

# ***FM Insurance Company Limited***

## ***Consolidated financial statements for the year ended 31 December 2016***

*Registered number: 0755780*



*Regulated by the Prudential Regulation Authority  
Registered address: 1 Windsor Dials, Windsor, SL4 1RS, Berkshire*

***FM Insurance Company Limited***

***Consolidated financial statements  
for the year ended 31 December 2016***

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## ***FM Insurance Company Limited***

Registered number: 755780

### ***Strategic report for the year ended 31 December 2016***

The directors present their Strategic report of FM Insurance Company Limited (the "Company") and its subsidiaries (the "Group") for the year ended 31 December 2016.

#### **Review of the business**

Gross premiums written increased to £606,158,000 from £565,709,000 (7.2%) during the year. The net loss ratio decreased to 53.3% (2015: 75.6%) and the expense ratio was 4.7% (2015: 25.0%) including a foreign exchange gain of £75,580,000 (2015: gain of £32,974,000). Realised and unrealised gains on investments amounted to £35,908,000 (2015: £18,801,000 loss) as a result of the general movements in the stock markets.

The profit for the year and other movements described in the consolidated statement of comprehensive income resulted in an overall increase in shareholder's funds of £74,726,000 resulting in total shareholder's funds of £582,405,000 as at 31 December 2016.

As part of a global restructure the New Zealand insurance business transferred to a Factory Mutual Insurance Company branch on 1 January 2016, on a renewal basis.

The current ratings of the Group are AA (Very Strong) from Fitch Ratings, A+ (Superior) from A.M. Best and A+ (Strong) from Standard & Poor's.

#### **Principal risks and uncertainties**

Key management recognise the critical importance of having efficient and effective risk management systems in place. Risk management is deeply embedded within the corporate culture of the FM Global group of which the Company is an integral part.

The Company has established a risk management function with clear terms of reference from the board of directors and the board committees. The risk management function is overseen by a Risk Management Committee which is a board committee made up of senior management from across the business. The Risk Management Committee oversees all areas of risk management, with the main aim of optimising the structure and sources of capital to support its policyholders, maintain its strong ratings and ensure regulatory compliance.

The Company's approach to managing capital involves managing assets, liabilities and risks in a coordinated way, and taking appropriate action to maintain the capital position of the Company in the light of changes in economic conditions and risk characteristics.

Principal risks identified by the Company are insurance risk, credit risk and regulatory risk. These are covered in detail in note 24 to the financial statements.

#### **Future developments**

The Group anticipate that during the last quarter of 2017 the EU business in mainland Europe will start to transition to a newly formed European subsidiary of the Group's parent, Factory Mutual Insurance Company, on a renewals basis. The transition, together with market conditions, will reduce the premiums from 2016 levels. The Group's exposure to the Eurozone is limited to Euro currency holdings as the Group does not hold any Euro denominated debt securities. Furthermore it is the Group's policy to convert excess currency into US Dollars, the functional currency of the parent company.

#### **On behalf of the board**



**Rachel Cope**  
Finance Director

## ***FM Insurance Company Limited***

*Registered number: 755780*

### ***Directors' report for the year ended 31 December 2016***

The directors present their annual financial statements for the year ended 31 December 2016.

#### **Results and dividends**

The results of the operations of the Group for the financial year are set out on pages 7 and 8 and the financial position of the Group at the end of the financial year is set out on pages 9 and 10. The cash flow of the Group for the financial year is set out on page 14.

The directors do not recommend the payment of a dividend for the year ended 31 December 2016 (2015: £Nil).

The profit for the year retained in the Group is £87,453,000 (2015: £7,922,000 loss).

#### **Principal activities**

The Group's principal activities during the year continued to be the underwriting of property insurance risks and the provision of related engineering and loss prevention services to large and medium sized clients of the UK and various international branches. The Group is incorporated in the United Kingdom and is wholly owned by, and places reinsurance with, Factory Mutual Insurance Company located in Johnston, Rhode Island, USA (the "Parent").

#### **Going concern**

The directors believe the Group is able to manage its business risks successfully in any economic environment. Furthermore, the directors have a high expectation that the Group has adequate resources to continue in existence for the foreseeable future. As such, they continue to adopt the going concern basis in preparing the annual financial statements.

#### **Directors and employees**

The directors who held office during the year and to the date of this report were as follows:

Vincent A. Reyda	Managing Director
Jeffrey Burchill	(Retired 15 December 2016)
Rachel Cope	
Jonathan W. Hall	
Omar F. Hameed	
Kevin S. Ingram	(Appointed 15 December 2016)
Christopher Johnson	
Thomas A. Lawson	
Natalie Spotswood	(Appointed 21 July 2016)
Thomas S. Keevil	
Kenneth Lever	
Peter C. Wilson	

No directors had any interest in the shares of the Company during the year.

Details of employees are set out in note 7 to the financial statements.

#### **Political contributions**

The Group made no political contributions during the year (2015: £Nil).

#### **Insurance of directors**

Insurance is maintained for the directors in respect of their duties as directors of the Group.

## ***FM Insurance Company Limited***

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### ***Directors' report for the year ended 31 December 2016 (continued)***

#### **Employee note**

The Group considers all employment applications equally on their merits, regardless of the applicant's sex, sexual orientation, religion or belief, marital status, age, race, ethnic origin or disability. It is the Group's policy to treat all employees fairly and consistently throughout their employment with us, regardless of their sex, sexual orientation, religion or belief, marital status, age, race, ethnic origin or disability, and the Group will favourably consider reasonable workplace adjustments and provide the necessary training in the event that an employee becomes disabled. Performance management and promotion processes focus on recognising achievement and potential and encourage personal and career development for all employees, regardless of sex, sexual orientation, religion or belief, marital status, age, race, ethnic origin or disability.

#### **Disclosure of information to the auditors**

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Having made enquiries of fellow directors and the Group's auditor, each director has taken all the steps that he/she is obliged to take as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information.

#### **Statement of directors' responsibilities**

The directors are responsible for preparing the Strategic report, Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with *United Kingdom Generally Accepted Accounting Practice* (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and the profit or loss of the Company for that period.

In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

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

#### **Re-appointment of auditors**

Pursuant to a shareholders' resolution the Company is not obliged to re-appoint its auditor annually and Ernst & Young LLP will therefore continue in office.

#### **On behalf of the board**



**Rachel Cope**  
**Finance Director**

## ***FM Insurance Company Limited***

*Registered number: 755780*

### ***INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDER OF FM INSURANCE COMPANY LIMITED***

We have audited the financial statements of FM Insurance Company Limited for the year ended 31 December 2016 which comprise the consolidated profit and loss account, consolidated statement of comprehensive income, consolidated balance sheet, company balance sheet, consolidated statement of changes in equity, consolidated statement of cash flows and the related notes 1 to 25. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Group's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Group's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Group and the Group's members as a body, for our audit work, for this report, or for the opinions we have formed.

#### **Respective responsibilities of directors and auditors**

As explained more fully in the statement of directors' responsibilities set out on page 4, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

#### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the consolidated financial statements to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### **Opinion on financial statements**

In our opinion the financial statements:

- Give a true and fair view of the state of the Group's and the Company's affairs as at 31 December 2016 and of the Group's result for the year then ended;
- Have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- Have been prepared in accordance with the requirements of the Companies Act 2006.

#### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion, based on the work undertaken in the course of the audit:

- The information given in the Strategic Report and Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- The Strategic Report and Directors' Report have been prepared in accordance with applicable legal requirements.

***FM Insurance Company Limited***

*Registered number: 755780*

***INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDER OF FM INSURANCE COMPANY LIMITED (continued)***

**Matters on which we are required to report by exception**

In light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have identified no material misstatements in the Strategic Report or Directors' Report.

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

*Ernst & Young LLP*

Ed Jervis (Senior statutory auditor)  
for and on behalf of Ernst & Young LLP, Statutory Auditor  
London

**21** March 2017

**FM Insurance Company Limited**  
Registered number: 755780

**Consolidated profit and loss account: technical account – general business  
for the year ended 31 December 2016**

	Notes	2016		2015	
		£000	£000	£000	£000
Gross written premium	2	606,158		565,709	
Outward reinsurance premium		(469,406)		(438,880)	
			136,752		126,829
Change in the gross provision for unearned premiums	15	1,754		19,640	
Change in the provision for unearned premiums, reinsurers' share	15	161		(16,909)	
			1,915		2,731
<b>Earned premiums, net of reinsurance</b>			138,667		129,560
Other technical income			7,875		6,651
Claims paid:	16				
Gross amount		(357,430)		(447,252)	
Reinsurers' share		260,642		347,058	
		(96,788)		(100,194)	
Change in the provision for claims:	16				
Gross amount		153,664		168,382	
Reinsurers' share		(130,849)		(166,105)	
		22,815		2,277	
<b>Claims incurred, net of reinsurance</b>			(73,973)		(97,917)
Net operating expenses	4		(14,332)		(38,995)
Change in equalisation provision	17		9,294		(2,946)
<b>Balance on the technical account - general business</b>			67,531		(3,647)



**FM Insurance Company Limited**

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**Consolidated profit and loss account: non-technical account  
for the year ended 31 December 2016**

	Notes	2016 £000	2015 £000
Balance on the technical account - general business		67,531	(3,647)
Other finance (charge)/ income	3	(2,181)	57
Profit on transfer of branches	3	1,196	-
Investment income	3	40,000	29,892
Unrealised gain/(loss) on investments	3	11,583	(32,440)
<b>Profit/(Loss) on ordinary activities before taxation</b>		<b>118,129</b>	<b>(6,138)</b>
Tax charge on ordinary activities	8	(30,676)	(1,784)
<b>Retained profit/(loss) for the financial year transferred to reserves</b>		<b>87,453</b>	<b>(7,922)</b>

The movements in the year are all in respect of continuing operations.

