derivatives Association and Credit Support Annex ("CSA") agreements with each counterparty. SLOC UK also complies with the requirements of the European Market Infrastructure Regulation. The market value of derivatives and collateral is monitored regularly by the ALMC. As at 31 December 2019, SLOC UK's non-linked business pledged an aggregate collateral balance of £0.7 million, all of which was cash, (2018: £4.1 million) in respect of uncleared derivatives with £0.3 million total market value (2018: £(5.3) million).

Derivatives where other WWG companies act as counterparty are not required to be collateralised.

**Management of reinsurance counterparty default risk**

As described in *Section C.1.5 Material underwriting risk mitigation techniques* SLOC UK has entered into reinsurance agreements with other entities in the WWG. In order to limit counterparty credit exposure, the reinsurer is required to deposit back investments approximating to the value of the reserves of the reinsured business.

The deposit back funds hold investments approximating to the IFRS reserves requirement, and the amount is recognised on the SLOC UK balance sheet and is presented as 'deposits received from reinsurers'. This amounted to £3,161 million as at 31 December 2019 (2018 £3,122 million).

In addition to the deposit back funds SLOC UK can make use of a Secured Custody Account ("SCA"). Where further deposits are required to meet thresholds with respect to Solvency II reserves, the reinsurer deposits additional funds into the SCA. The SCA is not recognised on the SLOC UK balance sheet. Use of the SCA isolates the deposit back fund from potentially significant fluctuations arising from changes in Solvency II reserves, resulting in efficient and flexible use of WWG capital. No funds were held in the SCA at 31 December 2019 (2018: nil).

Each quarter the reserves and the funds held in the arrangements are reviewed and the reinsurer is obliged to top up the deposit back fund and / or the SCA to the required level if necessary.

Should the credit rating of the reinsurer fall below a certain limit, the treaties have provisions for automatic recaptures.

Management information, including commentary on all reinsurance arrangements entered into, is produced annually for submission and discussion at the Risk Committee.

SLOC UK has significant counterparty exposure to SLACC, particularly in respect of the deterioration of SLOC UK's capital position that would occur should SLACC become financially impaired, necessitating recapture of these agreements. Whilst substantial diminution of the financial capacity of SLACC appears to be a remote possibility at present, should this not continue to be the case a number of actions are available to management as listed below:

- Capital injection – SLOC UK could seek additional capital from SLACC.  However, it is recognised that any cause of a forced recapture is likely to have diminished SLACC's ability to provide such capital.
- Cessation of dividends – Any future surplus emerging in respect of both the recaptured business and other business of SLOC UK could be used to restore the solvency position before any dividends were paid.  The SLOC UK Board has full discretion over dividends.
- A matching adjustment could be applied to annuities in payment.
- Risks could be transferred to an external third party.

The optimal strategy depends on the market and regulatory environment as well as SLOC UK's longer term strategic objectives at the time such options are considered.

**Material credit risk concentrations within SLOC UK and how they are managed**

SLOC UK has no material credit risk concentrations.

Credit risk concentrations are assessed by allocating sector and single issuer names to fixed interest securities.  This enables credit risk exposures to be aggregated across the lines of business. Restrictions are then placed on the exposures to a single issue, single issuers and single sectors to ensure appropriate diversification.  For example, Sun Life Capital Management (Canada) Inc. which manages the majority of corporate bonds held in the non-linked business include the following restrictions in the investment guidelines:

- A maximum investment of 30% in any one sector;
- A requirement to ensure exposure to five distinct sectors to ensure diversification;
- A maximum investment in any one issuer name (varies between 3% - 5% across the business);
- A maximum investment of 10% in a single bond at purchase date.  For public issues, no new purchases unless the available issue size is at least £100m; and
- A maximum exposure of 5% to sub investment grade debt (below BBB-).  No new purchases permitted.

The largest single issuer exposures and all sector exposures are reported in the quarterly investment reports which are reviewed by the ALMC.

SLOC UK executes derivative trades with a number of high quality derivative counterparties to ensure diversification and reduce credit risk concentration.

**Credit risk mitigation techniques**

SLOC UK invests in credit default swaps in order to mitigate credit risk in the non-linked business.  As at 31 December 2019, the credit default swaps had a total market value of £3.0 million (2018: £2.9 million) and a total notional value of £36.4 million (2018: £51.5 million).  The credit default swaps are held for the purposes of hedging and efficient portfolio management only, as required by the IMA, and the positions are monitored for compliance with the IMA on a monthly basis.

**Credit risk stress tests and scenario analysis**

**Spread risk**

Under the Pillar 1 standard formula, the capital requirement for spread risk is the sum of three capital requirements: the capital requirement for the spread risk of bonds and loans other than mortgage loans, the capital requirement for the spread risk on securitisations and the capital requirement for credit derivatives.

The spread risk sub-module covers credit derivatives that are not held as part of a recognised risk mitigation policy.

The stresses applied to each security are dependent on the asset's credit rating.

The spread stress figures are calculated from the change in own funds.

The impact of this stress was £20 million net of the loss absorbing capacity of the technical provisions (2018: £19 million). Under Pillar 1 standard formula, spread risk is included with the market risks not within counterparty default risk.

**Counterparty risk**

Reinsurance, derivative and deposit counterparty risk is stressed in this module. Other counterparties are stressed with the market concentration calculation. It is calculated using the standard formula.

For with-profits business, provided there are sufficiently large future discretionary benefits to absorb the risk, it is assumed reductions in surplus from stresses will be offset by reductions in bonuses (with no allowance for any timing effects from the delay in acting to reduce bonuses). This means that the stress net of management actions will be zero on with-profits business.

No unrated exposures or type 2 exposures due for more than three months currently appear in the counterparty default risk calculation for SLOC UK.

## C.4 Liquidity risk

Liquidity risk is the risk that a given security or asset cannot be traded quickly without incurring a loss.

**C.4.1 Liquidity profile**

SLOC UK is shown to have sufficient liquidity to be able to meet all of its obligations under reasonably foreseeable conditions, and in modelled extreme adverse circumstances.

**C.4.2 Objectives of liquidity management**

Liquidity is managed to achieve the following goals:

- All cash outflow commitments should be honoured as they fall due; and
- The forced sale of assets, the need to borrow funds at high rates, and excess liquidity should be avoided.

### C.4.3 Liquidity / cash management at the fund level

In normal circumstances, the basic measure of liquidity risk - the 'liquidity ratio' - is the total value of the immediately available cash inflows receivable from assets (and from policyholders where relevant) divided by the total value of the immediate outflows arising from liabilities and other commitments.

Under these circumstances, we would expect to have extremely secure cover for cashflow commitments. This is because expected outflows are matched to a large extent by expected income. Additionally, it should be possible to sell a reasonable proportion of the investments at market value (or close to) to raise additional cash at any time.

Safeguards are in place to ensure that the liquidity position under normal conditions remains satisfactory. These include regular monitoring of the cash positions and cash flow requirements. The level of cash required for each fund is set by reference to a liquidity ratio, which is monitored on an on-going basis by the ALMC.

### C.4.4 Liquidity risk appetite

SLOC UK liquidity risk appetite thresholds and limits are designed to support the liquidity needs of the SLOC UK business and ensure it can withstand a market liquidity crisis. A prudent liquidity requirement is calculated to cover claims and expenses due over the next three months and one year in normal and stressed conditions, and dividends expected to be paid with cash to the shareholder. Cash and cash equivalents are held to cover three month liquidity requirements. One year liquidity requirements are covered by cash, cash equivalents and UK government bonds.

The table includes the liquidity ratios calculated at 31 December 2019:

| | Threshold | Limit | 2019 |
|---|---|---|---|
| Liquidity ratio: | | | |
| - one year (non-profit business) | 110% | 105% | 284% |
| - one year (with-profits business) | 110% | 105% | 238% |
| - three months (non-profit business) | 110% | 105% | 255% |
| - three months (with-profits business) | 110% | 105% | 278% |

### C.4.5 Unit-linked funds

Cash balances are maintained and monitored to meet policyholder flows as they arise. This is overseen by the IMC.

### C.4.6 Liquidity Contingency Plan ("LCP")

SLOC UK has formulated an LCP in order to assist it in managing a liquidity crisis event should one occur. If the calculated ratios were to approach a liquidity threshold point, the contingency plan would be put into action. The LCP covers policy on customer services, public relations, investment and liquidation of assets. The LCP is reviewed regularly by the ALMC.

Currently there are no areas of material liquidity risk concentration within SLOC UK. Sufficiently high liquidity ratios are maintained to ensure SLOC UK has sufficient assets available to pay claims as and when they fall due.

Solvency II Pillar 1 results confirm liquidity risk is very low within SLOC UK and no capital is required to meet this risk.

### C.4.7 Controlling and monitoring liquidity risk

The nature of the business and the assets being held means liquidity risk has not been a major concern for SLOC UK. Nonetheless, SLOC UK monitors three month and one year liquidity ratios quarterly against risk appetite.

### C.4.8 Expected profit included in future premiums

As the business is substantially single premium business (recurrent single premium pensions business) and business that has already become paid up, the expected profit included in future premiums is not significant as a proportion of the total reserves.

The figure for 31 December 2019 was £63 million (2018: £67 million).

### C.4.9 Pillar 2 liquidity risk

Sufficiently high liquidity ratios are maintained to ensure that there are sufficient assets available to pay claims as and when they fall due. An extreme adverse scenario test is undertaken being an instantaneous ‘point-in-time’ test of an immediate panic or run-on-the-bank at the valuation date. Results confirm that liquidity risk is very low within the company and that no capital is required to meet this risk.

### C.4.10 Liquidity risk stresses

The liquidity risk appetites specified above allow for liquidity requirements in stressed conditions and avoid reliance on selling potentially illiquid assets in the event of a market liquidity crisis.

## C.5 Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, or from personnel and systems, or from external events. SLOC UK has identified material operational risk exposures in the following areas:

- Outsourcing risk – life and pensions;
- Outsourcing risks – fund administration, fund managers, unit pricing, custody services, actuarial services;
- Product design and pricing risk;
- Model risk;
- Taxation risk;
- Key people risk; and
- Governance, systems and controls risk; and
- Cyber risk.

The only significant area of risk concentration is in respect of outsourcing risk (as described in *Section B.7 Outsourcing*, SLOC UK relies on material outsourcing arrangements with a small number of outsource providers). In line with the Long Term Business Plan, whilst maintaining an outsourced business model, SLOC UK will continue to consider actions to reduce exposure to outsourcing risk where possible.

Those risks considered to have a sufficiently high score are reported to the Risk Committee as part of the key risk reporting pack.

### C.5.1 Operational risk calculations

#### C.5.1.1 Pillar 1 operational risk

Pillar 1 operational risk is calculated as per the standard formula and is based on gross non-linked liabilities and net administration expenses for unit-linked business. The immaterial technical provisions and earned premiums on health business are combined with those for life business.

The Pillar 1 capital requirement for operational risk is £30 million (2018: £32 million).

#### C.5.1.2 Pillar 2 operational risk

Pillar 2 operational risk is based on an internal risk assessment of the risks and is diversified in the same way as other risks. The calculation at the valuation date uses a stochastic process to determine the number of risk events crystallising and another to determine the financial impact of each risk event. Inputs are derived from both scenario analysis, and the risk control self-assessment process embedded within the RMS.

The capital requirement for each of the risk events is calculated by allowing for diversification benefits between the individual risks within each event. The overall capital requirement for operational risk is then calculated by aggregating the capital requirements under Solvency II operational risk taxonomy using a further correlation matrix.

**Management of operational risk**

The overall aim of management of operational risk is to mitigate risk where such mitigations are cost effective. This recognises that initiatives may require a short-term increase in operational risk, to deliver longer-term benefits. Any action or initiative undertaken by management should not increase the long-term operational risk profile of the organisation.

All operational risks have in place mitigating controls that reduce the level of residual risk. In the case of those operational risks that are regarded as outside of risk appetite (where the level of residual risk is regarded as too high as currently measured), additional actions have been identified to further reduce the level of residual operational risk.

