Solvency and Financial Condition Report

Entity: QBE European Operations plc

Contents

Summary

QBE European Operations plc is an investment holding company (the Company). The principal activities of its subsidiary undertakings (together with the Company comprising QBE EO or the Group) are the transaction of insurance and reinsurance business. The Group will continue these activities for the foreseeable future.

The Company is a wholly owned indirect subsidiary of the Sydney headquartered QBE Insurance Group Limited (QBE Group). The QBE Group is ASX listed and is a top 20 global insurer and reinsurer. The QBE Group manages its business via four geographically aligned external facing divisions:

- QBE European Operations
- QBE North America (QBE NA)
- QBE Australia and New Zealand (QBE ANZO)
- QBE Emerging Markets (QBE EM)

The Group's strategic priorities have been developed in accordance with the QBE Group strategy and focus on five key priorities, outlined below:

- Underwriting excellence – Maintaining best-in-class underwriting skill and discipline, and offering specialist products through the London market and regional hubs
- Customer and partner-led growth – Strengthening major customer and broker relationships, protecting profitable portfolios, and driving new, high quality business through an extensive distribution footprint
- Claims excellence – Implementing the global claims excellence program, including sharing claims expertise with other divisions
- Data and analytics – Driving the use of data and analytics in underwriting, claims and distribution, improving the quality of new and renewal business
- World class talent – Attracting, retaining, motivating and rewarding the best people in the sectors

Classification of entities within the Group

The Group is constituted of a number of entities that carry out different functions and have different characteristics. In compliance with Solvency II regulations these entities have been classified into the following types:

- (Re)insurance undertakings
- Insurance holding companies
- Ancillary services undertakings
- Undertakings carrying out financial activities
- Other related undertakings

This approach differs to that employed under previous regulations and, hence, the calculation of capital requirements and eligible funds to cover those requirements differs significantly from that used under the previous regulatory regime. This is detailed further in Section E: Capital Management.

Business and Performance Summary

The Group reported for the year ended 31 December 2016 (2015 £142,070k).

Trading conditions deteriorated in most areas in the period, with average premium rate reductions on renewed business of 2.4%, reflecting a slight improvement on the 3.2% reduction experienced during 2015. The Group completed several reinsurance transactions in order to reduce exposure to UK long tail liabilities during the year, benefitting net claims incurred and reducing net earned premium by £122m.

On the 27 February 2017, the Ministry of Justice announced a change in the discount rate which is applied to certain lump sum bodily injury claims (the Ogden rate). The pre-tax impact of this adjusting post balance sheet event was £95,027k.

Excluding the effect of the reinsurance transactions, QBE European Operations plc (QBE EO) recorded a strong underlying performance, against an industry wide increase in large risk and catastrophe claims activity. Including the reinsurance transactions and impact of change in Ogden tables, the division produced a combined operating ratio of 100.0% compared with 89.1% in the prior year.

The underlying trends experienced by the Group reflect the experience of the underlying (re)insurance entities and the Group's Lloyd's participations.

The Group's commitment to underwriting excellence and preserving profit margins remains central to success.

Brexit planning is well advanced to restructure the Group's business. The Group has recently announced its intention to establish a Belgian subsidiary to ensure that the QBE Group continues to have access to the European single market.

System of Governance Summary

The Company's corporate governance structure has continued to evolve during 2016, reflecting the Boards' commitment to ensuring that it remains efficient, relevant and supportive of the strategic aims of the Company. The structure complies with all relevant regulatory and legal requirements. As a member of the QBE Group, the Company is not bound by the UK Corporate Governance Code. However, as a matter of best practice, the Company's Boards seeks to comply with the Code, where practical and relevant.

Key changes to the corporate governance structure during the year were:

- The establishment of a Compliance Management Group (CMG) to support the Risk and Capital Committee (RCC) in providing co-ordinated oversight and monitoring of the Company's adherence to its Compliance Framework
- The establishment of a Brexit Steering Group to provide oversight, direction and guidance to support the Boards in responding to the United Kingdom's exit from the European Union
- The disbanding of the Solvency II Steering Group (previously a sub-group of the RCC), the Group having received approval from the Prudential Regulation Authority (PRA) to the use of an Internal Model in December 2015

- The formalisation of the Risk and Capital Group (RCG) as a formal sub-group of the RCC. The RCG was established in 2015 to provide executive support, and filter information flow, to the RCC. Given its importance in the structure, in February 2016 it was determined that the RCG should become a formal sub-group of the RCC

During the year, Committee Terms of Reference and Board Charters were all reviewed by the relevant Committees and Boards, with minor enhancements being made to reflect ongoing assessment of key responsibilities of the Committees and matters reserved for the Boards.