**Consolidated statement of comprehensive income  
for the year ended 31 December 2016**

	Notes	2016 £000	2015 (restated) £000
<b>Profit/(Loss) for the financial year</b>		<b>87,453</b>	<b>(7,922)</b>
Exchange differences on retranslation of net investments in foreign branches		22,570	(14,173)
Exchange differences on translating to the presentational currency		(2,964)	1,073
Remeasurement loss recognised on defined benefit pension schemes	20	(40,789)	(10,810)
Movement on deferred tax relating to pension scheme	8	8,456	550
<b>Total other comprehensive loss</b>		<b>(12,727)</b>	<b>(23,360)</b>
<b>Total comprehensive income/(loss) for the year</b>		<b>74,726</b>	<b>(31,282)</b>

**FM Insurance Company Limited**  
Registered number: 755780

**Consolidated balance sheet  
at 31 December 2016**

ASSETS	Notes	2016		2015 (restated)	
		£000	£000	£000	£000
<i>Investments</i>					
Financial investments	9	541,493		562,122	
			541,493		562,122
<i>Reinsurers' share of technical provisions</i>					
Provision for unearned premiums	15	186,931		156,646	
Claims outstanding	16	193,905		286,812	
			380,836		443,458
<i>Debtors</i>					
Debtors arising out of direct insurance operations		125,086		88,777	
Debtors arising out of reinsurance operations		43,223		51,294	
Other debtors:	12				
Amounts falling due within one year		8,874		32,596	
Amounts falling due after one year		60,147		33,171	
			237,330		205,838
<i>Other assets</i>					
Tangible fixed assets	11	6,464		7,266	
Cash and cash equivalents	21	235,799		110,913	
			242,263		118,179
<i>Prepayments and accrued income</i>					
Accrued interest and rent		2,654		2,249	
Deferred acquisition costs	13	2,596		2,037	
Other prepayments and accrued income		765		1,010	
			6,015		5,296
<i>Total assets</i>		1,407,937		1,334,893	

**FM Insurance Company Limited**  
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**Consolidated balance sheet  
at 31 December 2016**

EQUITY AND LIABILITIES	Notes	2016		2015 (restated)	
		£000	£000	£000	£000
<i>Capital and reserves</i>					
Called up share capital	14	355,000		355,000	
Share premium account		978		978	
Profit and loss account		226,427		151,701	
Shareholder's funds attributable to equity interests			582,405		507,679
<i>Technical provisions</i>					
Provision for unearned premium	15	250,173		208,375	
Claims outstanding	16	285,951		386,637	
Equalisation provision	17	-		9,294	
			536,124		604,306
<i>Creditors</i>					
Creditors arising out of direct insurance operations		137,491		146,311	
Other creditors including taxation and social security	18	33,930		15,197	
			171,421		161,508
<i>Accruals and deferred income</i>	19		31,495		24,136
<i>Net pension liability</i>	20		86,492		37,264
<i>Total equity and liabilities</i>			1,407,937		1,334,893

These financial statements were approved by the board of directors on 16 March 2017 and were signed on its behalf by:



**Rachel Cope**  
Finance Director

**FM Insurance Company Limited**

Registered number: 755780

**Company balance sheet  
at 31 December 2016**

ASSETS	Notes	2016		2015 (restated)	
		£000	£000	£000	£000
<i>Investments</i>					
Financial investments	9	541,493		562,122	
Investment in subsidiary undertakings	10	<u>50</u>		<u>50</u>	
			541,543		562,172
<i>Reinsurers' share of technical provision</i>					
Provision for unearned premiums	15	186,931		156,646	
Claims outstanding	16	<u>193,905</u>		<u>286,812</u>	
			380,836		443,458
<i>Debtors</i>					
Debtors arising out of direct insurance operations		125,086		88,777	
Debtors arising out of reinsurance operations		43,223		51,294	
Other debtors:	12				
Amounts falling due within one year		7,820		30,617	
Amounts falling due after one year		<u>60,109</u>		<u>33,123</u>	
			236,238		203,811
<i>Other assets</i>					
Tangible fixed assets	11	6,391		7,193	
Cash and cash equivalents		<u>234,656</u>		<u>110,398</u>	
			241,047		117,591
<i>Prepayments and accrued income</i>					
Accrued interest and rent		2,656		2,247	
Deferred acquisition costs	13	2,596		2,037	
Other prepayments and accrued income		<u>755</u>		<u>1,010</u>	
			6,007		5,294
<i>Total assets</i>		<u>1,405,671</u>		<u>1,332,326</u>	

**FM Insurance Company Limited**  
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**Company balance sheet  
at 31 December 2016**

EQUITY AND LIABILITIES	Notes	2016		2015 (restated)	
		£000	£000	£000	£000
<b>Capital and reserves</b>					
Called up share capital	14	355,000		355,000	
Share premium account		978		978	
Profit and loss account		<u>222,887</u>		<u>148,052</u>	
Shareholder's funds attributable to equity interests			578,865		504,030
<b>Technical provisions</b>					
Provision for unearned premium	15	250,173		208,375	
Claims outstanding	16	285,951		386,637	
Equalisation provision	17	<u>-</u>		<u>9,294</u>	
			536,124		604,306
<b>Creditors</b>					
Creditors arising out of direct insurance operations		137,491		146,311	
Other creditors including taxation and social security	18	<u>35,665</u>		<u>16,578</u>	
			173,156		162,889
<b>Accruals and deferred income</b>	19		31,034		23,837
<b>Net pension liability</b>	20		86,492		37,264
<b>Total equity and liabilities</b>			<u><u>1,405,671</u></u>		<u><u>1,332,326</u></u>

These financial statements were approved by the board of directors on 16 March 2017 and were signed on its behalf by:



**Rachel Cope**  
Finance Director

**FM Insurance Company Limited**  
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**Consolidated statement of changes in equity  
for the year ended 31 December 2016**

	2016			
	Called up share capital	Share premium account	Profit and loss account	Total
	£000	£000	£000	£000
<b>At 1 January</b>	<b>355,000</b>	<b>978</b>	<b>151,701</b>	<b>507,679</b>
Total comprehensive income for the year	-	-	74,726	74,726
<b>Total changes in equity</b>	<b>-</b>	<b>-</b>	<b>74,726</b>	<b>74,726</b>
<b>At 31 December</b>	<b>355,000</b>	<b>978</b>	<b>226,427</b>	<b>582,405</b>

	2015 (restated)			
	Called up share capital	Share premium account	Profit and loss account	Total
	£000	£000	£000	£000
<b>At 1 January</b>	<b>355,000</b>	<b>978</b>	<b>182,983</b>	<b>538,961</b>
Total comprehensive loss for the year	-	-	(31,282)	(31,282)
<b>Total changes in equity</b>	<b>-</b>	<b>-</b>	<b>(31,282)</b>	<b>(31,282)</b>
<b>At 31 December</b>	<b>355,000</b>	<b>978</b>	<b>151,701</b>	<b>507,679</b>

**FM Insurance Company Limited**  
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**Consolidated statement of cash flows  
for the year ended 31 December 2016**

	Notes	2016 £000	2015 (restated) £000
<b>Profit/(Loss) on ordinary activities before taxation</b>		<b>118,129</b>	<b>(6,138)</b>
Depreciation of tangible fixed assets	11	1,378	1,139
Movement in technical provisions		(5,560)	(13,266)
Difference between current service cost and pension contributions	20	4,243	33,243
Investment (return)/loss	3	(50,598)	2,491
Movement in other assets/liabilities	21	(121,986)	(200,784)
Corporation tax paid		(15,146)	(6,604)
<b>Net cash outflow from operating activities</b>		<b>(69,540)</b>	<b>(189,919)</b>
<b>Investing activities</b>			
Payments to acquire tangible fixed assets	11	(195)	(3,989)
Disposal proceeds from insurance branches		1,196	-
Investment income received		15,600	16,989
Purchase of portfolio investments		(14,263)	(98,643)
Disposal of portfolio investments		169,939	155,619
<b>Net inflow from investing activities</b>		<b>172,277</b>	<b>69,976</b>
Increase/(decrease) in cash and cash equivalents		102,737	(119,943)
Cash and cash equivalents at beginning of period		110,913	229,438
Exchange differences on opening cash		22,149	1,418
<b>Cash and cash equivalents at 31 December</b>		<b>235,799</b>	<b>110,913</b>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **1. Accounting policies**

##### **1.1 Statement of compliance**

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

##### **1.2 Basis of preparation**

The consolidated financial statements were approved for issue by the Board of Directors on 16 March 2017.

The consolidated financial statements are prepared in British Pound Sterling which is the presentation currency of the Group and rounded to the nearest £'000.

As permitted by FRS 103 the Group continues to apply the existing accounting policies that were applied prior to this standard for its insurance contracts.

The Group has taken advantage of the exemption under FRS 102 Section 33 Related Party Disclosures not to disclose transactions with companies in the Factory Mutual Insurance Company (FMIC) group as it is a wholly owned subsidiary of FMIC which publishes consolidated financial statements.

##### **1.3 Basis of consolidation**

The Group financial statements consolidate the financial statements of FM Insurance Company Limited and its subsidiary undertaking drawn up to 31 December each year.