### C.5.2 Pillar 2 operational risk stress testing

Operational risk capital calculations are supplemented by stress testing scenarios to examine possible causes of business model failure. The purpose of these is to examine scenarios, other than solvency challenges, that could cause the business to fail.

The process concluded that it is unlikely that any single operational risk would fulfil the business model failure criteria. Whilst some combinations of scenarios were sufficiently extreme to warrant significant management actions, the probability of their occurrence is remote.

## C.6 Other material risks

**The use of derivatives**

The investment authorisations granted by the Board of directors allow derivative instruments to be used for hedging purposes or for efficient portfolio management only, and their use is subject to the same standards of prudence, due diligence, management supervision, controls and reporting as apply to other investments. Derivative risk management guidelines are also incorporated in the policies covering asset liability and market risk management and credit risk, which are reviewed annually.

Examples of the major hedges used by SLOC UK are as follows:

**GAO hedge**

The longevity and investment risk relating to GAO liabilities are reinsured to Sun Life Bermuda. SLOC UK manages the derivative strategy related to the GAO on behalf of Sun Life Bermuda. To hedge the interest rate risk of the GAO liabilities, the company holds a portfolio of interest rate derivatives to mitigate increases in cost due to interest rates.

**Solvency II hedge**

The objective of this hedge is to manage the sensitivity of the Solvency II position against movements in interest rates and swap spreads within Board approved thresholds. This is achieved through the use of derivatives.

**With-profits hedge**

The objective of this hedge is to manage the sensitivity of the Solvency II position of the with-profits pensions business against movements in interest rates and swap spreads within limits set in the investment guidelines. Fixed income assets are used to match liability cash flows whilst interest rate derivatives are applied to manage any residual interest rate risk and manage the swap spread sensitivity arising on a Solvency II basis.

**Other**

Some with-profits managers and some unit-linked asset managers also use derivatives for the purpose of hedging and efficient portfolio management, as outlined in the respective IMAs.

SLOC UK does not perform any securitised lending.

## C.7 Any other information

**C.7.1 Tax and risk profile**

**Financial tax risk**

The valuation of deferred tax assets in the balance sheet is dependent on future taxable profits emerging in the same business categories as anticipated. Any changes to these profits, for example because of worsening market conditions, adverse experience against valuation assumptions, or a change in strategy may affect the valuation of these tax assets and have adverse tax and capital effects. *Section D.1 Valuation for solvency purposes – Assets* gives consideration of this risk in the recognition and valuation of these assets.

**Legislative tax risk**

Possible legislative changes are considered and the likelihood of any adverse tax risk is assessed.

There is the generic risk that any transaction carried out may be subject to uncertainty regarding the interpretation of legislation by the tax authorities, or that there is uncertainty over tax issues currently under dispute with the tax authorities.

**Transactional tax risk**

This covers process management risks and includes examples where transactions are incorrectly undertaken leading to unintended adverse tax consequences. This also covers transactions which are not identified by the Tax function, not given tax consideration and also not notified to Her Majesty's Revenue and Customs.

**Reputational tax risk**

It is important to maintain good relations with the tax authorities by completing tax returns and paying tax due in an accurate and timely fashion. Failure to do this could result in additional scrutiny over the tax affairs of the company, a higher overall risk rating and a higher risk that, in advance of transactions, tax authority clearance may not be received.

It is also important to maintain a good reputation with customers by not making errors with regards to policyholder taxes.

### C.7.2 Climate change

The PRA is leading an initiative on how financial services firms should govern, assess, test and disclose how they are dealing with the risks posed by the physical and transitional aspects of climate change. SLOC UK has appointed its CRO as its designated Senior Manager with specific responsibilities for the management of this risk.

The company is also monitoring other requirements as they develop, such as the recommendations made by the Taskforce on Climate-related Financial Disclosures. These are expected to deliver additional disclosure requirements in future years as regulatory requirements become clearer and the company's exposure to climate change both as an asset owner and as an insurer matures.

### C.7.3 UK departure from the EU ("Brexit")

The company has closely monitored the political and regulatory developments arising from Brexit negotiations. Although there remains uncertainty on the final terms of Brexit, the company is confident that it is well prepared to address the various conduct, prudential and data risks it and its outsourcers face. The company regards conduct risk as its principle concern in relation to Brexit, as changes to the passporting arrangements between the UK and EU members could impact continuity of service for the small number of policyholders that reside in the EEA. Based on guidance from the European Insurance and Occupational Pensions Authority ("EIOPA") and a supportive legal opinion, the company intends to maintain uninterrupted service for all policyholders, paying claims and receiving premiums as they fall due.

### C.7.4 Scenario analyses

Scenario testing has been carried out using the scenarios listed below:

- A two-stage severe economic scenario caused by political instability;
- A worldwide pandemic of working population with mortality improvement for older ages coinciding with a reinsurance recapture scenario; and
- Regulatory pension business developments resulting in changes in policyholder behaviour.

These scenarios are judged to be reasonable situations that test the robustness of the business. With the exception of recapture, SLOC UK was able to meet the necessary solvency requirements with the impact of the scenarios being absorbed by reducing future dividends. The reinsurance arrangements are material and recapture without compensation would require management actions to cover the SCR. These management actions are covered in *Section C.3. Credit Risk*.

**Scenario stress testing against risk appetite**

Scenarios are compared against risk appetite at current point in time and also over a five-year projection period as part of the ORSA process. Management actions are considered for those scenarios where risk appetite thresholds or limits are potentially breached.

### C.7.5 Covid-19

In respect of the Covid-19 pandemic, the RMS remains an appropriate tool to frame the related exposures. Both the financial and non-financial existing risk appetite statements measures continue to appropriately define the triggers under which action may be required. There have been no breaches of existing risk appetite thresholds since 31 December 2019. Actions will prioritise employee wellbeing and customer outcomes, as well as considering financial impacts as described in *Section A.1.3 Covid-19*. The stress testing undertaken as part of the ORSA has demonstrated that the business remains financially solvent even under highly stressed adverse circumstances. The business continues to engage with the regulators and to respond to enquiries as they arise.

# D. Valuation for solvency purposes

## D.1 Assets

The value of each class of asset for SLOC UK and for the EEA Group is shown in the balance sheets included in the appended quantitative reporting templates. The valuation methods for assets held by the EEA Group are not materially different from those for assets held by SLOC UK.

**D.1.1 SLOC UK deferred tax asset calculation**

Deferred tax assets are recognised for Solvency II purposes using International Accounting Standard ("IAS") 12 Income Taxes principles, where SLOC UK has deductible temporary differences or accumulated losses for tax purposes. With respect to tax losses, the balances recognised represent the estimated future loss utilisation. The following table shows the drivers of the deferred tax calculation for SLOC UK.

| **Valuation differences between Solvency II and IFRS and other deferred tax items** | **Gross (taxable) / deductible difference £ million** | **Associated deferred tax asset / (liability) £ million** |
|---|---|---|
| Investment differences | (191) | (11) |
| Accounting differences | (107) | (18) |
| Actuarial differences – pension business reserves | 11 | 2 |
| Actuarial differences – life business reserves | (23) | 1 |
| New life tax regime transitional adjustments | (55) | (2) |
| Onerous contracts provision | (4) | (1) |
| Pension business losses carried forward | 121 | 20 |
| **SLOC UK Total** | (248) | **(9)** |

In accordance with IAS 12, deferred tax assets are recognised only to the extent that it is probable that future profits will be available, against which carried forward trade losses can be offset. If deferred tax assets are not expected to be recovered, they are not recognised or a valuation allowance is recorded.

Recognition and measurement on the Solvency II balance sheet of the deferred tax asset of £20 million (2018: £23 million) relating to unused tax losses are based on management projections of future profits in the Long Term Business Plan, which indicates that losses are able to be fully recovered.

Deferred tax assets have been set off against deferred tax liabilities to the extent allowable.

Deferred tax liabilities relate mainly to unrealised gains on investments which have not yet been included in the computation of taxable profit.

**Reconciliation of deferred tax calculated on Solvency II and IFRS basis**

Under IFRS, deferred tax is determined based on temporary differences between the carrying amounts of assets or liabilities on the IFRS balance sheet and the corresponding tax bases used in the computation of taxable profit. The tax rates used are those that have been enacted or substantively enacted by the balance sheet date.

Deferred tax for Solvency II valuation purposes is determined on temporary differences between the economic value of assets or liabilities on the Solvency II balance sheet and their tax base.

This gives rise to the following differences:

| | Deferred tax asset £ million | |
|---|---|---|
| Net deferred tax assets per Solvency II balance sheet | | (9) |
| Net deferred tax liability per IFRS balance sheet | (37) | |
| Less deferred tax liability in the linked funds* | 27 | |
| | | (10) |
| **Difference** | | **(1)** |

*For Solvency II balance sheet purposes, the deferred tax liability in linked funds is within the line Assets held for index-linked and unit-linked contracts and does not form part of the net deferred tax asset shown explicitly in the balance sheet. Under IFRS, the whole company deferred tax position is disclosed including the deferred tax liability relating to linked funds. To make a valid comparison, the deferred tax liability for linked funds is removed from the IFRS balance sheet figure.

The above difference is attributable to the different valuation methods applied to deferred income liability, deferred acquisition costs, onerous contract provision, mathematical reserves, and asset valuation differences.

**Assessment of any additional deferred tax assets within the EEA Group**

As detailed in the table below, there remain unrecognised deferred tax assets of £280 million (£264 million capital losses and £16 million trading losses) within EEA Group companies other than SLOC UK. These predominantly relate to capital losses in SLF of Canada UK Limited, resulting from a corporate restructuring. A valuation allowance has been recorded against these losses as it is not anticipated that there will be any capacity for recovery in the foreseeable future.

| | Gross (taxable) / deductible difference £ million | Associated deferred tax asset / (liability) £ million |
|---|---|---|
| **Non-Life subsidiaries** | | |
| Capital losses | 264 | - |
| Trading losses | 16 | - |
| Excess capital allowances | 9 | 1 |
| **Non-Life subsidiaries Total** | **289** | **1** |

**D.1.2 Pensions benefit surplus and obligations**

SLOC UK operates two pension schemes.

**Main scheme (approved)**

The company operates a funded defined benefit plan, which closed to new entrants in March 2002 and closed to future accrual from 31 December 2011.

The most recent full actuarial valuation for funding purposes was carried out by Hymans Robertson LLP, independent actuarial advisers to the scheme, as at 31 December 2016 using the projected unit method.

The company paid no contributions to the scheme in 2019 (2018: £5 million).

The surplus in the scheme valued on an IAS 19 basis at 31 December 2019 was £102.5 million (2018: £93.3 million).

**Unfunded scheme (unapproved)**

The company operates an unfunded plan to provide defined benefits to certain former employees.

Full actuarial valuations for funding purposes are not required for the unfunded plan. The most recent actuarial valuation for accounting purposes was carried out by Hymans Robertson LLP as at 31 December 2019. The scheme has no assets and the value of the liabilities at the valuation date was £2.6 million (2018: £2.5 million).

### D.1.3 Investments

For Solvency II and IFRS, the fair market values for liquid bonds, listed equities, exchange traded funds, unit trusts and derivatives are sourced on a daily basis from leading financial information services companies (e.g. IBOXX, Bloomberg etc) according to a waterfall approach that is detailed in a price source agreement with State Street, the fund administrator.

For bonds, if there is not enough current pricing information for State Street to supply a current price then a stale price is supplied and the fact that it is stale is highlighted. If the situation persists then the asset is valued using the illiquid bonds method described in *Section D.4 Alternative methods for valuation*.

Derivatives are priced daily by an independent financial information services company, the counterparty and Bloomberg. SLOC UK can close out a derivative at any time with the counterparty or a third party, and the quoted price provides a good indication of the close-out price that would be received. As such, this is used for valuation purposes.