During 2016 the Group Boards undertook Board Effectiveness Reviews, evaluating Board, committee, and individual director performance. Areas for enhancement to support continuous improvement of effectiveness arising from the review were discussed and agreed by the Boards.

A combined Board away day is held annually, providing the opportunity for the Boards to focus on strategy (with presentations from senior management) and to meet more informally. Non-executive Director engagement is further supported through informal meetings exclusively for the Group's non-executive Directors and meetings with non-executive Directors from the QBE Group Board.

Risk Profile Summary

Risks that could affect the Group's ability to achieve its objectives are identified on a continuous basis through business unit risk and control workshops and the emerging risk process.

The main risks are regularly reported and discussed at the Group's RCC through the Own Risk and Solvency Assessment (ORSA). A brief summary of the main risk categories is below:

- Strategic risk – defined as the current and prospective impact on earnings and/or capital arising from strategic business decisions and responsiveness to external change
- Insurance risk - defined as the risk of fluctuations in the timing, frequency and severity of insured events and claims settlements, relative to expectations
- Credit risk – defined as the risk of not recovering money owed to the Company by third parties, as well as the loss in value of assets due to deterioration in credit quality
- Group risk – defined as the risk arising specifically from being part of a wider group, including financial impact and loss of support from the QBE Group
- Market risk – defined as adverse impacts on earnings resulting from changes in market factors
- Liquidity risk – defined as the risk of holding insufficient liquid assets to meet liabilities as they fall due to policyholders or creditors, or only being able to do so at excessive cost
- Operational risk – defined as the risk of financial loss resulting from inadequate or failed internal processes, people and systems or from external events

The Group uses a number of risk mitigation techniques to mitigate these risks, as described in section B.

There have been no material changes to the system of risk management in the period.

Valuation Summary

The IFRS statutory financials are the starting point for the valuation of the Group's assets and liabilities on a Solvency II basis. The IFRS financials have been assessed for consistency with Solvency II valuation principles and, where appropriate, adjusted to reflect differences in basis. Section D sets out the adjustments made and expert judgements applied to arrive at a Solvency II basis balance sheet.

On a Solvency II valuation basis at 31 December 2016 the Group held total assets of £8,156,092k, had total Technical Provisions of £3,715,364k (comprising a net best estimate provision of £3,265,158k and risk margin of £450,206k) and had other liabilities of £2,132,568k.

Capital Management Summary

The Group's primary capital management objective is to maintain sufficient own funds to cover the Solvency Capital Requirement (SCR) with an appropriate surplus. The Group has adopted a Capital Appetite Framework, setting out the target levels of capital and potential remediation actions in the event that capital falls below the stated appetite. The Capital Appetite Framework has been approved by the Group's Board and senior management hold regular meetings, on at least a quarterly basis, to monitor the ratio of Eligible Own Funds (EOF) over SCR.

The Group's own funds have been assessed against the criteria of Article 71 of the Delegated Acts and the majority of the capital has been classified as sufficient quality to meet the eligibility requirements of 'Tier 1' capital, the only exception being Deferred Tax Assets (DTA) which have been classified as 'Tier 3' EOF.

The EOF at 31 December 2016 was £1,980,311k, after adjusting for valuation basis differences between IFRS statutory financials and Solvency II and applying restrictions in relation to Ring Fenced Funds (RFF). The SCR at 31 December 2016 was £1,466,930k and the Minimum Capital Requirement (MCR) was £583,188k.

The SCR Coverage Ratio of 126% presented in the Group's Annual PRA submission includes a foreseeable dividend payable in Q2 2017. This dividend is included in the Annual Return as an adjusting post balance sheet event as it is foreseeable at the date of board approval of submission.

The SCR coverage ratio at 31 December 2016 would be disclosed as 135% in the absence of this foreseeable dividend.

The Group has an approved Internal Model which it uses as the basis for the SCR. The Internal Model reflects the risk assessment processes that have been reflected across the business for several years and considers all classes of business underwritten by the Group. The Internal Model incorporates consideration of underwriting risk, reserving risk, credit risk, market risk, liquidity risk, operational risk, group risk and pension risk.

The data flows within the Internal Model are documented, self-assessed and output reported to the Data Quality Group, a sub Group of the Operations Management Group (OMG). Areas identified as requiring remediation are recorded on a Data Quality Issues Log and progress reported regularly to the Data Quality Group.