No profit and loss account is presented for the Company as permitted by section 408 of the Companies Act 2006.

In the Company financial statements investments in subsidiaries are accounted for at cost less impairment.

##### **1.4 Judgements and key sources of estimation uncertainty**

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities as at the balance sheet date and the amounts reported as revenues and expenses during the year. However, the nature of estimation means that actual outcomes could differ from those estimates. The following represent the key sources of estimation and judgement:

###### ***Insurance contract technical provisions***

For insurance contracts, estimates are made both for the expected ultimate cost of claims reported at the reporting date and for the expected ultimate cost of claims incurred, but not yet reported, at the reporting date.

The provision for claims outstanding is based on information available at the balance sheet date. Delays can be experienced in the notification and settlement of certain claims. Accordingly, the ultimate cost of such claims cannot be known with certainty at the balance sheet date. Subsequent information and events may result in the ultimate liability being different than the amount provided. Any differences between provisions and subsequent settlements are dealt with in the technical account – general business of later years.

Further details are given in note 24.



## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **1. Accounting policies (continued)**

##### **1.4 Judgements and key sources of estimation uncertainty (continued)**

###### ***Defined benefit pension benefits***

The cost of defined benefit pension plans are determined using actuarial valuations. The actuarial valuation involves making assumptions about discount rates, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and the long term nature of these plans, such estimates are subject to significant uncertainty.

Further details are given in note 20.

##### **1.5 Significant accounting policies**

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Group's financial statements.

###### ***Premiums***

Written premiums, gross of commission, comprise the premiums receivable for the period of cover provided by contracts incepting during the financial year, and are stated before commissions, taxes and duties levied on premiums.

Premiums written are accounted for in the year in which the risk incepts and include adjustments to premiums written in prior accounting periods and estimates for binder premiums. Outward reinsurance premiums are accounted for in the same accounting period as the premiums for the related inwards direct insurance business.

###### ***Acquisition costs***

Acquisition costs comprise the expenses, both direct and indirect, of acquiring insurance and reinsurance policies incepting during the financial year. Acquisition costs which relate to a subsequent financial year are deferred and charged to the accounting periods in which the related premiums are earned.

Deferred acquisition costs represent the proportion of acquisition costs incurred which corresponds to the proportion of gross premiums written which are unearned at the balance sheet date.

###### ***Technical provisions***

Technical provisions comprise claims outstanding, provisions for unearned premiums and provision for unexpired risk, when required.

###### ***Claims outstanding***

Outstanding claims comprise provisions for the estimated costs of settling all claims incurred up to but not paid at the balance sheet date whether reported or not, together with related claims handling expenses. Claims incurred includes all claims payments made in respect of the financial period, claims handling expenses and the movement in provision for outstanding claims and claims handling expenses.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **1. Accounting policies (continued)**

##### **1.5 Significant accounting policies (continued)**

###### ***Unearned premiums***

The provision for unearned premiums comprises the amount representing that part of gross premiums written which is estimated to be earned in the following or subsequent financial years, computed separately for each insurance contract using the daily pro rata method. The proportion attributable to subsequent periods are deferred as a provision for unearned premiums.

The provision for reinsurers' share of unearned premiums comprises the amount representing the part of reinsurers' share of written premiums which is estimated to be earned in the following or subsequent financial years. Unearned reinsurance premiums are deferred over the term of the underlying direct insurance policies for both risks-attaching contracts and losses-occurring contracts.

###### ***Unexpired risk provision***

Provision for unexpired risks is made when the estimated costs of future claims and related deferred acquisition costs are expected to exceed the unearned premium provision. In determining the need for an unexpired risk provision the different classes of business have been regarded as business that is managed together. Based on information available at the balance sheet date, before taking into account investment income but including previous claims experience, the Group has assessed that no provision is required.

###### ***Reinsurance***

In the normal course of business the Group seeks to reduce losses that may arise from catastrophes or other events that cause unfavourable underwriting results by reinsuring certain levels of risk with other insurance enterprises. Amounts recoverable from reinsurers are accounted for in a manner consistent with the underlying contract liabilities, outstanding claims provisions or settled claims associated with the reinsured policies and in accordance with the relevant reinsurance contract.

###### ***Financial instruments***

The Group measures its financial instruments in line with Sections 11 and 12 of FRS 102.

###### ***Financial investments***

Financial investments comprise exchange traded equity instruments and high grade debt securities. Such assets are initially measured at fair value and subsequent changes in fair value are recognised in the profit and loss account.

The Group has designated its debt securities at fair value through the profit and loss account to enable the short term gains and losses to be matched against the short-tail nature of the Company's insurance liabilities. Furthermore debt securities are managed on a fair value basis, alongside equity investments held by the Group within the overall investment portfolio, and reported on that basis to the Company's board of directors.

Realised gains or losses represent the difference between net sales proceeds and book value. Unrealised gains and losses represent the difference between the valuation of investments at the balance sheet date and their purchase price. All realised and unrealised gains and losses are taken to the non-technical account in the profit and loss account.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **1. Accounting policies (continued)**

##### **1.5 Significant accounting policies (continued)**

###### ***Cash and cash equivalents***

Cash and cash equivalents in the balance sheet comprise cash at bank and in hand and short term deposits with an original maturity date of three months or less.

###### ***Short-term debtors and creditors***

Debtors and creditors receivable or payable within one year are recorded at transaction price. Due to the short term nature of the balances they are held at an undiscounted amount rather than subsequently re-measured at amortised cost using the effective interest rate method.

Any losses arising from impairment are recognised in the profit and loss account in other operating expenses.

###### ***Investment income***

Investment income comprises of dividends and interest, together with realised and unrealised gains and losses on the investment portfolio. Dividend income is recognised when the right to receive payment is established. Interest income is accounted for on an accruals basis. Realised and unrealised gains and losses are referenced within other financial investments.

###### ***Tangible fixed assets***

Depreciation is provided by the Group to write off the cost less the estimated residual value of tangible fixed assets by instalments over their estimated useful economic lives as follows:

Office equipment	20% of cost per annum
Office furniture	10% of cost per annum
Computer equipment	33.3% or 50% of cost per annum
Leasehold improvements	Over the life of the lease

The carrying values of tangible fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

###### ***Leases***

Rentals payable under operating leases are charged in the profit and loss account on a straight line basis over the lease term. Lease incentives are recognised over the lease term on a straight line basis.

###### ***Foreign currencies***

Each branch within the Group determines its own functional currency. Transactions in foreign currencies are initially recorded in the functional currency of the branch by applying the spot exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at exchange rates ruling at the balance sheet date. Non-monetary assets are converted at historical rates. Exchange differences arising from transactions are taken to the profit and loss account.

The assets and liabilities of the branches are translated into the presentational currency at the rate of exchange ruling at the balance sheet date. Income and expenses for each statement of comprehensive income are translated at average rates. All resulting exchange differences are recognised in other comprehensive income.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **1. Accounting policies (continued)**

##### **1.5 Significant accounting policies (continued)**

###### ***Provisions***

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation.

###### ***Pensions***

The Group operates a number of defined benefit pension schemes. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and are discounted at the current rate of return of a high quality corporate bond of equivalent term and currency to the liabilities.

The increase in the present value of the liabilities of the Group's defined benefit pension schemes expected to arise from employee service in the period is charged to the profit and loss account. The net interest element is determined by multiplying the net defined benefit asset or liability by the discount rate at the start of the period, taking into account any changes in the net defined benefit asset or liability during the period as a result of contribution and benefit payments. The net interest is recognised in profit or loss as other finance revenue or cost.

Re-measurement, comprising actuarial gains and losses, the effect of the asset ceiling and the return on the net defined benefit asset or liability (excluding amounts included in net interest) are recognised immediately in other comprehensive income in the period in which they occur. Re-measurements are not reclassified to profit or loss in subsequent periods.

The German pension scheme is covered by an insurance contract, which is designed to meet the pension obligations, but does not meet the technical criteria to be considered a pension plan asset. The value of this insurance contract is recorded in the balance sheet as a company asset in other debtors. The insurance contract is valued at the accumulated benefit obligation for the German pension scheme and does not take into account future changes to salaries and service levels. The amount due to the company under the contract in the next twelve months is classified as current and the amount falling due after twelve months is classified as non-current.

Any pension scheme surplus, to the extent it is considered recoverable, or deficit, is recognised in full and presented on the balance sheet.

The Group also operates a number of defined contribution schemes. Contributions to defined contribution schemes are recognised in the profit and loss account in the period in which they become payable.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **1. Accounting policies (continued)**

##### **1.5 Significant accounting policies (continued)**

###### ***Taxation***

Current tax liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date. To the extent that losses of an individual UK company are not offset in any one year, they can be carried back for one year or carried forward indefinitely to be offset against profits arising from the same company.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed by the balance sheet date. Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

The Parent's UK subsidiaries each file separate tax returns. In accordance with UK tax legislation, where one domestic UK company is a 75 per cent owned subsidiary of another UK company or both are 75 per cent owned subsidiaries of a common parent, the companies are considered to be within the same UK tax group. For companies within the same tax group, trading profits and losses arising in the same accounting period may be offset for the purposes of determining current and deferred taxes.

##### **1.6 Prior year restatement**

Germany's pension obligations are covered by an insurance contract with a third party, for which premiums are paid annually. In 2015, the insurance asset was recorded at the same value as the pension obligation liability and the two were offset and reported as a net nil liability. During the year, the company amended the German pension scheme to include a final year bonus amount in addition to the final salary. As part of the review of this amendment, it was identified that this insurance contract had previously been accounted for incorrectly.