SLOC UK retains overall responsibility for the prices provided to it and has oversight of them. Accordingly prices provided to SLOC UK are tested and any apparent anomalies are investigated.

### D.1.4 Investment property

The valuation of properties held as investments is described in *Section D.4.2 Alternative methods for valuation - Property.*

### D.1.5 Participations

SLOC UK holds one participation which is valued identically under IFRS and under Solvency II principles at fair value, which is its net asset value.

The EEA Group does not hold participations in companies outside of the EEA Group.

### D.1.6 Cash, cash equivalents and deposits other than cash equivalents

Cash and cash equivalents are measured at market value in the Solvency II balance sheet and under IFRS.

Cash is held in various currencies and is converted to pounds sterling in the balance sheet at the foreign exchange rate as at the balance sheet date.

Cash equivalents and deposits other than cash equivalents are measured at market value using quoted prices in active markets for identical assets. The prices are provided by State Street and the price includes an allowance for the risk of future default on deposits other than cash equivalents.

**D.1.7 Loans on policies**

The valuation of policy loans is covered in *Section D.4.3 Alternative methods for valuation - Policy facilities*.

**D.1.8 Reinsurance recoverables**

The valuation of reinsurance recoverables is described in *Section D.2 Technical provisions*.

**D.1.9 Reinsurance and trade receivables**

The reinsurance receivables are accruals for unpaid reinsurance premiums and claims and are valued under Solvency II and IFRS at amortised cost, with the carrying amount approximating to fair value.

**D.1.10 Property, plant and equipment**

SLOC UK has a leasing arrangement with the owner of the building it occupies and has non-cancellable future minimum lease payments each year until 2022. The right of use asset is included in property, plant and equipment with a value of £1.1 million as at 31 December 2019.

## D.2 Technical provisions

The choice of method used to calculate technical provisions for each product group is proportionate to the nature, scale and complexity of the risks underlying the insurance obligations.

Stochastic models are used for products that offer material guarantees or options, such as GAOs. Deterministic models are used for other product groups.

The technical provisions quantitative reporting template appended shows the value of technical provisions comprising best estimate liabilities (“BEL”) and risk margins, as well as reinsurance recoverables.

The amounts recoverable from reinsurance contracts are calculated separately from technical provisions. The calculations are based on projected cashflows relating to the reinsurer, using the same boundaries as the relevant insurance contracts, with an adjustment to allow for expected losses due to default of a reinsurer.

**D.2.1 Methods and simplifications**

**Unit-linked**

Unit-linked products are modelled in a deterministic cashflow model with reinsurance assets modelled explicitly. Assumptions are best-estimate, and market-consistent term-dependent yields and inflation are used.

Calculations are performed at a policy level.

All expected cashflows are modelled for products within this model except for the immaterial simplifications noted below:

- The model does not allow for indexation of premiums and benefits;
- A single yield curve is used for all business including non-UK policies;
- Incurred but not reported claims, claims in payment and certain rider benefits are calculated within other reserves; and
- Some smaller reinsurance treaties are not modelled.

**Annuities**

Annuities are modelled using a deterministic cashflow model. The model uses market-consistent term-dependent assumptions for yields and inflation. Reinsurance assets are calculated separately.

Calculations are performed at a policy level and cashflows are monthly.

All expected cashflows are modelled for products within this model except for the immaterial simplifications noted below:

- No allowance is made for the possibility that the second life of a joint-life annuity may have died prior to the valuation date; and
- A UK yield curve is used for all business including non-UK policies.

**SLOC With-Profits fund**

The SLOC With-Profits fund policies are modelled using a best estimate deterministic cashflow model.

Future fund values, policy guarantees and cashflows are projected using best-estimate assumptions. They are then used in the calculation of the liabilities.

**GAO**

GAO is an annuity option for some pension policyholders. The impact on technical provisions is mitigated using reinsurance. The policies with GAO are usually modelled using a stochastic cashflow model.

The projections allow for cashflows such as premiums and expenses, the impact of investment and inflation and the assumptions for decrements such as death, surrender and retirement. At the assumed retirement age, the value of the option is calculated.

The following immaterial simplifications are made:

- Policies are grouped in order to reduce the run-time of the model using the categories nearest age, gender, value of units in force and annual premium;
- Indexation is not modelled for the small number of plans that have indexation; and
- The model has an annual time-step.

**Health products**

- Conventional health policies administered by Diligenta are modelled using a cashflow based multi-state model with explicit inception and recovery rates. This allows for lapsing plans (these products cannot be made paid-up).
- Reinsurance is not allowed for explicitly within the model. The reinsurance asset is calculated as the gross reserve multiplied by the proportion reinsured.

**Term products**

- Term policies administered by Diligenta are modelled using a cashflow based gross premium method. This allows for lapses.
- Reinsurance assets and gross liabilities are calculated explicitly.
- Conversion options on the policies are not modelled.
- Policies administered by Capita are valued using a net premium method.

**Conventional non-profit products**

- Policies administered by Diligenta and by Capita which were converted from with-profits policies are modelled using a cashflow based gross premium method.
- Policies administered by Capita which were not converted from with-profits policies are valued using a net premium method.

**Group pension products**

- Group pension products are modelled using a cashflow based gross premium method. This allows for lapses.

**D.2.2 Level of uncertainty in value of technical provisions**

The BEL is recalculated under significant stresses in order to calculate the SCR. These stresses provide information on the sensitivity of technical provisions to various risk factors.

The impact of stressing each of the major risk factors is shown in the table below. This allows for the loss absorbing effect of future discretionary benefits on with-profits business:

| **Solvency II Pillar 1 (£ million)** | **2019** | **2018** |
|---|---|---|
| **BEL at 31 December**<br>**(non-unit liabilities, net of reinsurance)** | **643** | **683** |
| Sensitivity of BEL to a change in the following risk factors (each change is shown in isolation), net of loss absorbency of technical provisions: | | |
| Lapses<br>One-off discontinuance of 40% of policies (for policies where this increases the BEL) | 82 | 107 |
| Equity market levels<br>Instantaneous decrease of 38.9% (2018: 32.6%) for type 1 equities (listed in markets in EEA or OECD countries) and 48.9% (2018: 42.6%) for type 2 equities (other equities) | 75 | 62 |
| Expenses<br>One-off increase of 10% in current expense levels and an addition of 1% to future expense inflation | 43 | 63 |

The risk margin is the present value of the cost of maintaining the non-hedgeable capital over the lifetime of the business. It is therefore sensitive to the level of non-hedgeable risk, the reduction over time of that risk and changes in the discount rate. The cost of capital rate is fixed at 6.0% per annum.

The sensitivity of risk margin to these factors is shown in the table below:

| **£ million** | **2019** | **2018** |
|---|---|---|
| **Risk Margin at 31 December** | **74** | **83** |
| Sensitivity of risk margin to a change in the following factors (each change is shown in isolation): | | |
| Level of non-hedgeable risk (increase of 10%) | 7 | 8 |
| Change in discount rate (decrease of 0.5%) | 5 | 6 |

The risk margin is sensitive to changes in the discount rate. This is because changes in the discount rate result in both changes to the capital requirements for non-hedgeable risks and changes to the discounted value of these capital requirements over the lifetime of the obligations.

**D.2.3 Assumptions**

**Changes in assumptions**

Each year, investigations into expenses and annuitant mortality are carried out. GAO take-up rate investigations are currently also being carried out annually following the introduction of pensions freedom legislation in April 2015. On a two-year rolling basis, investigations are conducted on longevity improvement factors and underlying experience, assured lives mortality, surrender, paid up and retirement experience. The investigations are used to set the assumptions used in valuation and these are approved by the Board. Economic assumptions are based on observed market rates at the valuation date.

**Economic**

The risk-free base curve published by the EIOPA is used. This curve is based on swaps less an adjustment for credit risk.

No credit is taken for a volatility or matching adjustment.

For business using term-dependent yields, a term-dependent inflation rate is also used.

Flat yields and inflation rates are used for less material business.

**Base expenses**

The liability models project outsourced and governance expenses separately. The base levels for these are taken from contractual agreements with outsourcers and expense analyses respectively.

Investment expenses are also taken from expense analyses.

**Policyholder options**

Decrement assumptions and GAO take-up rates are set at grouped product level at best estimate rates following an experience investigation. The following assumptions are set separately:

- Lapse / transfer from premium paying;
- Lapse / transfer from paid-up;

- Paid-up policy from premium paying;
- Retirement rates; and
- Take-up rate assumption for plans with GAOs.

**Mortality / morbidity**

Mortality rates are generally set at best-estimate following a mortality investigation. The base table and proportion used are set so as to reflect best-estimate assumptions.

For certain products where experience data is limited, mortality / morbidity rates are set equal to the rates underlying policy deductions, using reinsurers' rates or original product pricing rates.

### D.2.4 ESG

SLOC UK uses risk-neutral ESG scenarios to value its major stochastically modelled line of business (GAO) as well as less significant pension and investment guarantees.

SLOC UK's choices of sub-models can be summarised as follows:

| Category | Model |
|---|---|
| Nominal interest rates | Libor Market Model plus |
| Real interest rates | Two-factor Vasicek model |
| Equity returns | Stochastic Volatility and Jump Diffusion |
| Property returns | Fixed Volatility |
| Foreign exchange rates | Not modelled stochastically |
| Credit spreads | Cox-Ingersoll-Ross model |

### D.2.5 Risk margin

The risk margin forms a part of the technical provisions under Solvency II, and is a cost of capital calculation.

The individual undiversified risk components contributing to the risk margin in any future year are approximated. The degree of approximation in the projection of each stress amount depends on the nature, scale and complexity of both the risk and of the business being modelled. The significant non-hedgeable risks are lapse risk, expense risk and operational risk. These are calculated in line with the exposure to mass lapse, total expenses and reserves respectively. The projected risk capital amounts are then aggregated at each future time period to derive the projected SCRs.

### D.2.6 EIOPA requirements inapplicable to SLOC UK

BEL and risk margin are calculated separately for all business and so there is no section on technical provisions calculated as a whole.

SLOC UK is not using transitional provisions in the calculation of technical provisions.

SLOC UK is not allowing for any volatility or matching adjustment in the calculation of technical provisions. The transitional risk-free interest rate-term structure is not applied and the transitional deduction to technical provisions is not applied.

#### D.2.7 Differences between valuation for solvency purposes and valuation under IFRS

The IFRS reserves are different from Solvency II technical provisions, with Solvency II being £24 million lower (2018: £29 million lower). The main reasons (net of reinsurance) are as follows:

- Solvency II uses a risk margin which is an addition to the BEL, the Solvency II technical provisions are £74 million higher for this reason (2018: £84 million higher).
- IFRS does not use a risk margin, but does have margins for adverse deviation applied to the best estimate assumptions. Solvency II technical provisions are £52 million lower for this reason (2018: £87 million lower).
- Under Solvency II the insurance and investments contract definitions and valuation restrictions do not apply. The Solvency II technical provisions are £35 million lower for this reason (2018: £19 million lower).
- IFRS best estimate expense assumptions include additional expenses not permitted under Solvency II. The Solvency II technical provisions are £8 million lower for this reason (2018: £5 million lower).

The IFRS reinsurance recoverables are different from Solvency II reinsurance recoverables for the same reasons.

## D.3 Other liabilities

The value of each class of other liability, for SLOC UK and for the EEA Group, is given in the quantitative reporting templates in *Appendices 1 and 2*.

#### D.3.1 Deposits from reinsurers

The deposits from reinsurers are detailed in *Section C.3 Credit risk*. The deposits from reinsurers are valued for Solvency II and IFRS at fair value through profit or loss.

#### D.3.2 Insurance and intermediaries payables

The amounts due to policyholders and other policy benefits payable are held at amortised cost, with the carrying amount approximating to fair value, which is consistent with the valuation under IFRS.

#### D.3.3 Payables (trade, not Insurance)

Other liabilities are measured at amortised cost, which is consistent with the valuation under IFRS.