Directors' Report

Directors

T C W Ingram *

John Neal **

R V Pryce

D J Winkett

* Independent non-executive Director

** Non-executive Director

Resignations and appointments during the year

P A Dodridge Resigned 19 December 2016

Company secretary

A J Smith

Statement of Directors' responsibilities

The Directors are responsible for ensuring that the Solvency and Financial Condition Report, including the attached public quantitative reporting templates, have been prepared in all material respects in accordance with PRA rules and Solvency II regulations.

The Directors are satisfied that, throughout the year and in all material respects, the Company has complied with the requirements of the Solvency II Directive, the Delegated Acts, Technical Standards and Guidelines, and PRA rules. The Company reasonably believes that compliance with these rules and regulations will continue in all material respects for the foreseeable future.

Statement of disclosure of information to auditors

Each person who is a Director at the date of this report confirms that:

- So far as the Director is aware, there is no relevant audit information of which the auditors are unaware
- The Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of, and to establish that the Company's auditors are aware of, any relevant audit information

By order of the Board:

Director

QBE European Operations Plc

Registered Number 2641728

London

29 June 2017

Auditors' Report

Report of the external independent auditors to the Directors of QBE European Operations plc ('the Company') pursuant to Rule 4.1 (2) of the External Audit Part of the PRA Rulebook applicable to Solvency II firms

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

Opinion

Except as stated below, we have audited the following documents prepared by the Company as at 31 December 2016:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the Group Solvency and Financial Condition Report of the Company as at 31 December 2016, ('**the Narrative Disclosures subject to audit**'); and

- Group templates S.02.01.02, S.23.01.22 and S.32.01.22 ('**the Templates subject to audit'**).

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

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

- Information contained within the relevant elements of the Group Solvency and Financial Condition Report set out above which are, or derive from the Solvency Capital Requirement, as identified in the Appendix to this report;

- The 'Summary', 'Business and performance', 'System of governance' and 'Risk profile' elements of the Group Solvency and Financial Condition Report;

- Group templates S.05.01.02, S.05.02.01 and S.25.03.22;

- The written acknowledgement by management of their responsibilities, including for the preparation of the Group Solvency and Financial Condition Report ('**the Responsibility Statement**');

- Information which pertains to an undertaking that is not a Solvency II undertaking and has been prepared in accordance with PRA rules other than those implementing the Solvency II Directive or in accordance with an EU instrument other than the Solvency II regulations ('**the sectoral information**') as identified in the Appendix to this report.

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

In our opinion, the information subject to audit in the relevant elements of the Group Solvency and Financial Condition Report of the Company as at 31 December 2016 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based, as supplemented by supervisory approvals.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & I)), International Standard on Auditing (UK) 800 and International Standard on Auditing (UK) 805, and applicable law. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the relevant elements of the Group Solvency and Financial Condition Report* section of our report.

Emphasis of Matter - Basis of Accounting

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

Responsibilities of Directors for the Group Solvency and Financial Condition Report

The Directors are responsible for the preparation of the Group Solvency and Financial Condition Report in accordance with the financial reporting provisions of the PRA rules and Solvency II regulations which have been supplemented by the approvals made by the PRA under the PRA Rules and Solvency II regulations on which they are based, as detailed below:

- Approval to use a full or partial internal models

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

Auditors' Responsibilities for the Audit of the relevant elements of the Group Solvency and Financial Condition Report

It is our responsibility to form an independent opinion, in accordance with applicable law, ISAs (UK & I) and ISAs (UK) 800 and 805 as to whether the information subject to audit in the relevant elements of the Group Solvency and Financial Condition Report is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based. ISAs (UK & I) require us to comply with the Auditing Practices Board's Ethical Standard for Auditors.

An audit involves obtaining evidence about the amounts and disclosures in the relevant elements of the Group Solvency and Financial Condition Report sufficient to give reasonable assurance that the relevant elements of the Group Solvency and Financial Condition Report are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the relevant elements of the Group Solvency and Financial Condition Report. In addition, we read all the financial and non-financial information in the Group Solvency and Financial Condition Report to identify material inconsistencies with the audited relevant elements of the Group Solvency and Financial Condition Report. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

This report, including the opinion, has been prepared for the Directors of the Company to comply with their obligations under External Audit rule 2.1 of the Solvency II firms Sector of the PRA Rulebook and for no other purpose. We do not, in providing this report, accept or assume responsibility for any other purpose save where expressly agreed by our prior consent in writing.