The company recognises the projected benefit obligation as the pension liability, however the insurance contract covers the accumulated benefit obligation covered by premiums paid up to 31 December 2016 and does not take into account future changes to salaries and service levels. The insurance contract is designed to meet the pension obligations, but does not meet the technical criteria to be considered a pension plan asset and therefore recorded in the balance sheet as a company asset in other debtors. The insurance contract is measured at the fair value of the accumulated benefit obligation.

The 2015 comparatives have been restated to reflect the difference between the projected benefit obligation and the value of the insurance asset, and also to reflect the treatment of the insurance debtor as a company asset and not a pension asset, as reported in the prior year – the impact of this restatement is as follows:

	Previously Reported £000	Restated £000	Impact £000
Pension asset	37,352	-	(37,352)
Pension liability	(37,352)	(37,352)	-
Net pension asset/(liability)	-	(37,352)	(37,352)
Other debtors	-	29,650	29,650
Remeasurement loss recognised on defined benefit pension schemes	-	(7,702)	(7,702)

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **2. Analysis by class of business**

Analysis of gross premiums written, gross premiums earned, gross claims incurred, gross operating expenses, reinsurance balance and the technical provisions:

	2016						
	Gross premiums written	Gross premiums earned	Gross claims incurred	Gross operating expenses	Reinsurance balance	Total	Net assets
	£000	£000	£000	£000	£000	£000	£000
Marine, Aviation and Transport	3,262	3,436	(3,338)	(330)	1,094	862	3,134
Fire and Other	561,931	560,587	(169,253)	(56,908)	(285,656)	48,770	539,911
Assumed	40,965	43,889	(31,175)	(4,149)	(7,835)	730	39,360
Total	<u>606,158</u>	<u>607,912</u>	<u>(203,766)</u>	<u>(61,387)</u>	<u>(292,397)</u>	<u>50,362</u>	<u>582,405</u>

	2015 (restated)						
	Gross premiums written	Gross premiums earned	Gross claims incurred	Gross operating expenses	Reinsurance balance	Total	Net assets
	£000	£000	£000	£000	£000	£000	£000
Marine, Aviation and Transport	5,671	4,217	(7,925)	(893)	1,319	(3,282)	5,089
Fire and Other	518,158	513,175	(270,806)	(81,679)	(176,866)	(16,176)	465,006
Assumed	41,880	67,957	(139)	(6,600)	(49,112)	12,106	37,584
Total	<u>565,709</u>	<u>585,349</u>	<u>(278,870)</u>	<u>(89,172)</u>	<u>(224,659)</u>	<u>(7,352)</u>	<u>507,679</u>

	2016		
	Direct £000	Assumed £000	Total £000
Resulting from contracts concluded:			
In the EU member state of its head office	321,878	24,225	346,103
In the other EU member states	228,444	16,779	245,223
In other countries	14,871	(39)	14,832
Total	<u>565,193</u>	<u>40,965</u>	<u>606,158</u>

	2015		
	Direct £000	Assumed £000	Total £000
Resulting from contracts concluded:			
In the EU member state of its head office	327,490	27,820	355,310
In the other EU member states	174,616	14,509	189,125
In other countries	21,723	(449)	21,274
Total	<u>523,829</u>	<u>41,880</u>	<u>565,709</u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **3. Investment return and charges**

	2016 £000	2015 £000
Net (charge)/return on defined benefit pension scheme	(2,181)	57
Net income from investments	14,882	15,321
Net interest received from bank accounts and fixed deposits	793	932
Profit on transfer of branches	1,196	-
Realised gain on investments	24,325	13,639
Investment income	39,015	29,949
Unrealised gain/(loss) on investments	11,583	(32,440)
<b>Total investment return/(loss)</b>	<b>50,598</b>	<b>(2,491)</b>

#### **4. Net operating expenses**

	2016 £000	2015 £000
Acquisition costs	16,013	15,715
Change in gross deferred acquisition costs	534	626
	16,547	16,341
Administrative expenses	44,838	72,831
Gross operating expenses	61,385	89,172
Reinsurance commissions	(46,393)	(47,694)
Change in deferred reinsurance commission	(660)	(2,483)
	14,332	38,995

Included within administrative expenses are:

	2016 £000	2015 £000
Gain on foreign exchange	(75,580)	(32,974)
Depreciation of tangible fixed assets	1,378	1,139
Operating lease rentals - buildings	6,500	6,468
Operating lease rentals - other	2,366	2,418
Auditors' remuneration (see note 5)	614	495

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **5. Auditors' remuneration**

The remuneration of the auditors is further analysed as follows:

	2016 £000	2015 £000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	232	244
The audit of the Company's subsidiaries and branches	184	191
Fees pursuant to legislation	128	60
<i>Fees payable to the Company's auditor and its associates for other services:</i>		
Audit – related assurance services	70	-
	<u>614</u>	<u>495</u>

#### **6. Remuneration of directors**

	2016 £000	2015 £000
Aggregate remuneration in respect of qualifying services	1,289	1,280
Aggregate amounts receivable under long term incentive plans	265	666
	<u>1,554</u>	<u>1,946</u>

The aggregate of remuneration and amounts receivable under long term incentive schemes of the highest paid director was £1,210,000 (2015: £1,187,000). This includes amounts receivable under long term incentives of £265,000 (2015: £666,000).

	2016	2015
Retirement benefits are accruing to the following number of directors under defined benefit schemes.	2	1

#### **7. Staff numbers and costs**

The average number of employees of the Group during the year ended 31 December 2016 were as follows:

	2016	2015
Engineering	388	382
Administration & Professional	285	292
Operations	128	141
Underwriting	76	70
	<u>877</u>	<u>885</u>



# ***FM Insurance Company Limited***

## ***Notes to the consolidated financial statements for the year ended 31 December 2016***

### **7. Staff numbers and costs (continued)**

Staff costs consist of:

	2016 £000	2015 £000
Wages and salaries	66,795	57,961
Social security costs	12,588	10,502
Other pension costs	19,195	11,290
	<u>98,578</u>	<u>79,753</u>

Included in other pension costs are £15,980,000 (2015: £8,970,000) in respect of the defined benefit schemes and £3,215,000 (2015: £2,320,000) in respect of the defined contribution pension schemes.

### **8. Tax charge/(credit) on ordinary activities**

#### **(a) Tax on ordinary activities**

The charge to taxation is made up as follows:

	2016 £000	2015 £000
<b>Current Tax :</b>		
UK corporation tax on profits of the period	21,221	12
Overseas relief	(7,510)	(12)
Foreign tax	10,088	2,377
Withholding tax	1,831	2,611
	<u>25,630</u>	<u>4,988</u>
Adjustment in respect of foreign exchange	(64)	22
Adjustment in respect of prior periods	4,454	(435)
Total current tax	<u>30,020</u>	<u>4,575</u>
<b>Deferred Tax:</b>		
Decelerated capital allowances	42	(271)
Timing difference in respect of pension	(1,261)	(684)
Adjustment in respect of prior year	592	(4)
Adjustment in respect of rate change	(309)	(65)
Trading gain/(losses)	1,694	(2,206)
Other timing differences	(102)	439
Total deferred tax	<u>656</u>	<u>(2,791)</u>
Taxation charge on ordinary activities	<u>30,676</u>	<u>1,784</u>

# ***FM Insurance Company Limited***

## ***Notes to the consolidated financial statements for the year ended 31 December 2016***

### **8. Tax charge/(credit) on ordinary activities (continued)**

#### **(b) Tax included in the statement of comprehensive income**

	2016 £000	2015 £000
Deferred tax on actuarial gain	(9,091)	(622)
Effect of rate change	635	72
Total tax credit	<u>(8,456)</u>	<u>(550)</u>

#### **(c) Factors affecting tax charge for the period**

The tax assessed for the year is higher than the standard rate of corporation tax in the UK of 20% (2015 20.25%). The differences are reconciled below:

	2016 £000	2015 £000
Profit/(Loss) on ordinary activities before tax	<u>118,129</u>	<u>(6,138)</u>
Profit/ (Loss) on ordinary activities multiplied by the rate of corporation tax in the UK, applicable for 2016 of 20% (2015: 20.25%)	23,626	(1,243)
Effects of :		
Withholding tax not relieved	1,831	2,611
Prior year losses utilised	(1,882)	-
Foreign tax suffered	10,088	2,377
Expenses not deductible for tax purposes	(1,999)	(1,882)
Losses group relieved	-	385
Adjustments in respect of Rate Change	(309)	(65)
Other timing differences	1,849	30
Foreign exchange	(64)	22
Adjustment in respect of prior year	5,046	(439)
Double tax relief credited	(7,510)	(12)
Total tax charge for the period	<u>30,676</u>	<u>1,784</u>

#### **(d) Deferred tax**

##### **Consolidated**

	2016 £000	2015 £000
Deferred tax asset at the start of the year	3,857	516
Deferred tax credit/(charge) to the profit and loss	(656)	2,791
Deferred tax credit to other comprehensive income	8,456	550
Deferred tax asset at the end of the year	<u>11,657</u>	<u>3,857</u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **8. Tax charge/(credit) on ordinary activities (continued)**

Deferred tax asset at the end of the year is made up of:

	2016 £000	2015 £000
Excess depreciation over capital allowances	963	1,145
Deferred tax on pension movements	10,295	(64)
Other timing differences	399	2,776
Deferred tax asset at the end of the year	<u>11,657</u>	<u>3,857</u>

#### **Company**

	2016 £000	2015 £000
Deferred tax asset at the start of the year	3,809	460
Deferred tax (charge)/credit to the profit and loss	(646)	2,799
Deferred tax credit to other comprehensive income	8,456	550
Deferred tax asset at the end of the year	<u>11,619</u>	<u>3,809</u>

Deferred tax asset at the end of the year is made up of:

	2016 £000	2015 £000
Excess depreciation over capital allowances	936	1,099
Deferred tax on pension movements	10,295	(64)
Other timing differences	388	2,774
Deferred tax asset at the end of the year	<u>11,619</u>	<u>3,809</u>

Deferred tax has been calculated at 18.0% (2015: 20.0%).