SLOC UK has a leasing arrangement with the owner of the building it occupies and has non-cancellable future minimum lease payments each year until 2022. The lease liability is included in payables, this is consistent with treatment under IFRS 16, with a value of £(1.1) million as at 31 December 2019.

## D.4 Alternative methods for valuation

#### D.4.1 Illiquid bonds

At 31 December 2019, SLOC UK held £215 million of bonds where the fund administrator had been unable to source an updated market price for more than five continuous business days (2018: £149 million).

Where market prices have not been sourced for five continuous business days, a discounted cash flow approach is used to place a mark-to-model value on bonds.

The significant assumptions in the model are as follows:

- The risk free rates of interest;
- The credit spreads; and
- An illiquidity / modelling parameter to reflect the fact that the bonds are illiquid.

**D.4.2 Property**

The property portfolio is managed by a specialist fund manager (Aberdeen Standard Investments) who employs an independent third party specialist valuation agent (Savills UK Limited ("Savills")). Regular meetings with the fund manager keep SLOC UK informed of the level of market activity. Valuations are undertaken monthly by Savills, and reported to SLOC UK by Aberdeen Standard Investments.

Property is valued by Savills in accordance with the Royal Institution of Chartered Surveyors' ("RICS") Valuation – Global Standards 2017, incorporating the International Valuation Standards issued in June 2017 and effective from 1 July 2017 (the RICS Red Book).

The unique nature of properties and infrequent sales make property valuations subjective. Independent property valuations are specific to a property and take account of the circumstances of the property e.g. location, sector, state of repair, quality of tenants, length of outstanding leases. Property valuations also take account of regional factors, such as a scarcity of certain types of properties, and national trends, such as an increase in demand for industrial properties. Experienced valuation agents can accurately value properties allowing for these factors.

The value of a property is the price the property would be expected to sell at in the open market at the date of valuation given the assumptions and guidelines set out in the 'RICS Red Book'. The rental income stream is capitalised at a discount rate that reflects the qualities and risks of the income. The discount rate will be in line with comparable sales and expected market trends.

The monthly valuation takes into account all significant events that occur e.g. the amendment of a lease, change of tenants or the refurbishment of a property. The value of a property would also be reviewed in the light of other similar sales in the region. Each property is visited in-person once a year by Savills.

**D.4.3 Policy facilities**

SLOC UK has a small amount of policy facilities which are mainly in the SLOC With-Profits fund.

Policy facilities are advances that policyholders have taken against the value of their policies. They are valued at the face value of the amounts that were borrowed plus any accumulated interest, since this reflects the amount that customers will repay, or the reduction applied on redemption.

No valuation assumptions are required.

## D.5 Any other information

None

# E. Capital management

## E.1 Own funds

Information on the structure, amount, quality and eligibility of own funds at the end of the year and at the end of the previous year, for SLOC UK and for the EEA Group, is given in the quantitative reporting templates in *Appendices 1 and 2*.

### E.1.1 SLOC UK

**Capital instruments**

The ordinary share capital is fully paid up and is fully available for the absorption of losses. It is the most deeply subordinated in the event of a winding up and is free from all requirements or incentives to redeem, mandatory fixed charges and encumbrances.

All paid up ordinary share capital is classified as tier 1 capital. On 26 March 2018, all preference share capital (£7.5 million) was repaid to the immediate parent company, SLF of Canada UK Limited.

**Movement of own funds in the year**

The following movements have occurred in available own funds for the year:

| | 2019<br>£ million | 2018<br>£ million |
|---|---|---|
| **Available own funds at 1 January** | **424.3** | **466.6** |
| Impact of operating assumption changes | (7.6) | (18.3) |
| Foreseeable dividend | (66.0) | (56.0) |
| Repayment of preference shares | - | ((7.5) |
| Other movements in own funds | 46.8 | 39.5 |
| **Available own funds at 31 December** | **397.5** | **424.3** |

The structure of own funds at 31 December 2019 was identical to that at 1 January 2019. The value of ordinary share capital did not change in the year. The net deferred tax liability is £(9) million (2018: asset of £3 million). The reconciliation reserve decreased from £399 million to £375 million.

**Reconciliation of Net Assets calculated for solvency purposes and Financial Statements' Equity**

£ million

| **Financial Statements Equity** | Reserves Difference | Deferred Acquisition Costs | Deferred Income Liability | Onerous Contracts Provision | Valuation Adjustment for Private Debt Securities | Deferred Tax Difference | **Solvency II Net Assets** |
|---|---|---|---|---|---|---|---|
| **432.7** | 23.7 | (2.5) | 4.9 | 3.9 | 0.3 | 1.3 | **464.3** |

The valuation of reserves and reinsurance recoverables for solvency purposes uses different methods, bases and assumptions from the valuation for the financial statements, as discussed in *Section D.2 Technical provisions*.

Deferred acquisition costs, deferred income liability and onerous contracts provisions are all excluded for solvency purposes.

Private debt securities are measured at amortised cost in the financial statements, but are measured at fair value for solvency purposes. An equivalent adjustment is made to the deposits received from reinsurers.

A deferred tax difference arises due to the differences in valuation of assets and liabilities between the bases.

**E.1.2 The EEA Group**

The EEA Group own funds have been calculated on an accounting consolidation basis, net of all intra-group transactions.

**Capital instruments**

The ordinary share capital included as own funds is fully paid up and is fully available for the absorption of losses. It is the most deeply subordinated in the event of a winding up and is free from all requirements or incentives to redeem, mandatory fixed charges and encumbrances.

£999 of unpaid ordinary share capital has not been included in the own funds of the EEA Group because, in light of its immateriality, approval to do so has not been sought from the regulator.

All paid up ordinary share capital is classified as tier 1 capital.

On 26 March 2018, all preference share capital (£24.5 million) was repaid to the immediate parent company, SLACC.

The structure of own funds at 1 January 2019 is identical to that at 31 December 2019. The value of ordinary share capital did not change in the year. The net deferred tax liability is £(7) million (2018: asset of £4 million). The reconciliation reserve decreased from £172 million to £150 million.

**Movement of EEA Group own funds in the year**

The following movements have occurred in available own funds for the year:

| | **2019 £ million** | **2018 £ million** |
|---|---|---|
| **Available own funds at 1 January** | **426.5** | **485.9** |
| Impact of operating assumption changes | (7.6) | (18.3) |
| Foreseeable dividend | (66.0) | (56.0) |
| Repayment of preference shares | - | (24.5) |
| Other movements in own funds | 46.8 | 39.4 |
| **Available own funds at 31 December** | **399.7** | **426.5** |

**Reconciliation of net assets calculated for solvency purposes and financial statements' equity**

The items causing differences between net assets calculated for solvency purposes and financial statements' equity are identical to those for SLOC UK.

**E.1.3 Deferred tax assets**

Net deferred tax assets are classified as tier 3 capital, as required by the classification rules.

**E.1.4 Reconciliation reserve**

The reconciliation reserve represents retained earnings net of adjustments for restrictions to excess surplus in with-profits business and foreseeable dividends and distributions. The reconciliation reserve is classified as tier 1 capital.

**E.1.5 Restrictions to own funds**

Excess surplus in with-profits business is not available to meet the capital requirements of SLOC UK or the EEA Group, and own funds are reduced accordingly. The total amount of excess surplus is equal to the value of the restriction which reduces the available own funds to zero. The amount is given in the quantitative reporting templates in *Appendices 1 and 2*.

The prescribed limits on restricted tier 1 capital, eligible tier 2 capital and eligible tier 3 capital have no impact.

There are no restrictions affecting transferability, fungibility or availability of own funds items.

**E.1.6 Objectives, policies and processes for capital management**

Capital management, maintenance of a suitable capital structure and capital monitoring work is undertaken by the Capital Management Group ("CMG"), working closely with the RCMC, in accordance with the Capital Management Policy. On a day to day basis, the Head of Business Planning and Capital Management is responsible for ensuring that matters affecting capital are identified and addressed on a timely basis and that capital is considered in all significant business decisions.

The Capital Management Policy defines the approach to management of capital adequacy risk, which is defined as the risk that capital is not or will not be sufficient to withstand adverse conditions and to meet regulatory requirements. It is reviewed and approved by the Board at least annually and sets out the capital management principles including those listed below:

- Setting the level of capital adequacy risk to be prudent and consistent with the principles outlined in the WWG and UK risk management framework documents and risk appetite policies and processes;
- A commitment to maintaining financial strength in order for the organisation to meet its obligations to policyholders and investors as they fall due;
- Maintenance of preferential access to the capital markets for the WWG by maintaining appropriate financial ratings, reflecting strong financial strength and quality;
- Maintenance of a high quality capital structure to ensure compliance with capital adequacy and tiering requirements;
- Aim to, within the level of risk it deems appropriate, maximise the rate of return on its capital; and

- The need to return excess capital to the parent in order to ensure an appropriate return on capital.

The Capital Management Policy also sets out other requirements:

- Reporting and monitoring to be undertaken in respect of UK regulations, Canadian regulations and the SLOC UK and EEA Group risk appetite statements in relation to capital;
- Capital planning requirements and consideration of capital impacts in all significant business decisions;
- The governance approach and the responsibilities in respect of capital management; and
- Details of initiatives available to management to manage capital effectively and mitigate capital risks.

**Capital planning and the overall strategy**

Capital management is a core driver for strategic considerations. In order to properly assess any strategic change, the capital implications are considered, documented and challenged. The requirement for an understanding of capital implications is embedded throughout the business, and particularly in all change initiatives and projects. Any business cases to support initiatives include commentary on capital and evaluation of capital implications. The CMG reviews the projected capital impacts of business initiatives that would materially affect the capital position.

## E.2 Solvency capital requirement and minimum capital requirement

Information on the amount of the capital requirements at the end of the year for SLOC UK and for the EEA Group, both in total and by risk module, is given in the quantitative reporting templates in *Appendices 1 and 2*.

**E.2.1 Minimum capital requirement**

The Linear Minimum Capital Requirement (“$MCR_L$”) is calculated using the prescribed formula.

The Minimum Capital Requirement (“MCR”) floor of 25% of the SCR bites. Changes in MCR are therefore driven by changes in SCR.

**E.2.2 Solvency capital requirement**

SLOC UK uses the standard formula approach to calculate capital requirements, so the inputs used to calculate the SCR are provided by the standard formula. The table below shows how the SCR has changed over the period by risk module, before and after consideration of future discretionary benefits (gross and net, respectively):

| £ million | 2019 | | 2018 | | Change | |
|---|---|---|---|---|---|---|
| | Gross | Net | Gross | Net | Gross | Net |
| **Before Diversification** | | | | | | |
| Market | 181 | 114 | 156 | 98 | 25 | 16 |
| Default | 8 | 8 | 11 | 11 | (3) | (3) |
| Life | 124 | 114 | 164 | 153 | (40) | (39) |
| Health | 3 | 3 | 3 | 3 | - | - |
| Diversification | (62) | (55) | (67) | (59) | 5 | 4 |
| Basic SCR | 254 | 184 | 267 | 206 | (13) | (22) |
| | | | | | | |
| Operational Risk | 30 | 30 | 32 | 32 | (2) | (2) |
| | | | | | | |
| Adjustment included for loss absorbing capacity of technical provisions | - | (70) | - | (61) | - | (9) |
| | | | | | | |
| **SCR - Modular** | **284** | **214** | **299** | **238** | **(15)** | **(24)** |

The SCR has decreased over the year as a result of lower life underwriting risk which has been partially offset by an increase in market risk. Life underwriting risk has reduced due to the implementation of the expense indemnity agreement at the start of the year as described in *Section C.1.5 Material underwriting risk mitigation techniques*. Higher than expected equity returns have contributed to an increase in market risk.

### E.2.3 Undertaking specific parameters, transitional measures and capital add-ons

Undertaking-specific parameters are not used in the SLOC UK standard formula calculation.

No transitional measures have been used.

The supervisor has not specified a capital add-on.