Other Matter

The Company has authority to calculate its Group Solvency Capital Requirement using an internal model ('the Model') approved by the Prudential Regulation Authority in accordance with the Solvency II Regulations. In forming our opinion (and in accordance with PRA Rules), we are not required to audit the inputs to, design of, operating effectiveness of and outputs from the Model, or whether the Model is being applied in accordance with the Company's application or approval order.

Report on Other Legal and Regulatory Requirements

Sectoral Information

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

Other Information

In accordance with Rule 4.1 (3) of the External Audit Part of the PRA Rulebook for Solvency II firms we are required to read the Other Information and consider whether it is materially inconsistent with the relevant elements of the Group Solvency and Financial Condition Report and our knowledge obtained in the audits of the Group Solvency and Financial Condition Report and of the Company's statutory financial statements. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants
7 More London Riverside
London
SE1 2RT
29 June 2017

- The maintenance and integrity of the QBE European Operations plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Group Solvency and Financial Condition Report since it was initially presented on the website.
- Legislation in the United Kingdom governing the preparation and dissemination of Solvency and Financial Condition Reports may differ from legislation in other jurisdictions.

Appendix – relevant elements of the Group Solvency and Financial Condition Report that are not subject to audit

The relevant elements of the Group Solvency and Financial Condition Report that are not subject to audit comprise:

- The following elements of Group template S.02.01.02:
  - Row R0550: Technical provisions - non-life (excluding health) - risk margin
  - Row R0590: Technical provisions - health (similar to non-life) - risk margin
  - Row R0640: Technical provisions - health (similar to life) - risk margin
  - Row R0680: Technical provisions - life (excluding health and index-linked and unit-linked) - risk margin
  - Row R0720: Technical provisions - Index-linked and unit-linked - risk margin

- The following elements of Group template S.23.01.22
  - Row R0020: Non-available called but not paid in ordinary share capital at group level
  - Row R0060: Non-available subordinated mutual member accounts at group level
  - Row R0080: Non-available surplus at group level
  - Row R0100: Non-available preference shares at group level
  - Row R0120: Non-available share premium account related to preference shares at group level
  - Row R0150: Non-available subordinated liabilities at group level
  - Row R0170: The amount equal to the value of net deferred tax assets not available at the group level
  - Row R0190: Non-available own funds related to other own funds items approved by supervisory authority
  - Row R0210: Non-available minority interests at group level
  - Row R0380: Non-available ancillary own funds at group level
  - Row R0680: Group SCR
  - Row R0740: Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds
  - Row R0750: Other non available own funds

- Elements of the Narrative Disclosures subject to audit identified as 'unaudited'.