#### **Factors that may affect future tax charges**

The Group earns income in many different countries and, on average, pays taxes at rates higher than the UK statutory rate. The overall impact of these higher taxes is subject to changes in enacted tax rates and the country mix of the Group's income.

With effect from the 1 April 2017 the rate for UK Corporation Tax will reduce from 20% to 19%, and will then reduce again to 17% with effect from 1 April 2020. Deferred tax has been provided for at 18% for the year. A blended rate is deemed appropriate because assets will unwind over several years resulting in tax relief occurring at different corporation tax rates.

None of these changes require the adjustment of disclosures in the current period. The impact of these changes is not expected to significantly affect either the current or deferred tax charges in the future.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **9. Consolidated and Company – Financial investments**

	2016		2015	
	Fair value £000	Cost £000	Fair value £000	Cost £000
Equity investments	404,732	343,932	423,029	373,583
Debt securities	136,761	136,884	139,093	139,469
	<u>541,493</u>	<u>480,816</u>	<u>562,122</u>	<u>513,052</u>

The following table shows financial investments recorded at fair value analysed between the three levels in the fair value hierarchy.

	Level 1 £000	Level 2 £000	Total £000
<b>31 December 2016</b>			
Equity investments	404,732	-	404,732
Debt securities	-	136,761	136,761
	<u>404,732</u>	<u>136,761</u>	<u>541,493</u>
	Level 1 £000	Level 2 £000	Total £000
<b>31 December 2015</b>			
Equity investments	423,029	-	423,029
Debt securities	-	139,093	139,093
	<u>423,029</u>	<u>139,093</u>	<u>562,122</u>

Included in the level 1 category are financial assets that are measured by reference to published quotes in an active market.

Included in the level 2 category are financial assets measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions. Debt securities are priced by an independent vendor using evaluated market pricing models.

Level 3 category financial assets are measured using a valuation technique (model) based on assumptions that are neither supported by prices from observable current market transactions in the same instrument nor are they based on available market data. The Company does not hold any level 3 financial investments.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **10. Company – Investment in subsidiary undertakings**

	2016	2015
	£000	£000
As at 31 December	<u>50</u>	<u>50</u>

Particulars of subsidiary undertakings (ordinary shares) included in these consolidated financial statements are as follows:

Subsidiary	Country of Incorporation	Percentage ownership	Nature of business
FM Engineering International Limited	UK	100%	Engineering Services

#### **11. Consolidated and Company – Tangible fixed assets**

	Consolidated 2016 Equipment furniture and computers £000	Company 2016 Equipment furniture and computers £000
<b>Cost</b>		
At beginning of year	20,180	19,824
Additions	195	185
Disposals	-	-
Exchange adjustments	1,616	1,555
At end of year	<u>21,991</u>	<u>21,564</u>
<b>Depreciation</b>		
At beginning of year	12,914	12,631
Charge for year	1,378	1,355
Disposals	-	-
Exchange adjustments	1,235	1,187
At end of year	<u>15,527</u>	<u>15,173</u>
<b>Net book value</b>		
At 31 December 2016	<u>6,464</u>	<u>6,391</u>
At 31 December 2015	<u>7,266</u>	<u>7,193</u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **12. Consolidated – Other debtors**

	2016 £000	2015 (restated) £000
<i>Amounts falling due within one year:</i>		
Corporation tax	2,209	6,754
Amounts owed by affiliated undertakings	781	649
Sundry debtors	<u>5,884</u>	<u>25,193</u>
	<u>8,874</u>	<u>32,596</u>
<i>Amounts falling due after one year:</i>		
Deferred tax (see note 8)	11,657	3,857
Sundry debtors	<u>48,490</u>	<u>29,314</u>
	<u>60,147</u>	<u>33,171</u>

#### **Company – Other debtors**

	2016 £000	2015 (restated) £000
<i>Amounts falling due within one year:</i>		
Corporation tax	2,199	6,719
Amounts owed by affiliated undertakings	811	728
Sundry debtors	<u>4,810</u>	<u>23,170</u>
	<u>7,820</u>	<u>30,617</u>
<i>Amounts falling due after one year:</i>		
Deferred tax (see note 8)	11,619	3,809
Sundry debtors	<u>48,490</u>	<u>29,314</u>
	<u>60,109</u>	<u>33,123</u>

Amounts due from group undertakings are unsecured, interest free, have no fixed date of repayments and are repayable on demand.

#### **13. Consolidated and Company – Deferred acquisition costs**

	2016 £000	2015 £000
At 1 January	2,037	3,137
Change in deferred acquisition costs	(534)	(626)
Foreign exchange	1,093	(474)
At 31 December	<u>2,596</u>	<u>2,037</u>

# ***FM Insurance Company Limited***

## ***Notes to the consolidated financial statements for the year ended 31 December 2016***

### **14. Consolidated and Company – Share capital**

	2016 £000	2015 £000
<i>Authorised</i>		
500,000,000 Ordinary shares of £1 each	<u>500,000</u>	<u>500,000</u>
<i>Allotted, called up and fully paid</i>		
355,000,000 Ordinary shares of £1 each	<u>355,000</u>	<u>355,000</u>

### **15. Consolidated and Company – Provision for unearned premiums**

	Gross £000	2016 Reinsurers' share £000	Net £000
At 1 January 2016	208,375	156,646	51,729
Premiums written in the year	606,158	469,406	136,752
Premiums earned in the year	(607,912)	(469,245)	(138,667)
Foreign exchange	43,552	30,124	13,428
At 31 December 2016	<u>250,173</u>	<u>186,931</u>	<u>63,242</u>
		2015	
	Gross £000	Reinsurers' share £000	Net £000
At 1 January 2015	234,738	179,789	54,949
Premiums written in the year	565,709	438,880	126,829
Premiums earned in the year	(585,349)	(455,789)	(129,560)
Foreign exchange	(6,723)	(6,234)	(489)
At 31 December 2015	<u>208,375</u>	<u>156,646</u>	<u>51,729</u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **16. Consolidated and Company – Claims outstanding**

	Gross £000	2016 Reinsurers' share £000	Net £000
At 1 January 2016	386,637	286,812	99,825
Claims incurred in current accident year	285,690	184,364	101,326
Claims incurred in prior accident years	(81,924)	(54,571)	(27,353)
Claims paid during the year	(357,430)	(260,642)	(96,788)
Foreign exchange	52,978	37,942	15,036
At 31 December 2016	<u>285,951</u>	<u>193,905</u>	<u>92,046</u>
	Gross £000	2015 Reinsurers' share £000	Net £000
At 1 January 2015	576,439	466,568	109,871
Claims incurred in current accident year	327,163	218,151	109,012
Claims incurred in prior accident years	(48,293)	(37,198)	(11,095)
Claims paid during the year	(447,252)	(347,058)	(100,194)
Foreign exchange	(21,420)	(13,651)	(7,769)
At 31 December 2015	<u>386,637</u>	<u>286,812</u>	<u>99,825</u>

#### **17. Consolidated and Company – Equalisation provision**

An equalisation provision has previously been recognised in accordance with the rules of the PRA handbook, and was required by Schedule 3 to the Regulations to be included within technical provisions. Solvency II has been implemented with effect from 1 January 2016 and there is no longer a requirement to hold an equalisation provision. It has therefore been released in the 2016 year.

The release of the equalisation provision during the year was £9,294,000 which has been taken to the technical account - general business and thereby increases the profit before tax.



## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **18. Consolidated – Other creditors including taxation and social security**

	2016	2015
	£000	£000
Corporation taxation payable	10,719	390
Social security	4,251	3,913
Engineering fee income	3,738	2,252
Amounts owed to affiliated undertakings	1,597	2,129
Other sundry creditors	13,625	6,513
	<u>33,930</u>	<u>15,197</u>

#### **Company – Other creditors including taxation and social security**

	2016	2015
	£000	£000
Corporation taxation payable	10,680	366
Social security	4,247	3,903
Engineering fee income	3,738	2,252
Amounts owed to affiliated undertakings	3,378	3,701
Other sundry creditors	13,622	6,356
	<u>35,665</u>	<u>16,578</u>

Amounts due to group undertakings are unsecured, interest free, have no fixed date of repayments and are repayable on demand.

#### **19. Consolidated – Accruals and deferred income**

	2016	2015
	£000	£000
Deferred reinsurance commissions	9,255	8,086
Salary and incentive accruals	15,561	11,897
Other accruals and deferred income	6,679	4,153
	<u>31,495</u>	<u>24,136</u>

#### **Company – Accruals and deferred income**

	2016	2015
	£000	£000
Deferred reinsurance commissions	9,255	8,086
Salary and incentive accruals	15,384	11,746
Other accruals and deferred income	6,395	4,005
	<u>31,034</u>	<u>23,837</u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **20. Pensions**

Substantially all of the employees are covered through either state-type schemes or schemes provided by the Group. Most of the employees not included in state-type schemes are covered through final salary defined benefit schemes in the UK and Germany.