### E.2.4 Simplifications used in calculation of the SCR

No material simplifications are used in the calculation of the SCR.

### E.2.5 Allowance for reinsurance

Reinsurance arrangements are allowed for within the technical provisions and SCR. The overall impact of reinsurance is to reduce BEL by £2.9 billion (2018: £3.0 billion). It also significantly reduces the impact of some of the SCR stresses.

The nature of the reinsurance treaties with Sun Life Bermuda are such that:

Reinsurance cashflows = (gross cashflows excluding expense cashflows) + (fixed allowance from reinsurer for expenses).

These are allowed for within the SCR calculation by calculating a reinsurance asset using the same modelling (including stresses applied) as for the gross reserve but with expenses appropriate to the reinsurer and allowing for this reinsurance asset within the SCR calculation.

### E.2.6 Allowance for future management actions in SCR calculation

Future management actions are allowed for in calculating the technical provisions (these are covered in *Section D.2 Technical provisions*). The same approach is followed in the SCR calculation with the following additional features:

#### E.2.6.1 Varying of future bonus payments for with-profits policies

Within the SCR calculation, aside from operational risk, it is assumed that in the event of a stressed scenario, bonuses can be adjusted to fully offset the cost of the stress, with no allowance made of the time taken to implement such a change.

#### E.2.6.2 Reducing overhead expenses in a mass lapse event

In an event that results in a large number of policyholders lapsing their policies, management would take action to reduce SLOC UK's overhead expenses in response to the smaller customer base.

#### E.2.6.3 Adjustable policy charges

Allowance, up or down, is made for policy charges that are contractually variable, allowing for a short time delay in implementation.

### E.2.7 Allowance for financial risk mitigation techniques in SCR calculation

Significant financial risk mitigation techniques currently used by SLOC UK are shown below:

- The holding of collateral in respect of annuities and GAOs reinsured with Sun Life Bermuda and SLACC – credit is taken for this collateral in the counterparty default risk calculation.

  The deposit back fund for the reinsurance collateral held assets of £3,161 million at 31 December 2019 (2018: £3,122 million). A 10% reduction in the value of that collateral would increase the undiversified counterparty default risk by £4 million (2018: £4 million). Derivative hedges for the SLOC UK GAO and annuity risk exist within the deposit back fund. The SCA for the reinsurance collateral held no funds as at 31 December 2019.

  Although the deposit back fund and SCA are financial risk mitigation techniques used by SLOC UK, the hedges are not since the risks relating to the hedges are reinsured to Sun Life Bermuda and SLACC. The investment management of the deposit back fund, of which derivatives form a part, is carried out by SLOC UK on behalf of the reinsurers and therefore the specifics relating to the hedges are included in management information and documentation.
- The use of derivatives – in the SLOC With-Profits fund there are currency forwards which aim to reduce currency exposure. £6 million of credit is taken for this in the currency risk calculation within the gross SCR (2018: £9 million).
- An interest rate hedge is in place to help protect the overall solvency position of SLOC UK against falls in interest rates.

## E.3 Use of the duration-based equity risk sub-module in the calculation of the solvency capital requirement

The duration-based equity risk sub-module is not used in the calculation of the SCR.

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

An internal model is not used.

## E.5 Non-compliance with the minimum capital requirement and non-compliance with the solvency capital requirement

During the period, the SCR and the MCR were complied with at all times. There is no expectation of future non-compliance with SCR or MCR.

Should the SCR or MCR become under pressure, then management actions would be taken to maintain the solvency position.

## E.6 Any other information

There is no other material information relevant to the capital management of the company or of the EEA Group that has not been disclosed above.

# Appendices

# Sun Life Assurance Company of Canada (U.K.) Limited

## Solvency and Financial Condition Report

## Disclosures

31 December

2019

(Monetary amounts in GBP thousands)

## General information

| | |
|---|---|
| Undertaking name | Sun Life Assurance Company of Canada (U.K.) Limited |
| Undertaking identification code | 549300NZ227BVL5W4E72 |
| Type of code of undertaking | LEI |
| Type of undertaking | Life undertakings |
| Country of authorisation | GB |
| Language of reporting | en |
| Reporting reference date | 31 December 2019 |
| Currency used for reporting | GBP |
| Accounting standards | IFRS |
| Method of Calculation of the SCR | Standard formula |
| Matching adjustment | No use of matching adjustment |
| Volatility adjustment | No use of volatility adjustment |
| Transitional measure on the risk-free interest rate | No use of transitional measure on the risk-free interest rate |
| Transitional measure on technical provisions | No use of transitional measure on technical provisions |

## List of reported templates

S.02.01.02 - Balance sheet
S.05.01.02 - Premiums, claims and expenses by line of business
S.05.02.01 - Premiums, claims and expenses by country
S.12.01.02 - Life and Health SLT Technical Provisions
S.23.01.01 - Own Funds
S.25.01.21 - Solvency Capital Requirement - for undertakings on Standard Formula
S.28.01.01 - Minimum Capital Requirement - Only life or only non-life insurance or reinsurance activity

S.02.01.02

## Balance sheet

| | | Solvency II value |
|---|---|---|
| | Assets | C0010 |
| R0030 | Intangible assets | 0 |
| R0040 | Deferred tax assets | 14,200 |
| R0050 | Pension benefit surplus | 104,432 |
| R0060 | Property, plant & equipment held for own use | 1,070 |
| R0070 | Investments (other than assets held for index-linked and unit-linked contracts) | 4,186,146 |
| R0080 | *Property (other than for own use)* | 38,096 |
| R0090 | *Holdings in related undertakings, including participations* | 440 |
| R0100 | *Equities* | 115,937 |
| R0110 | *Equities - listed* | 115,937 |
| R0120 | *Equities - unlisted* | 0 |
| R0130 | *Bonds* | 3,838,421 |
| R0140 | *Government Bonds* | 1,010,971 |
| R0150 | *Corporate Bonds* | 2,744,310 |
| R0160 | *Structured notes* | 0 |
| R0170 | *Collateralised securities* | 83,140 |
| R0180 | *Collective Investments Undertakings* | 35,047 |
| R0190 | *Derivatives* | 158,204 |
| R0200 | *Deposits other than cash equivalents* | 0 |
| R0210 | *Other investments* | 0 |
| R0220 | Assets held for index-linked and unit-linked contracts | 6,672,816 |
| R0230 | Loans and mortgages | 16,542 |
| R0240 | *Loans on policies* | 16,542 |
| R0250 | *Loans and mortgages to individuals* | 0 |
| R0260 | *Other loans and mortgages* | 0 |
| R0270 | Reinsurance recoverables from: | 2,941,492 |
| R0280 | *Non-life and health similar to non-life* | 0 |
| R0290 | *Non-life excluding health* | 0 |
| R0300 | *Health similar to non-life* | 0 |
| R0310 | *Life and health similar to life, excluding index-linked and unit-linked* | 2,932,497 |
| R0320 | *Health similar to life* | 0 |
| R0330 | *Life excluding health and index-linked and unit-linked* | 2,932,497 |
| R0340 | *Life index-linked and unit-linked* | 8,995 |
| R0350 | Deposits to cedants | 0 |
| R0360 | Insurance and intermediaries receivables | 78 |
| R0370 | Reinsurance receivables | 4,040 |
| R0380 | Receivables (trade, not insurance) | 30,236 |
| R0390 | Own shares (held directly) | 0 |
| R0400 | Amounts due in respect of own fund items or initial fund called up but not yet paid in | 0 |
| R0410 | Cash and cash equivalents | 14,622 |
| R0420 | Any other assets, not elsewhere shown | 0 |
| R0500 | Total assets | 13,985,672 |

S.02.01.02

## Balance sheet

| | | Solvency II value |
|---|---|---|
| | Liabilities | C0010 |
| R0510 | Technical provisions - non-life | 0 |
| R0520 | *Technical provisions - non-life (excluding health)* | 0 |
| R0530 | *TP calculated as a whole* | 0 |
| R0540 | *Best Estimate* | 0 |
| R0550 | *Risk margin* | 0 |
| R0560 | *Technical provisions - health (similar to non-life)* | 0 |
| R0570 | *TP calculated as a whole* | 0 |
| R0580 | *Best Estimate* | 0 |
| R0590 | *Risk margin* | 0 |
| R0600 | Technical provisions - life (excluding index-linked and unit-linked) | 3,568,994 |
| R0610 | *Technical provisions - health (similar to life)* | 0 |
| R0620 | *TP calculated as a whole* | 0 |
| R0630 | *Best Estimate* | 0 |
| R0640 | *Risk margin* | 0 |
| R0650 | *Technical provisions - life (excluding health and index-linked and unit-linked)* | 3,568,994 |
| R0660 | *TP calculated as a whole* | 0 |
| R0670 | *Best Estimate* | 3,544,288 |
| R0680 | *Risk margin* | 24,706 |
| R0690 | Technical provisions - index-linked and unit-linked | 6,493,549 |
| R0700 | *TP calculated as a whole* | 0 |
| R0710 | *Best Estimate* | 6,444,358 |
| R0720 | *Risk margin* | 49,191 |
| R0740 | Contingent liabilities | 0 |
| R0750 | Provisions other than technical provisions | 3,999 |
| R0760 | Pension benefit obligations | 2,555 |
| R0770 | Deposits from reinsurers | 3,161,148 |
| R0780 | Deferred tax liabilities | 23,103 |
| R0790 | Derivatives | 36,080 |
| R0800 | Debts owed to credit institutions | 0 |
| R0810 | Financial liabilities other than debts owed to credit institutions | 0 |
| R0820 | Insurance & intermediaries payables | 92,333 |
| R0830 | Reinsurance payables | 0 |
| R0840 | Payables (trade, not insurance) | 139,629 |
| R0850 | Subordinated liabilities | 0 |
| R0860 | *Subordinated liabilities not in BOF* | 0 |
| R0870 | *Subordinated liabilities in BOF* | 0 |
| R0880 | Any other liabilities, not elsewhere shown | 0 |
| R0900 | Total liabilities | 13,521,391 |
| | | |
| R1000 | Excess of assets over liabilities | 464,282 |

S.05.01.02

## Premiums, claims and expenses by line of business

### Life

| | | Line of Business for: life insurance obligations | | | | | | Life reinsurance obligations | | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Health insurance | Insurance with profit participation | Index-linked and unit-linked insurance | Other life insurance | Annuities stemming from non-life insurance contracts and relating to health insurance obligations | Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations | Health reinsurance | Life reinsurance | |
| | | C0210 | C0220 | C0230 | C0240 | C0250 | C0260 | C0270 | C0280 | C0300 |
| | Premiums written | | | | | | | | | |
| R1410 | Gross | 0 | 5,930 | 71,043 | 9,149 | | | | | 86,121 |
| R1420 | Reinsurers' share | 0 | 19 | 8,164 | 8,138 | | | | | 16,321 |
| R1500 | Net | 0 | 5,910 | 62,879 | 1,011 | | | 0 | 0 | 69,800 |
| | Premiums earned | | | | | | | | | |
| R1510 | Gross | 0 | 5,930 | 71,043 | 9,149 | | | | | 86,121 |
| R1520 | Reinsurers' share | 0 | 19 | 8,164 | 8,138 | | | | | 16,321 |
| R1600 | Net | 0 | 5,910 | 62,879 | 1,011 | | | 0 | 0 | 69,800 |
| | Claims incurred | | | | | | | | | |
| R1610 | Gross | 0 | 68,545 | 647,461 | 181,469 | | | | | 897,475 |
| R1620 | Reinsurers' share | 0 | 0 | 29,775 | 168,361 | | | | | 198,136 |
| R1700 | Net | 0 | 68,545 | 617,686 | 13,108 | | | 0 | 0 | 699,339 |
| | Changes in other technical provisions | | | | | | | | | |
| R1710 | Gross | 0 | 0 | 0 | 0 | | | | | 0 |
| R1720 | Reinsurers' share | 0 | 0 | 0 | 0 | | | | | 0 |
| R1800 | Net | 0 | 0 | 0 | 0 | | | 0 | 0 | 0 |
| R1900 | Expenses incurred | 0 | 3,793 | 78,150 | 11,293 | | | 0 | 0 | 93,236 |
| R2500 | Other expenses | | | | | | | | | |
| R2600 | Total expenses | | | | | | | | | 93,236 |

S.05.02.01

## Premiums, claims and expenses by country

### Life

| | | C0150 | C0160 | C0170 | C0180 | C0190 | C0200 | C0210 |
|---|---|---|---|---|---|---|---|---|
| | | Home Country | Top 5 countries (by amount of gross premiums written) - life obligations | | | Top 5 countries (by amount of gross premiums written) - life obligations | | Total Top 5 and home country |
| R1400 | | | | | | | | |
| | | C0220 | C0230 | C0240 | C0250 | C0260 | C0270 | C0280 |
| | Premiums written | | | | | | | |
| R1410 | Gross | 86,121 | | | | | | 86,121 |
| R1420 | Reinsurers' share | 16,321 | | | | | | 16,321 |
| R1500 | Net | 69,800 | | | | | | 69,800 |
| | Premiums earned | | | | | | | |
| R1510 | Gross | 86,121 | | | | | | 86,121 |
| R1520 | Reinsurers' share | 16,321 | | | | | | 16,321 |
| R1600 | Net | 69,800 | | | | | | 69,800 |
| | Claims incurred | | | | | | | |
| R1610 | Gross | 897,475 | | | | | | 897,475 |
| R1620 | Reinsurers' share | 198,136 | | | | | | 198,136 |
| R1700 | Net | 699,339 | | | | | | 699,339 |
| | Changes in other technical provisions | | | | | | | |
| R1710 | Gross | 0 | | | | | | 0 |
| R1720 | Reinsurers' share | 0 | | | | | | 0 |
| R1800 | Net | 0 | | | | | | 0 |
| R1900 | Expenses incurred | 93,236 | | | | | | 93,236 |
| R2500 | Other expenses | | | | | | | |
| R2600 | Total expenses | | | | | | | 93,236 |

S.12.01.02

## Life and Health SLT Technical Provisions

| | | Insurance with profit participation | Index-linked and unit-linked insurance | | | Other life insurance | | | Annuities stemming from non-life insurance contracts and relating to insurance obligation other than health insurance obligations | Accepted reinsurance | Total (Life other than health insurance, including Unit-Linked) | Health insurance (direct business) | | | Annuities stemming from non-life insurance contracts and relating to health insurance obligations | Health reinsurance (reinsurance accepted) | Total (Health similar to life insurance) |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Contracts without options and guarantees | Contracts with options or guarantees | | Contracts without options and guarantees | Contracts with options or guarantees | | | | | Contracts without options and guarantees | Contracts with options or guarantees | | | |
| | | C0020 | C0030 | C0040 | C0050 | C0060 | C0070 | C0080 | C0090 | C0100 | C0150 | C0160 | C0170 | C0180 | C0190 | C0200 | C0210 |
| R0010 | Technical provisions calculated as a whole | | | | | | | | | 0 | 0 | | | | | | 0 |
| R0020 | Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole | | | | | | | | | 0 | 0 | | | | | | 0 |
| | Technical provisions calculated as a sum of BE and RM | | | | | | | | | | | | | | | | |
| | Best estimate | | | | | | | | | | | | | | | | |
| R0030 | Gross Best Estimate | 511,322 | | 5,170,638 | 1,273,720 | | 2,553,406 | 476,547 | | 3,014 | 9,988,646 | | 0 | 0 | | 0 | 0 |
| R0080 | Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default | 0 | | 8,073 | 922 | | 2,572,553 | 359,944 | | 0 | 2,941,492 | | 0 | 0 | | 0 | 0 |
| R0090 | Best estimate minus recoverables from reinsurance/SPV and Finite Re | 511,322 | | 5,162,566 | 1,272,798 | | -19,148 | 116,603 | | 3,014 | 7,047,155 | | 0 | 0 | | 0 | 0 |
| R0100 | Risk margin | 1,555 | 49,191 | | | 23,128 | | | | 23 | 73,897 | 0 | | | | 0 | 0 |
| | Amount of the transitional on Technical Provisions | | | | | | | | | | | | | | | | |
| R0110 | Technical Provisions calculated as a whole | | | | | | | | | | 0 | | | | | | 0 |
| R0120 | Best estimate | | | | | | | | | | 0 | | | | | | 0 |
| R0130 | Risk margin | | | | | | | | | | 0 | | | | | | 0 |
| R0200 | Technical provisions - total | 512,877 | 6,493,549 | | | 3,053,081 | | | | 3,037 | 10,062,543 | 0 | | | | 0 | 0 |

S.23.01.01

## Own Funds

| | Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35 | Total | Tier 1 unrestricted | Tier 1 restricted | Tier 2 | Tier 3 |
|---|---|---|---|---|---|---|
| | | C0010 | C0020 | C0030 | C0040 | C0050 |
| R0010 | Ordinary share capital (gross of own shares) | 22,500 | 22,500 | | 0 | |
| R0030 | Share premium account related to ordinary share capital | 0 | 0 | | 0 | |
| R0040 | Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings | 0 | 0 | | 0 | |
| R0050 | Subordinated mutual member accounts | 0 | | 0 | 0 | 0 |
| R0070 | Surplus funds | 0 | 0 | | | |
| R0090 | Preference shares | 0 | | 0 | 0 | 0 |
| R0110 | Share premium account related to preference shares | 0 | | 0 | 0 | 0 |
| R0130 | Reconciliation reserve | 374,970 | 374,970 | | | |
| R0140 | Subordinated liabilities | 0 | | 0 | 0 | 0 |
| R0160 | An amount equal to the value of net deferred tax assets | 0 | | | | 0 |
| R0180 | Other own fund items approved by the supervisory authority as basic own funds not specified above | 0 | 0 | 0 | 0 | 0 |
| R0220 | Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds | 0 | | | | |
| R0230 | Deductions for participations in financial and credit institutions | 0 | 0 | 0 | 0 | |
| R0290 | Total basic own funds after deductions | 397,470 | 397,470 | 0 | 0 | 0 |
| | Ancillary own funds | | | | | |
| R0300 | Unpaid and uncalled ordinary share capital callable on demand | 0 | | | | |
| R0310 | Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand | 0 | | | | |
| R0320 | Unpaid and uncalled preference shares callable on demand | 0 | | | | |
| R0330 | A legally binding commitment to subscribe and pay for subordinated liabilities on demand | 0 | | | | |
| R0340 | Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC | 0 | | | | |
| R0350 | Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC | 0 | | | | |
| R0360 | Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC | 0 | | | | |
| R0370 | Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC | 0 | | | | |
| R0390 | Other ancillary own funds | 0 | | | | |
| R0400 | Total ancillary own funds | 0 | | | 0 | 0 |
| | Available and eligible own funds | | | | | |
| R0500 | Total available own funds to meet the SCR | 397,470 | 397,470 | 0 | 0 | 0 |
| R0510 | Total available own funds to meet the MCR | 397,470 | 397,470 | 0 | 0 | |
| R0540 | Total eligible own funds to meet the SCR | 397,470 | 397,470 | 0 | 0 | 0 |
| R0550 | Total eligible own funds to meet the MCR | 397,470 | 397,470 | 0 | 0 | |
| R0580 | SCR | 213,720 | | | | |
| R0600 | MCR | 53,430 | | | | |
| R0620 | Ratio of Eligible own funds to SCR | 185.98% | | | | |
| R0640 | Ratio of Eligible own funds to MCR | 743.91% | | | | |

| | Reconcilliation reserve | C0060 |
|---|---|---|
| R0700 | Excess of assets over liabilities | 464,282 |
| R0710 | Own shares (held directly and indirectly) | 0 |
| R0720 | Foreseeable dividends, distributions and charges | 66,000 |
| R0730 | Other basic own fund items | 22,500 |
| R0740 | Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds | 812 |
| R0760 | Reconciliation reserve | 374,970 |
| | Expected profits | |
| R0770 | Expected profits included in future premiums (EPIFP) - Life business | 62,532 |
| R0780 | Expected profits included in future premiums (EPIFP) - Non- life business | 0 |
| R0790 | Total Expected profits included in future premiums (EPIFP) | 62,532 |

S.25.01.21

## Solvency Capital Requirement - for undertakings on Standard Formula

| | | Gross solvency capital requirement | USP | Simplifications |
|---|---|---|---|---|
| | | C0110 | C0090 | C0120 |
| R0010 | Market risk | 180,735 | | 9 |
| R0020 | Counterparty default risk | 8,090 | | |
| R0030 | Life underwriting risk | 124,327 | 9 | 9 |
| R0040 | Health underwriting risk | 2,843 | 9 | 9 |
| R0050 | Non-life underwriting risk | 0 | 9 | 9 |
| R0060 | Diversification | -61,808 | | |
| R0070 | Intangible asset risk | 0 | | |
| R0100 | Basic Solvency Capital Requirement | 254,186 | | |

USP Key

For life underwriting risk:
1 - Increase in the amount of annuity benefits
9 - None

For health underwriting risk:
1 - Increase in the amount of annuity benefits
2 - Standard deviation for NSLT health premium risk
3 - Standard deviation for NSLT health gross premium risk
4 - Adjustment factor for non-proportional reinsurance
5 - Standard deviation for NSLT health reserve risk
9 - None

For non-life underwriting risk:
4 - Adjustment factor for non-proportional reinsurance
6 - Standard deviation for non-life premium risk
7 - Standard deviation for non-life gross premium risk
8 - Standard deviation for non-life reserve risk
9 - None

| | Calculation of Solvency Capital Requirement | C0100 |
|---|---|---|
| R0130 | Operational risk | 29,639 |
| R0140 | Loss-absorbing capacity of technical provisions | -70,105 |
| R0150 | Loss-absorbing capacity of deferred taxes | 0 |
| R0160 | Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC | 0 |
| R0200 | Solvency Capital Requirement excluding capital add-on | 213,720 |
| R0210 | Capital add-ons already set | 0 |
| R0220 | Solvency capital requirement | 213,720 |
| | Other information on SCR | |
| R0400 | Capital requirement for duration-based equity risk sub-module | 0 |
| R0410 | Total amount of Notional Solvency Capital Requirements for remaining part | 211,419 |
| R0420 | Total amount of Notional Solvency Capital Requirements for ring fenced funds | 2,301 |
| R0430 | Total amount of Notional Solvency Capital Requirements for matching adjustment portfolios | 0 |
| R0440 | Diversification effects due to RFF nSCR aggregation for article 304 | 0 |

| | Approach to tax rate | C0109 |
|---|---|---|
| R0590 | Approach based on average tax rate | 0 |

| | Calculation of loss absorbing capacity of deferred taxes | LAC DT |
|---|---|---|
| | | C0130 |
| R0640 | LAC DT | 0 |
| R0650 | LAC DT justified by reversion of deferred tax liabilities | 0 |
| R0660 | LAC DT justified by reference to probable future taxable economic profit | 0 |
| R0670 | LAC DT justified by carry back, current year | 0 |
| R0680 | LAC DT justified by carry back, future years | 0 |
| R0690 | Maximum LAC DT | 0 |

S.28.01.01

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

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

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

| | Linear formula component for life insurance and reinsurance obligations | C0040 |
|---|---|---|
| R0200 | $MCR_L$ Result | 50,944 |

| | | Net (of reinsurance/SPV) best estimate and TP calculated as a whole | Net (of reinsurance/SPV) total capital at risk |
|---|---|---|---|
| | | C0050 | C0060 |
| R0210 | Obligations with profit participation - guaranteed benefits | 332,140 | |
| R0220 | Obligations with profit participation - future discretionary benefits | 179,182 | |
| R0230 | Index-linked and unit-linked insurance obligations | 6,435,363 | |
| R0240 | Other life (re)insurance and health (re)insurance obligations | 100,470 | |
| R0250 | Total capital at risk for all life (re)insurance obligations | | 1,164,502 |

| | Overall MCR calculation | C0070 |
|---|---|---|
| R0300 | Linear MCR | 50,944 |
| R0310 | SCR | 213,720 |
| R0320 | MCR cap | 96,174 |
| R0330 | MCR floor | 53,430 |
| R0340 | Combined MCR | 53,430 |
| R0350 | Absolute floor of the MCR | 3,187 |
| R0400 | Minimum Capital Requirement | 53,430 |