The pension scheme assets for the UK are held in separate trustee administered funds to meet long-term pension liabilities to past and present employees. The defined benefit obligation arises wholly from funded plans.

Germany's obligations are covered by an insurance contract with a third party, for which premiums are paid annually. The insurance contract is designed to meet the pension obligations, but does not meet the technical criteria to be considered a pension plan asset and the recoverable amount is therefore recorded in the balance sheet as a company asset in other debtors. The company recognises the projected benefit obligation as the pension liability. The projected benefit obligation net of the value of the insurance contract is presented in the tables below as a net liability to illustrate the obligation not covered by the insurance contract.

During the year, the company amended the German pension scheme to include a final year bonus amount in addition to the final salary. The impact of this amendment was to increase the projected benefit obligation by £6,397,000, the cost of which has been charged to the profit and loss account in the year.

Full actuarial valuations were carried out by a qualified independent actuary on 1 January 2014 for UK, and 31 December 2015 for Germany. The disclosures required under FRS 102 'Employee Benefits' have been calculated based on the most recent full actuarial valuations updated to 31 December 2016 and are applicable to both the Group and the Company.

#### **Assets and liabilities of the defined benefit schemes**

The fair value of the scheme's assets, which are not intended to be recognised in the short term and may be subject to significant change before they are recognised, and the present value of the scheme's liabilities, which are derived from cash flow projections over long periods and thus inherently uncertain, were:

	UK	2016 Germany	Total
	£000	£000	£000
<b>Scheme assets at fair value</b>			
Equities	110,486	-	110,486
Bonds	46,052	-	46,052
Other – Cash	45,447	-	45,447
Fair value of scheme assets	201,985	-	201,985
Present value of scheme liabilities	(229,789)	(58,688)	(288,477)
<b>Net scheme liability</b>	<b>(27,804)</b>	<b>(58,688)</b>	<b>(86,492)</b>
Net pension liability in the balance sheet	(27,804)	(58,688)	(86,492)
Net insurance debtor in the balance sheet	-	46,944	46,944
<b>Net liability</b>	<b>(27,804)</b>	<b>(11,744)</b>	<b>(39,548)</b>

# FM Insurance Company Limited

## Notes to the consolidated financial statements for the year ended 31 December 2016

### 20. Pensions (continued)

	UK £000	2015 (restated) Germany £000	Total £000
Scheme assets at fair value			
Equities	111,335	-	111,335
Bonds	48,618	-	48,618
Other – Cash	2,107	-	2,107
Fair value of scheme assets	162,060	-	162,060
Present value of scheme liabilities	(161,972)	(37,352)	(199,324)
Net scheme asset/(liability)	88	(37,352)	(37,264)
Net pension liability in the balance sheet	88	(37,352)	(37,264)
Net insurance debtor in the balance sheet	-	29,650	29,650
Net liability	88	(7,702)	(7,614)

### Analysis of amounts recognised in the profit and loss account

	UK £000	2016 Germany £000	Total £000
Current service charge	7,595	2,063	9,658
Past service charge	-	6,397	6,397
Net interest (income)/cost on pension obligation	177	2,004	2,181
Amounts recognised in the profit and loss	7,772	10,464	18,236

	UK £000	2015 (restated) Germany £000	Total £000
Current service charge	7,260	2,084	9,344
Net interest income on pension obligation	(57)	-	(57)
Amounts recognised in the profit and loss	7,203	2,084	9,287

### Analysis of amounts recognised in the statement of comprehensive income

	UK £000	2016 Germany £000	Total £000
Return on plan assets less than the discount rate	(12,353)	-	(12,353)
Actuarial losses	56,359	4,412	60,771
Actuarial losses attributable to insurance contracts	-	(7,629)	(7,629)
Amounts recognised in other comprehensive income	44,006	(3,217)	40,789

# **FM Insurance Company Limited**

## **Notes to the consolidated financial statements for the year ended 31 December 2016**

### **20. Pensions (continued)**

#### **Analysis of amounts recognised in the statement of comprehensive income (continued)**

	UK £000	2015 (restated) Germany £000	Total £000
Return on plan assets greater than the discount rate	2,934	-	2,934
Actuarial losses/(gains)	174	(3,405)	(3,231)
Actuarial gain attributable to insurance contracts	-	11,107	11,107
Amounts recognised in other comprehensive income	<u>3,108</u>	<u>7,702</u>	<u>10,810</u>

#### **Changes in the fair value of the pension related assets and the present value of the defined benefit obligation**

<b>Fair value of the pension related assets</b>	<b>UK £000</b>	<b>Germany £000</b>	<b>Total £000</b>
At 1 January 2016	162,060	29,649	191,709
Exchange adjustments	-	6,081	6,081
Contributions paid to the scheme	23,887	-	23,887
Interest income on plan assets	6,135	-	6,135
Return on plan assets less than the discount rate	12,353	-	12,353
Benefits paid	(2,450)	(460)	(2,910)
Other movements on insurance contracts	-	11,674	11,674
<b>At 31 December 2016</b>	<u><b>201,985</b></u>	<u><b>46,944</b></u>	<u><b>248,929</b></u>

<b>Present value of the defined benefit obligation</b>	<b>UK £000</b>	<b>Germany £000</b>	<b>Total £000</b>
At 1 January 2016	161,972	37,352	199,324
Exchange adjustments	-	6,920	6,920
Current service charge	7,595	2,063	9,658
Past service charge	-	6,397	6,397
Benefits paid	(2,450)	(460)	(2,910)
Interest cost on defined benefit obligation	6,313	2,004	8,317
Actuarial losses/(gains)	56,359	4,412	60,771
<b>At 31 December 2016</b>	<u><b>229,789</b></u>	<u><b>58,688</b></u>	<u><b>288,477</b></u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **20. Pensions (continued)**

**Changes in the fair value of the pension related assets and the present value of the defined benefit obligation (continued)**

##### **Principal actuarial assumptions**

	2016		2015	
	UK %	Germany %	UK %	Germany %
Discount rate	2.55	2.00	3.75	2.30
Rate of increase in salaries	5.00	3.00	5.00	3.00
Inflation assumption	3.50	1.75	3.50	1.75

#### **21. Note to the statement of cash flows**

	2016 £000	2015 £000
Cash and cash equivalents comprise the following;		
Cash at bank and in hand	<u>235,799</u>	<u>110,913</u>

Of the cash and cash equivalents, £28,480,000 (2015: £11,441,000) is held to comply with regulatory requirements and is not available for immediate use.

Included in cash and cash equivalents are amounts totalling £1,758,000 (2015: £1,754,000) relating to the Group and £1,758,000 (2015: £1,745,000) relating to the Company which have been deposited with third parties to secure certain liabilities and is not available for immediate use.

The movement in other assets/liabilities in the Consolidated statement of cash flows is driven primarily by the timing difference between the gross cash out-flows and the expected reinsurance recovery. A process has been established whereby, when significant loss payments are required to be made, FMI has the ability to request advanced funding from FMIC for their portion of the loss. Historically such requests are driven by prudent business practices to avoid the cost of FMI selling investments to meet short term cash flow requirements.

#### **22. Capital Commitments**

The Company had the following future minimum lease payments under non-cancellable operating leases for each of the following periods:

	2016 £000	2015 £000
Payments due:		
Not later than one year	8,798	7,708
Later than one year and not later than five years	21,817	21,965
Later than five years	8,993	11,460
	<u>39,608</u>	<u>41,133</u>

The Company had no other off-balance sheet arrangements.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **23. Parent company and ultimate controlling party**

The Company is a wholly owned subsidiary of Factory Mutual Insurance Company (FMIC), the registered office of which is 270 Central Avenue, Johnston, RI 02919-4923, USA. FMIC is the largest group in which the financial results of FMI are included. Copies of the group accounts are available to the public either at the above address or from [www.fmglobal.com](http://www.fmglobal.com).

#### **24. Risk management**

##### **(a) Governance framework**

Key management recognises the critical importance of having efficient and effective risk management systems in place. Risk management is deeply embedded within the FM Global group of which the Company is an integral part.

The Company has established a risk management function with clear terms of reference from the board of directors and the board committees. The risk management function is overseen by a Risk Management Committee which is a board committee made up of senior management from across the business. The Risk Management Committee oversees all areas of risk management.

The risk management policy in place describes how the risk management function is run including the identification, assessment, management, monitoring and reporting of risks. The policy also provides guidance on the processes to be followed and the responsibilities of the different functions involved in the overall risk management framework.

##### **(b) Capital management objectives, policies and approach**

The Company seeks to optimise the structure and sources of capital to support its policyholders, maintain its strong ratings (AA (Very Strong) from Fitch Ratings, A+ (Superior) from A.M. Best and A+ (Strong) from Standard & Poor's) and ensure regulatory compliance.

The Company's approach to managing capital involves managing assets, liabilities and risks in a coordinated way, and taking appropriate action to maintain the capital position of the Company in the light of changes in economic conditions and risk characteristics.

The Company is subject to capital requirements prescribed by the Solvency II Directive and regulated by the Prudential Regulation Authority (PRA). It has complied throughout the year with these requirements.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **24. Risk management (continued)**

##### **(c) Insurance risk**

Insurance risk is the risk relating to fluctuations in the timing, frequency and severity of insured events, relative to the expectations of the Company at the time of underwriting. Insurance risk also refers to the fluctuations in the timing and amount of claims settlements. The objective of the Company is to ensure that sufficient reserves are available to cover these liabilities.