# SLF of Canada UK Limited

## Solvency and Financial Condition Report

## Disclosures

31 December

2019

(Monetary amounts in GBP thousands)

## General information

| | |
|---|---|
| Participating undertaking name | SLF of Canada UK Limited |
| Group identification code | 213800LBGGLJPIBQ4P08 |
| Type of code of group | LEI |
| Country of the group supervisor | GB |
| Language of reporting | en |
| Reporting reference date | 31 December 2019 |
| Currency used for reporting | GBP |
| Accounting standards | IFRS |
| Method of Calculation of the group SCR | Standard formula |
| Method of group solvency calculation | Method 1 is used exclusively |
| Matching adjustment | No use of matching adjustment |
| Volatility adjustment | No use of volatility adjustment |
| Transitional measure on the risk-free interest rate | No use of transitional measure on the risk-free interest rate |
| Transitional measure on technical provisions | No use of transitional measure on technical provisions |

## List of reported templates

S.02.01.02 - Balance sheet
S.05.01.02 - Premiums, claims and expenses by line of business
S.05.02.01 - Premiums, claims and expenses by country
S.23.01.22 - Own Funds
S.25.01.22 - Solvency Capital Requirement - for groups on Standard Formula
S.32.01.22 - Undertakings in the scope of the group

S.02.01.02

## Balance sheet

| | | Solvency II value |
|---|---|---|
| | Assets | C0010 |
| R0030 | Intangible assets | 0 |
| R0040 | Deferred tax assets | 15,696 |
| R0050 | Pension benefit surplus | 104,432 |
| R0060 | Property, plant & equipment held for own use | 1,420 |
| R0070 | Investments (other than assets held for index-linked and unit-linked contracts) | 4,185,955 |
| R0080 | *Property (other than for own use)* | 38,346 |
| R0090 | *Holdings in related undertakings, including participations* | 0 |
| R0100 | *Equities* | 115,937 |
| R0110 | *Equities - listed* | 115,937 |
| R0120 | *Equities - unlisted* | 0 |
| R0130 | *Bonds* | 3,838,421 |
| R0140 | *Government Bonds* | 1,010,971 |
| R0150 | *Corporate Bonds* | 2,744,310 |
| R0160 | *Structured notes* | 0 |
| R0170 | *Collateralised securities* | 83,140 |
| R0180 | *Collective Investments Undertakings* | 35,047 |
| R0190 | *Derivatives* | 158,204 |
| R0200 | *Deposits other than cash equivalents* | 0 |
| R0210 | *Other investments* | 0 |
| R0220 | Assets held for index-linked and unit-linked contracts | 6,672,816 |
| R0230 | Loans and mortgages | 16,542 |
| R0240 | *Loans on policies* | 16,542 |
| R0250 | *Loans and mortgages to individuals* | 0 |
| R0260 | *Other loans and mortgages* | 0 |
| R0270 | Reinsurance recoverables from: | 2,941,492 |
| R0280 | *Non-life and health similar to non-life* | 0 |
| R0290 | *Non-life excluding health* | 0 |
| R0300 | *Health similar to non-life* | 0 |
| R0310 | *Life and health similar to life, excluding index-linked and unit-linked* | 2,932,497 |
| R0320 | *Health similar to life* | 0 |
| R0330 | *Life excluding health and index-linked and unit-linked* | 2,932,497 |
| R0340 | *Life index-linked and unit-linked* | 8,995 |
| R0350 | Deposits to cedants | 0 |
| R0360 | Insurance and intermediaries receivables | 78 |
| R0370 | Reinsurance receivables | 4,040 |
| R0380 | Receivables (trade, not insurance) | 30,239 |
| R0390 | Own shares (held directly) | 0 |
| R0400 | Amounts due in respect of own fund items or initial fund called up but not yet paid in | 0 |
| R0410 | Cash and cash equivalents | 19,079 |
| R0420 | Any other assets, not elsewhere shown | 0 |
| R0500 | Total assets | 13,991,789 |

S.02.01.02

## Balance sheet

| | | Solvency II value |
|---|---|---|
| | **Liabilities** | C0010 |
| R0510 | Technical provisions - non-life | 0 |
| R0520 | *Technical provisions - non-life (excluding health)* | 0 |
| R0530 | *TP calculated as a whole* | 0 |
| R0540 | *Best Estimate* | 0 |
| R0550 | *Risk margin* | 0 |
| R0560 | *Technical provisions - health (similar to non-life)* | 0 |
| R0570 | *TP calculated as a whole* | 0 |
| R0580 | *Best Estimate* | 0 |
| R0590 | *Risk margin* | 0 |
| R0600 | Technical provisions - life (excluding index-linked and unit-linked) | 3,568,994 |
| R0610 | *Technical provisions - health (similar to life)* | 0 |
| R0620 | *TP calculated as a whole* | 0 |
| R0630 | *Best Estimate* | 0 |
| R0640 | *Risk margin* | 0 |
| R0650 | *Technical provisions - life (excluding health and index-linked and unit-linked)* | 3,568,994 |
| R0660 | *TP calculated as a whole* | 0 |
| R0670 | *Best Estimate* | 3,544,288 |
| R0680 | *Risk margin* | 24,706 |
| R0690 | Technical provisions - index-linked and unit-linked | 6,493,549 |
| R0700 | *TP calculated as a whole* | 0 |
| R0710 | *Best Estimate* | 6,444,358 |
| R0720 | *Risk margin* | 49,191 |
| R0740 | Contingent liabilities | 0 |
| R0750 | Provisions other than technical provisions | 5,310 |
| R0760 | Pension benefit obligations | 2,555 |
| R0770 | Deposits from reinsurers | 3,161,148 |
| R0780 | Deferred tax liabilities | 23,103 |
| R0790 | Derivatives | 36,080 |
| R0800 | Debts owed to credit institutions | 0 |
| R0810 | Financial liabilities other than debts owed to credit institutions | 0 |
| R0820 | Insurance & intermediaries payables | 92,333 |
| R0830 | Reinsurance payables | 0 |
| R0840 | Payables (trade, not insurance) | 142,205 |
| R0850 | Subordinated liabilities | 0 |
| R0860 | *Subordinated liabilities not in BOF* | 0 |
| R0870 | *Subordinated liabilities in BOF* | 0 |
| R0880 | Any other liabilities, not elsewhere shown | 0 |
| R0900 | **Total liabilities** | 13,525,277 |
| | | |
| R1000 | **Excess of assets over liabilities** | 466,512 |

S.05.01.02

## Premiums, claims and expenses by line of business

### Life

| | | Line of Business for: life insurance obligations | | | | | | Life reinsurance obligations | | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Health insurance | Insurance with profit participation | Index-linked and unit-linked insurance | Other life insurance | Annuities stemming from non-life insurance contracts and relating to health insurance obligations | Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations | Health reinsurance | Life reinsurance | |
| | | C0210 | C0220 | C0230 | C0240 | C0250 | C0260 | C0270 | C0280 | C0300 |
| | Premiums written | | | | | | | | | |
| R1410 | Gross | 0 | 5,930 | 71,043 | 9,149 | | | | | 86,121 |
| R1420 | Reinsurers' share | 0 | 19 | 8,164 | 8,138 | | | | | 16,321 |
| R1500 | Net | 0 | 5,910 | 62,879 | 1,011 | | | | | 69,800 |
| | Premiums earned | | | | | | | | | |
| R1510 | Gross | 0 | 5,930 | 71,043 | 9,149 | | | | | 86,121 |
| R1520 | Reinsurers' share | 0 | 19 | 8,164 | 8,138 | | | | | 16,321 |
| R1600 | Net | 0 | 5,910 | 62,879 | 1,011 | | | | | 69,800 |
| | Claims incurred | | | | | | | | | |
| R1610 | Gross | 0 | 68,545 | 647,461 | 181,469 | | | | | 897,475 |
| R1620 | Reinsurers' share | 0 | 0 | 29,775 | 168,361 | | | | | 198,136 |
| R1700 | Net | 0 | 68,545 | 617,686 | 13,108 | | | | | 699,339 |
| | Changes in other technical provisions | | | | | | | | | |
| R1710 | Gross | 0 | 0 | 0 | 0 | | | | | 0 |
| R1720 | Reinsurers' share | 0 | 0 | 0 | 0 | | | | | 0 |
| R1800 | Net | 0 | 0 | 0 | 0 | | | | | 0 |
| R1900 | Expenses incurred | 0 | 3,793 | 78,150 | 11,338 | | | | | 93,281 |
| R2500 | Other expenses | | | | | | | | | 0 |
| R2600 | Total expenses | | | | | | | | | 93,281 |

S.05.02.01

## Premiums, claims and expenses by country

### Life

| | | C0150 | C0160 | C0170 | C0180 | C0190 | C0200 | C0210 |
|---|---|---|---|---|---|---|---|---|
| | | Home Country | Top 5 countries (by amount of gross premiums written) - life obligations | | | Top 5 countries (by amount of gross premiums written) - life obligations | | Total Top 5 and home country |
| R1400 | | | | | | | | |
| | | C0220 | C0230 | C0240 | C0250 | C0260 | C0270 | C0280 |
| | Premiums written | | | | | | | |
| R1410 | Gross | 86,121 | | | | | | 86,121 |
| R1420 | Reinsurers' share | 16,321 | | | | | | 16,321 |
| R1500 | Net | 69,800 | | | | | | 69,800 |
| | Premiums earned | | | | | | | |
| R1510 | Gross | 86,121 | | | | | | 86,121 |
| R1520 | Reinsurers' share | 16,321 | | | | | | 16,321 |
| R1600 | Net | 69,800 | | | | | | 69,800 |
| | Claims incurred | | | | | | | |
| R1610 | Gross | 897,475 | | | | | | 897,475 |
| R1620 | Reinsurers' share | 198,136 | | | | | | 198,136 |
| R1700 | Net | 699,339 | | | | | | 699,339 |
| | Changes in other technical provisions | | | | | | | |
| R1710 | Gross | 0 | | | | | | 0 |
| R1720 | Reinsurers' share | 0 | | | | | | 0 |
| R1800 | Net | 0 | | | | | | 0 |
| R1900 | Expenses incurred | 93,281 | | | | | | 93,281 |
| R2500 | Other expenses | | | | | | | |
| R2600 | Total expenses | | | | | | | 93,281 |

S.23.01.22

## Own Funds

| | Basic own funds before deduction for participations in other financial sector | Total | Tier 1 unrestricted | Tier 1 restricted | Tier 2 | Tier 3 |
|---|---|---|---|---|---|---|
| | | C0010 | C0020 | C0030 | C0040 | C0050 |
| R0010 | Ordinary share capital (gross of own shares) | 250,050 | 250,050 | | 0 | |
| R0020 | *Non-available called but not paid in ordinary share capital at group level* | 0 | | | | |
| R0030 | Share premium account related to ordinary share capital | 0 | 0 | | 0 | |
| R0040 | Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings | 0 | 0 | | 0 | |
| R0050 | Subordinated mutual member accounts | 0 | | 0 | 0 | 0 |
| R0060 | *Non-available subordinated mutual member accounts at group level* | 0 | | | | |
| R0070 | Surplus funds | 0 | 0 | | | |
| R0080 | *Non-available surplus funds at group level* | 0 | 0 | | | |
| R0090 | Preference shares | 0 | | 0 | 0 | 0 |
| R0100 | *Non-available preference shares at group level* | 0 | | | | |
| R0110 | Share premium account related to preference shares | 0 | | 0 | 0 | 0 |
| R0120 | *Non-available share premium account related to preference shares at group level* | 0 | | | | |
| R0130 | Reconciliation reserve | 149,650 | 149,650 | | | |
| R0140 | Subordinated liabilities | 0 | | 0 | 0 | 0 |
| R0150 | *Non-available subordinated liabilities at group level* | 0 | | | | |
| R0160 | An amount equal to the value of net deferred tax assets | 0 | | | | 0 |
| R0170 | *The amount equal to the value of net deferred tax assets not available at the group level* | 0 | | | | 0 |
| R0180 | Other items approved by supervisory authority as basic own funds not specified above | 0 | 0 | 0 | 0 | 0 |
| R0190 | *Non available own funds related to other own funds items approved by supervisory authority* | 0 | | | | |
| R0200 | Minority interests (if not reported as part of a specific own fund item) | 0 | | | | |
| R0210 | *Non-available minority interests at group level* | 0 | | | | |
| R0220 | Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds | | | | | |
| R0230 | Deductions for participations in other financial undertakings, including non-regulated undertakings carrying out financial activities | 0 | | | | |
| R0240 | *whereof deducted according to art 228 of the Directive 2009/138/EC* | 0 | | | | |
| R0250 | Deductions for participations where there is non-availability of information (Article 229) | 0 | | | | |
| R0260 | Deduction for participations included by using D&A when a combination of methods is used | 0 | | | | |
| R0270 | Total of non-available own fund items | 0 | 0 | 0 | 0 | 0 |
| R0280 | Total deductions | 0 | 0 | 0 | 0 | 0 |
| R0290 | Total basic own funds after deductions | 399,700 | 399,700 | 0 | 0 | 0 |
| | **Ancillary own funds** | | | | | |
| R0300 | Unpaid and uncalled ordinary share capital callable on demand | 0 | | | | |
| R0310 | Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand | 0 | | | | |
| R0320 | Unpaid and uncalled preference shares callable on demand | 0 | | | | |
| R0330 | A legally binding commitment to subscribe and pay for subordinated liabilities on demand | 0 | | | | |
| R0340 | Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC | 0 | | | | |
| R0350 | Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC | 0 | | | | |
| R0360 | Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC | 0 | | | | |
| R0370 | Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC | 0 | | | | |
| R0380 | Non available ancillary own funds at group level | 0 | | | | |
| R0390 | Other ancillary own funds | 0 | | | | |
| R0400 | Total ancillary own funds | 0 | | | 0 | 0 |
| | **Own funds of other financial sectors** | | | | | |
| R0410 | Credit Institutions, investment firms, financial institutions, alternative investment fund managers, UCITS management companies | 0 | | | | |
| R0420 | Institutions for occupational retirement provision | 0 | | | | |
| R0430 | Non regulated entities carrying out financial activities | 0 | | | | |
| R0440 | Total own funds of other financial sectors | 0 | 0 | 0 | 0 | 0 |

S.23.01.22
## Own Funds

| | | Total | Tier 1 unrestricted | Tier 1 restricted | Tier 2 | Tier 3 |
|---|---|---|---|---|---|---|
| | Basic own funds before deduction for participations in other financial sector | C0010 | C0020 | C0030 | C0040 | C0050 |
| | Own funds when using the D&A, exclusively or in combination of method 1 | | | | | |
| R0450 | Own funds aggregated when using the D&A and combination of method | 0 | | | | |
| R0460 | Own funds aggregated when using the D&A and combination of method net of IGT | 0 | | | | |
| R0520 | Total available own funds to meet the consolidated group SCR (excluding own funds from other financial sector and from the undertakings included via D&A ) | 399,700 | 399,700 | 0 | 0 | 0 |
| R0530 | Total available own funds to meet the minimum consolidated group SCR | 399,700 | 399,700 | 0 | 0 | |
| R0560 | Total eligible own funds to meet the consolidated group SCR (excluding own funds from other financial sector and from the undertakings included via D&A ) | 399,700 | 399,700 | 0 | 0 | 0 |
| R0570 | Total eligible own funds to meet the minimum consolidated group SCR (group) | 399,700 | 399,700 | 0 | 0 | |
| R0610 | Minimum consolidated Group SCR | 53,430 | | | | |
| R0650 | Ratio of Eligible own funds to Minimum Consolidated Group SCR | 748.08% | | | | |
| R0660 | Total eligible own funds to meet the group SCR (including own funds from other financial sector and from the undertakings included via D&A ) | 399,700 | 399,700 | 0 | 0 | 0 |
| R0680 | Group SCR | 213,720 | | | | |
| R0690 | Ratio of Eligible own funds to group SCR including other financial sectors and the undertakings included via D&A | 187.02% | | | | |

| | Reconcilliation reserve | C0060 |
|---|---|---|
| R0700 | Excess of assets over liabilities | 466,512 |
| R0710 | Own shares (held directly and indirectly) | |
| R0720 | Forseeable dividends, distributions and charges | 66,000 |
| R0730 | Other basic own fund items | 250,050 |
| R0740 | Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds | 812 |
| R0750 | Other non available own funds | |
| R0760 | Reconciliation reserve | 149,650 |
| | Expected profits | |
| R0770 | Expected profits included in future premiums (EPIFP) - Life business | 62,532 |
| R0780 | Expected profits included in future premiums (EPIFP) - Non- life business | 0 |
| R0790 | Total Expected profits included in future premiums (EPIFP) | 62,532 |

S.25.01.22

## Solvency Capital Requirement - for groups on Standard Formula

| | | Gross solvency capital requirement | USP | Simplifications |
|---|---|---|---|---|
| | | C0110 | C0090 | C0120 |
| R0010 | Market risk | 180,735 | | 9 |
| R0020 | Counterparty default risk | 8,090 | | |
| R0030 | Life underwriting risk | 124,327 | 9 | 9 |
| R0040 | Health underwriting risk | 2,843 | 9 | 9 |
| R0050 | Non-life underwriting risk | 0 | 9 | 9 |
| R0060 | Diversification | -68,790 | | |
| R0070 | Intangible asset risk | 0 | | |
| R0100 | Basic Solvency Capital Requirement | 247,204 | | |

| | Calculation of Solvency Capital Requirement | C0100 |
|---|---|---|
| R0130 | Operational risk | 29,639 |
| R0140 | Loss-absorbing capacity of technical provisions | -70,105 |
| R0150 | Loss-absorbing capacity of deferred taxes | 0 |
| R0160 | Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC | 0 |
| R0200 | Solvency Capital Requirement excluding capital add-on | 206,738 |
| R0210 | Capital add-ons already set | 0 |
| R0220 | Solvency capital requirement for undertakings under consolidated method | 206,738 |
| | **Other information on SCR** | |
| R0400 | Capital requirement for duration-based equity risk sub-module | 0 |
| R0410 | Total amount of Notional Solvency Capital Requirements for remaining part | 211,419 |
| R0420 | Total amount of Notional Solvency Capital Requirements for ring fenced funds | 2,301 |
| R0430 | Total amount of Notional Solvency Capital Requirements for matching adjustment portfolios | 0 |
| R0440 | Diversification effects due to RFF nSCR aggregation for article 304 | 0 |
| R0470 | Minimum consolidated group solvency capital requirement | 53,430 |
| | **Information on other entities** | |
| R0500 | Capital requirement for other financial sectors (Non-insurance capital requirements) | 0 |
| R0510 | *Credit institutions, investment firms and financial institutions, alternative investment funds managers, UCITS management companies* | 0 |
| R0520 | *Institutions for occupational retirement provisions* | 0 |
| R0530 | *Capital requirement for non- regulated entities carrying out financial activities* | 0 |
| R0540 | Capital requirement for non-controlled participation requirements | 0 |
| R0550 | Capital requirement for residual undertakings | 0 |
| | **Overall SCR** | |
| R0560 | SCR for undertakings included via D&A | 0 |
| R0570 | Solvency capital requirement | 213,720 |

USP Key

For life underwriting risk:
1 - Increase in the amount of annuity benefits
9 - None

For health underwriting risk:
1 - Increase in the amount of annuity benefits
2 - Standard deviation for NSLT health premium risk
3 - Standard deviation for NSLT health gross premium risk
4 - Adjustment factor for non-proportional reinsurance
5 - Standard deviation for NSLT health reserve risk
9 - None

For non-life underwriting risk:
4 - Adjustment factor for non-proportional reinsurance
6 - Standard deviation for non-life premium risk
7 - Standard deviation for non-life gross premium risk
8 - Standard deviation for non-life reserve risk
9 - None

S.32.01.22

Undertakings in the scope of the group

| Row | Country | Identification code of the undertaking | Type of code of the ID of the undertaking | Legal Name of the undertaking | Type of undertaking | Legal form | Category (mutual/non mutual) | Supervisory Authority |
|---|---|---|---|---|---|---|---|---|
| | C0010 | C0020 | C0030 | C0040 | C0050 | C0060 | C0070 | C0080 |
| 1 | GB | 213800LBGGLJPIBQ4P08 | LEI | SLF of Canada UK Limited | Insurance holding company as defined in Article 212(1) (f) of Directive 2009/138/EC | Company limited by shares or by guarantee or unlimited | Non-mutual | |
| 2 | GB | 549300NZ227BVL5W4E72 | LEI | Sun Life Assurance Company of Canada (U.K.) Limi | Life insurance undertaking | Company limited by shares or by guarantee or unlimited | Non-mutual | Prudential Regulation Authority |
| 3 | GB | 2939726 | Specific code | Sun Life of Canada UK Holdings Limited | Insurance holding company as defined in Article 212(1) (f) of Directive 2009/138/EC | Company limited by shares or by guarantee or unlimited | Non-mutual | |
| 4 | GB | 6997417 | Specific code | SLFC Services Company (UK) Limited | Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35 | Company limited by shares or by guarantee or unlimited | Non-mutual | |
| 5 | GB | 600319 | Specific code | Barnwood Properties Limited | Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35 | Company limited by shares or by guarantee or unlimited | Non-mutual | |
| 6 | GB | 2306074 | Specific code | Laurtrust Limited | Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35 | Company limited by shares or by guarantee or unlimited | Non-mutual | |

S.32.01.22

Undertakings in the scope of the group

| | | | | Criteria of influence | | | | | | Inclusion in the scope of Group supervision | | Group solvency calculation |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Country | Identification code of the undertaking | Type of code of the ID of the undertaking | % capital share | % used for the establishment of consolidated accounts | % voting rights | Other criteria | Level of influence | Proportional share used for group solvency calculation | YES/NO | Date of decision if art. 214 is applied | Method used and under method 1, treatment of the undertaking |
| Row | C0010 | C0020 | C0030 | C0180 | C0190 | C0200 | C0210 | C0220 | C0230 | C0240 | C0250 | C0260 |
| 1 | GB | 213800LBGGLJPIBQ4P08 | LEI | | | | | | | Included in the scope | | Method 1: Full consolidation |
| 2 | GB | 549300NZ227BVL5W4E72 | LEI | 100.00% | 100.00% | 100.00% | Centralised managen | Dominant | 100.00% | Included in the scope | | Method 1: Full consolidation |
| 3 | GB | 2939726 | Specific code | 100.00% | 100.00% | 100.00% | Centralised managen | Dominant | 100.00% | Included in the scope | | Method 1: Full consolidation |
| 4 | GB | 6997417 | Specific code | 100.00% | 100.00% | 100.00% | Centralised managen | Dominant | 100.00% | Included in the scope | | Method 1: Full consolidation |
| 5 | GB | 600319 | Specific code | 100.00% | 100.00% | 100.00% | Centralised managen | Dominant | 100.00% | Included in the scope | | Method 1: Full consolidation |
| 6 | GB | 2306074 | Specific code | 100.00% | 100.00% | 100.00% | Centralised managen | Dominant | 100.00% | Included in the scope | | Method 1: Full consolidation |