The Company has strong controls in place to mitigate insurance risk and the risk exposure is mitigated by diversification across a portfolio of insurance contracts and geographical areas as well as through the use of reinsurance arrangements. The Company specialises in commercial property and business interruption. Risks are usually short-tail in nature and of approximately twelve months duration.

The Company purchases reinsurance as part of its risk mitigation programme. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts. Although the Company has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to ceded insurance, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements. This is considered within the credit risk category.

The purpose of the underwriting and reinsurance strategies is to limit exposure to large risk losses and catastrophes based on the Company's risk appetite as determined by management. The insurance risk appetite is monitored through the risk appetite framework which is monitored and reviewed regularly by the board and its committees.

The table below sets out the concentration of outstanding claims liabilities by class of business:

	£000	2016 £000	£000
	Gross liabilities	Reinsurance of liabilities	Net liabilities
Fire & Other	281,699	193,188	88,511
Marine, Aviation and Transport	4,252	717	3,535
	<u>285,951</u>	<u>193,905</u>	<u>92,046</u>
	£000	2015 £000	£000
	Gross liabilities	Reinsurance of liabilities	Net liabilities
Fire & Other	382,176	285,843	96,333
Marine, Aviation and Transport	4,461	969	3,492
	<u>386,637</u>	<u>286,812</u>	<u>99,825</u>

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **24. Risk management (continued)**

The geographical concentration of the outstanding claims liabilities is noted below and based upon the countries where business is written, which is consistent with the basis used to analyse premiums and expenses and aligned with country specific reporting requirements.

	2016	
£000	£000	£000
Gross liabilities	Reinsurance of liabilities	Net liabilities
In the EU member state of its head office	156,517	46,500
In the other EU member states	106,300	41,202
In other countries	23,134	4,344
<b>285,951</b>	<b>193,905</b>	<b>92,046</b>
	2015	
£000	£000	£000
Gross liabilities	Reinsurance of liabilities	Net liabilities
In the EU member state of its head office	225,741	52,895
In the other EU member states	130,641	40,290
In other countries	30,255	6,640
<b>386,637</b>	<b>286,812</b>	<b>99,825</b>

#### ***Sensitivities***

The liabilities that are in place at the year-end are based on the best estimate of current claims outstanding with an additional element for claims incurred but not reported (IBNR). The IBNR is based on historical data patterns to provide a reasonable estimate of the future development of current claims.

Sensitivity testing around claims is performed as part of the regulatory reporting required for insurance companies. Although insurance risk is a principal risk for FMI it is managed and mitigated as part of day to day business so is not considered to be a high risk area. Significant increases in gross claims would largely be mitigated by the reinsurance programme with the effect of only a marginal net impact to the Company's surplus.

#### ***Claims development table***

The following tables show the estimates of cumulative incurred claims, including IBNR, for each successive accident year at each reporting date, together with cumulative payments to date. In setting claims provisions the Company exercises a degree of caution where there is considerable uncertainty. In general, the uncertainty associated with the ultimate claims experience in an accident year is greatest when the accident year is at an early stage of development. However, as claims develop the ultimate cost of claims become more certain.

The Company has elected to translate estimated claims and claims payments into the presentation currency at the rates of exchange at the current reporting date. The impact of exchange differences is shown at the bottom of the table. The Company has taken advantage of the transitional rules of FRS 103 that permit only five years of information to be disclosed upon adoption. The claims development information disclosed is being increased from five years to ten years over the period 2016-2021.



**FM Insurance Company Limited**

**Notes to the consolidated financial statements  
for the year ended 31 December 2016**

**24. Risk management (continued)**

Gross outstanding claims provision as at 31 December 2016:

Accident year	Before 2011 £000	2011 £000	2012 £000	2013 £000	2014 £000	2015 £000	2016 £000	Total £000
Estimate of cumulative claims incurred:								
At end of accident year		1,187,350	432,109	579,530	633,685	378,933	282,240	
One year later		1,133,481	432,257	528,171	580,941	361,295		
Two years later		1,115,662	421,335	533,901	535,138			
Three years later		1,113,688	424,770	534,523				
Four years later		1,107,382	422,579					
Five years later		1,099,380						
<b>Current estimate of cumulative claims incurred</b>		<b>1,099,380</b>	<b>422,579</b>	<b>534,523</b>	<b>535,138</b>	<b>361,295</b>	<b>282,240</b>	
Cumulative claims paid								
At end of accident year		439,960	125,299	151,769	141,996	127,809	88,871	
One year later		845,054	361,009	399,056	438,260	288,948		
Two years later		1,091,690	414,689	508,159	527,057			
Three years later		1,106,513	420,750	531,748				
Four years later		1,106,387	421,511					
Five years later		1,099,221						
<b>Cumulative payments to date</b>		<b>1,099,221</b>	<b>421,511</b>	<b>531,748</b>	<b>527,057</b>	<b>288,948</b>	<b>88,791</b>	
Outstanding claims		159	1,068	2,775	8,081	72,347	193,369	
Foreign exchange adjustment		1	5	18	57	229	988	
<b>Gross outstanding claims provision at 31 December 2016</b>	<b>6,855</b>	<b>160</b>	<b>1,073</b>	<b>2,793</b>	<b>8,138</b>	<b>72,576</b>	<b>194,357</b>	<b>285,952</b>

**FM Insurance Company Limited**

**Notes to the consolidated financial statements  
for the year ended 31 December 2016**

**24. Risk management (continued)**

Net outstanding claims provision as at 31 December 2016:

Accident year	Before 2011 £000	2011 £000	2012 £000	2013 £000	2014 £000	2015 £000	2016 £000	Total £000
Estimate of cumulative claims incurred								
At end of accident year		217,595	144,786	174,072	131,372	126,555	95,519	
One year later		185,542	129,525	148,929	109,149	112,744		
Two years later		168,032	127,582	151,731	104,018			
Three years later		171,583	128,638	150,794				
Four years later		169,796	128,562					
Five years later		167,480						
<b>Current estimate of cumulative claims incurred</b>		<b>167,480</b>	<b>128,562</b>	<b>150,794</b>	<b>104,018</b>	<b>112,744</b>	<b>95,519</b>	
Cumulative claims paid								
At end of accident year		33,802	46,669	50,715	41,030	43,401	31,096	
One year later		118,740	110,590	118,950	92,260	92,956		
Two years later		164,626	125,236	144,184	99,106			
Three years later		171,670	127,165	149,322				
Four years later		168,305	127,627					
Five years later		167,334						
<b>Cumulative payments to date</b>		<b>167,334</b>	<b>127,627</b>	<b>149,322</b>	<b>99,106</b>	<b>92,956</b>	<b>31,096</b>	
Outstanding claims		146	935	1,472	4,912	19,788	64,423	
Foreign exchange adjustment		1	4	11	35	91	321	
<b>Net outstanding claims provision at 31 December 2016</b>	<b>(93)</b>	<b>147</b>	<b>939</b>	<b>1,483</b>	<b>4,947</b>	<b>19,879</b>	<b>64,744</b>	<b>92,046</b>

# **FM Insurance Company Limited**

## **Notes to the consolidated financial statements for the year ended 31 December 2016**

### **24. Risk management (continued)**

#### **(d) Financial risk**

##### **(1) Credit risk**

Credit risk is defined as the risk relating to the Company's ability to recover money owed by third parties. This includes all counterparties, including reinsurers, intermediaries, policyholders, banks and issuers of investments. The principal credit risks identified by the Company are non-payment by an insured and non-payment by a reinsurer.

A credit risk policy is in place and outlines the assessment and determination of what constitutes credit risk for the Company. Compliance with the policy is monitored each month and exposures and breaches are reported to the Risk Management Committee. The policy is regularly reviewed and monitored against changes in the risk environment and the risk appetite framework.

The Company has a low appetite for all areas of credit risk. Specific tolerances and limits for credit risk areas are set based on the principal risks. The limits are set as measurable guidelines.

Concentration risk is mitigated by following policy guidelines in respect of placing reinsurance which are set by the Group Security Committee and subject to regular review. The Company sets the maximum amounts and limits that may be advanced to corporate counterparties by reference to their long term credit ratings and level of capitalisation.

The tables below provide an analysis of the maximum exposure to credit risk as identified by the Company (including an analysis of financial assets exposed to credit risk).

	Neither past due nor impaired £000	Past due £000	Impaired £000	Total £000
<b>31 December 2016</b>				
Other financial investments – debt securities	136,761	-	-	136,761
Debtors arising out of direct insurance operations	110,567	14,579	(60)	125,086
Debtors arising out of reinsurance operations	26,895	16,328	-	43,223
Cash at bank and in hand	235,799	-	-	235,799
	<u>510,022</u>	<u>30,907</u>	<u>(60)</u>	<u>540,869</u>
	Neither past due nor impaired £000	Past due £000	Impaired £000	Total £000
<b>31 December 2015</b>				
Other financial investments – debt securities	139,093	-	-	139,093
Debtors arising out of direct insurance operations	69,479	19,357	(59)	88,777
Debtors arising out of reinsurance operations	31,189	20,105	-	51,294
Cash at bank and in hand	110,913	-	-	110,913
	<u>350,674</u>	<u>39,462</u>	<u>(59)</u>	<u>390,077</u>

## *FM Insurance Company Limited*

### *Notes to the consolidated financial statements for the year ended 31 December 2016*

#### **24. Risk management (continued)**

The table below provides information regarding the credit risk exposure of the Company as at 31 December 2016 by classifying assets according to the credit ratings of the counterparties. AAA is the highest possible rating. Assets that fall outside the range of AAA to BBB (including captives) are classified as not rated. Debtors, other than amounts due from reinsurers, have been excluded from the table as these are not rated.

<b>31 December 2016</b>	<b>AAA £000</b>	<b>AA £000</b>	<b>A £000</b>	<b>BBB £000</b>	<b>Not rated £000</b>	<b>Total £000</b>
Other financial investments – debt securities	-	102,181	18,325	16,255	-	136,761
Reinsurers' share of claims outstanding	-	11,905	117,327	3,913	60,760	193,905
Debtors arising out of reinsurance operations	-	10,108	9,747	1,567	21,801	43,223
Cash at bank and in hand	20,061	12,037	196,658	7,043	-	235,799
	<u>20,061</u>	<u>136,231</u>	<u>342,057</u>	<u>28,778</u>	<u>82,561</u>	<u>609,688</u>
<b>31 December 2015</b>	<b>AAA £000</b>	<b>AA £000</b>	<b>A £000</b>	<b>BBB £000</b>	<b>Not rated £000</b>	<b>Total £000</b>
Other financial investments – debt securities	103,975	5,814	15,534	13,770	-	139,093
Reinsurers' share of claims outstanding	-	29,187	175,481	3,942	78,202	286,812
Debtors arising out of reinsurance operations	-	13,592	13,905	2,107	21,690	51,294
Cash at bank and in hand	6,773	14,546	72,405	17,189	-	110,913
	<u>110,748</u>	<u>63,139</u>	<u>277,325</u>	<u>37,008</u>	<u>99,892</u>	<u>588,112</u>

It is the Company's policy to invest in highly rated fixed interest securities. It is also the Company's policy to use highly rated reinsurers, the acceptance criteria being based on a combination of the reinsurer credit rating and available surplus. Credit risk is monitored closely as part of the risk appetite framework and the Company actively manages its product mix to ensure that there is no significant concentration of credit risk.

#### **(2) Liquidity risk**

Liquidity risk is the risk the Company may have insufficient financial resources available to meet its obligations as they fall due.

A liquidity risk policy is in place and sets out the assessment and determination of what constitutes liquidity risk. Compliance with the policy is monitored as part of the risk appetite framework and exposures and breaches are reported to the Risk Management Committee. The policy is regularly reviewed and monitored against changes in the risk environment and the risk appetite framework.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **24. Risk management (continued)**

##### **Maturity profiles**

The table below summarises the estimated timing of the net cash outflows resulting from recognised insurance liabilities.

	<b>Carrying amount £000</b>	<b>Up to a year £000</b>	<b>1 - 2 years £000</b>	<b>2 - 5 years £000</b>
<b>31 December 2016</b>				
Claims outstanding	<b>285,951</b>	<b>118,042</b>	<b>121,295</b>	<b>46,614</b>
Creditors arising out of direct insurance operations	<b>137,491</b>	<b>137,941</b>	-	-
<b>31 December 2015</b>				
Claims outstanding	<b>386,637</b>	<b>177,273</b>	<b>148,476</b>	<b>60,888</b>
Creditors arising out of direct insurance operations	<b>146,311</b>	<b>146,311</b>	-	-

#### **(3) Market risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises of three types of risk:

- a) currency risk;
- b) interest rate risk; and
- c) equity price risk.

A market risk policy is in place and sets out the assessment and determination of what constitutes market risk. Compliance with the policy is monitored as part of the risk appetite framework and exposures and breaches are reported to the Risk Management Committee. The policy is regularly reviewed and monitored against changes in the risk environment and the risk appetite framework.

##### **a) Currency risk**

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Company is exposed to currency risk in respect of investments which are primarily denominated in USD as part of a global investment portfolio. In addition, certain assets and liabilities relating to general insurance business are denominated in foreign currency. Excess currency is converted into USD as part of the global strategy to limit the currency risk of the FM Global group.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **24. Risk management (continued)**

The tables below summarise the main exposures to foreign currency exchange risk at the reporting date:

	£000	2016 £000	£000
	Euro exposure	US Dollar exposure	Other currency exposure
Financial investments	-	541,493	-
Reinsurers' share of technical provisions	169,160	101,126	17,440
Debtors	106,543	74,741	7,977
Cash at bank and in hand	18,098	135,305	56,259
	<b>293,801</b>	<b>852,665</b>	<b>81,676</b>
Technical provisions	242,320	142,149	27,403
Creditors	18,109	83,307	8,567
Net Pension Liability	58,688	-	-
Accruals and Deferred Income	17,030	2,114	2,739
	<b>336,147</b>	<b>227,570</b>	<b>38,709</b>

  

	£000	2015 (restated) £000	£000
	Euro exposure	US Dollar exposure	Other currency exposure
Financial investments	-	544,624	17,576
Reinsurers' share of technical provisions	201,859	112,308	39,463
Debtors	77,195	86,477	12,327
Cash at bank and in hand	766	38,409	62,259
	<b>279,820</b>	<b>781,818</b>	<b>131,625</b>
Technical provisions	265,511	153,726	53,240
Creditors	20,626	90,384	4,253
Net Pension Liability	37,352	-	-
Accruals and Deferred Income	10,993	2,434	2,814
	<b>334,482</b>	<b>246,544</b>	<b>60,307</b>

At 31 December 2016, if the USD exchange rate had varied by +/- 5% against Sterling with all other variables held constant, net assets would have fluctuated by £31.1m (2015: £26.3m).

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **24. Risk management (continued)**

##### **b) Interest rate risk**

Interest rate risk is the risk that the value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has no significant concentration of or exposure to interest rate risk.

The Company invests only in fixed rate debt instruments and the Company's investment policy requires it to manage interest rate risk by maintaining a mix of assets. Interest on fixed rate instruments is priced at inception and is fixed until maturity. Insurance liabilities are short-term in nature and are not discounted.

##### **c) Equity price risk**

Equity price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The Company's equity price risk exposure relates to investment securities whose values will fluctuate as a result of changes in market prices. Investment guidelines are set in accordance with the principles and limits detailed in the risk appetite framework. The day to day management of the investment portfolio is performed by the FMIC Investment team, who manage the investments within the specified investment guidelines. There is no significant concentration of equity risk.

The analysis below is performed for potential movements in market indices with all other variables held constant, showing the impact on profit before tax for financial instruments recorded at fair value through profit or loss at the reporting date.

Changes in variables - market indices

	2016	2015
Change in market indices	Impact on profit before tax £000	Impact on profit before tax £000
+/- 20 %	80,946	84,606
+/- 10 %	40,473	42,303

The method used for deriving sensitivity information and significant variables did not change from the previous period.

## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **25. Reconciliation to US GAAP**

The financial statements have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP), which differs in certain respects from accounting principles generally accepted in the United States (US GAAP). Whilst there are numerous differences between the two bases of accounting, there are only a limited number that are applicable to the Group. The following is a reconciliation of UK GAAP shareholders funds attributable to equity interests and UK GAAP profit for the year to the equivalent measures under US GAAP. A description of the relevant differences follows the reconciliation.

##### **Shareholder's Equity Reconciliation:**

	2016	2015 (restated)
	£000	£000
UK GAAP shareholder's funds attributable to equity interests	582,405	507,679
Defined benefit pension asset	(488)	(646)
US GAAP shareholder's equity	<u>581,917</u>	<u>507,033</u>

##### **Profit and Loss Reconciliation:**

	2016	2015 (restated)
	£000	£000
UK GAAP profit/(loss) for the year	87,453	(7,922)
Equalisation provision	(9,294)	2,946
Defined benefit pension liability	(4,760)	2,134
Unrealised (gain)/loss on investments	(11,583)	32,440
Foreign exchange revaluations of investments	39,480	7,679
US GAAP profit for the year	<u>101,296</u>	<u>37,277</u>

##### ***Equalisation Provision***

Prior to 2016, an equalisation provision was recognised in accordance with the rules in the PRA handbook for the purpose of mitigating exceptionally high loss ratios in future years. The requirement was in place to help smooth fluctuations in loss ratios in future years for business where claims in any future year may be subject to significant deviations from recent or average claims experience, or where trends in experience may be subject to change. Solvency II has been implemented with effect from 1 January 2016 and there is no longer a requirement to hold an equalisation provision. It has therefore been released in the 2016 year.

##### ***Defined Benefit Pension Asset***

Under UK GAAP, retirement benefits are accounted for under FRS 102, Section 28 Employee Benefits. For US GAAP, the Company follows the accounting policy of its parent company, the Statement of Financial Accounting Standard No. 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS 158). Under both FRS 102 and SFAS 158, the funded status of defined benefit plans are recorded on the balance sheet. The basic principles of the two standards are similar, however there are differences in the underlying calculations of the funded status.



## ***FM Insurance Company Limited***

### ***Notes to the consolidated financial statements for the year ended 31 December 2016***

#### **25. Reconciliation to US GAAP (continued)**

##### ***Unrealised (gains)/losses on investments***

Under UK GAAP, unrealised gains and losses on investments are recognised in the profit and loss account. For US GAAP purposes, unrealised gains and losses on investments are recognised within Shareholder's Equity as a component of Other Comprehensive Income.

##### ***Foreign exchange revaluations of investments***

Under UK GAAP foreign exchange revaluations on investments are recognised in the profit and loss account. For US GAAP purposes, foreign exchange revaluations on investments are recognised directly in Shareholder's Equity as a component of Other Comprehensive Income, as long as the related investments are held at the Balance sheet date.