Section A: Business and Performance

1. Business

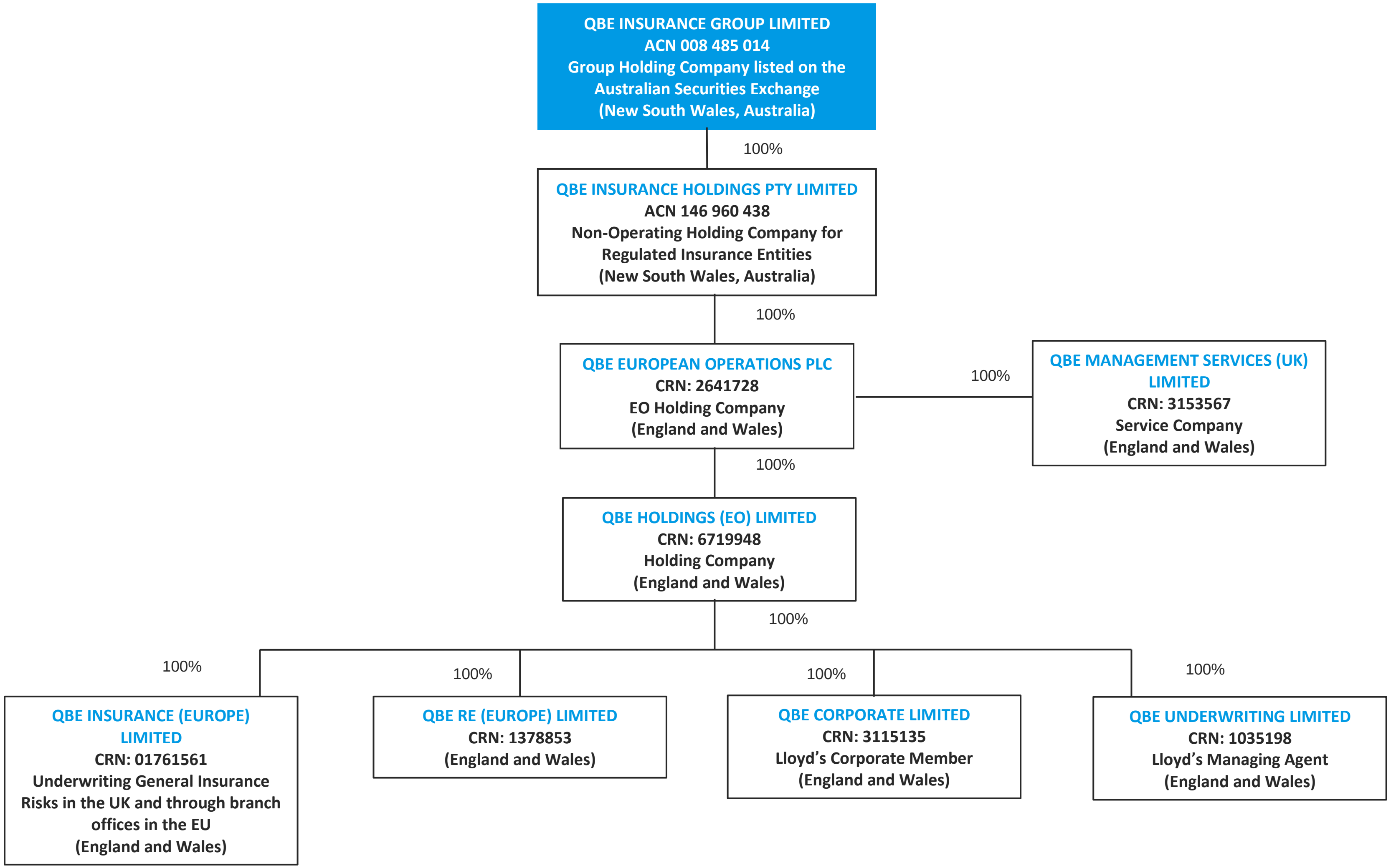
The holding company of the QBE European Group is QBE European Operations Plc. The entire issued share capital of the Company is owned by QBE Insurance Holdings Pty Limited and the Company is ultimately wholly owned by QBE Insurance Group Limited (QBE Group). QBE Insurance Group Limited is listed on Australian Stock Exchange and is subject to supervision by the Australian Prudential Regulation Authority.

The principal activities of the subsidiary undertakings within the Group are the transaction of insurance and reinsurance business. The Group will continue these activities for the foreseeable future.

The Group comprises leading specialty commercial insurer and reinsurer businesses operating through Lloyd's and company markets and comprises three market facing underwriting divisions; International Markets, Retail and QBE Re - QBE Insurance Group's global reinsurance division.

The Group has a strong UK and London market presence and a branch and office network across the UK and Ireland, Western Europe, Canada, Dubai, the mainland USA and Bermuda.

The Company's position within the QBE Group structure, along with the principal subsidiary undertakings that are included in the Group, is shown below:



Note: This is a high level simplified structure showing ownership chain of key operational companies in QBE European Operations

A full list of undertakings within the Group, and the nature of those undertakings, can be found in the quantitative reporting template (QRT) S.32.01, included in Appendix A.

The Company has no branches, however the Group has overseas operations in a number of countries. In respect of the regulated subsidiaries, insurance and reinsurance business has, during 2016, been written through the following locations:

Subsidiary	Branch locations
QBE Insurance (Europe) Limited	Denmark
	Dubai
	France
	Germany
	Italy
	Slovakia
	Spain
	Sweden
QBE Re (Europe) Limited	Belgium
	Bermuda
	Ireland

The main regulated subsidiaries within the Group, QBE Insurance (Europe) Limited and QBE Re (Europe) Limited, are authorised by the PRA and regulated by the Financial Conduct Authority (FCA) and the PRA. The supervisory authority responsible for financial supervision of the companies is the PRA. The PRA supervisor is Mr. David Kelland.

The PRA contact details are:

Prudential Regulation Authority
Bank of England
Threadneedle Street
London
EC2R 8AH
Telephone: +44 (0) 203 4614 444
www.bankofengland.co.uk/pra

The FCA contact details are:

Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London
E14 5HS
Telephone: +44 (0) 2070 661 000
www.fca.org.uk

The external auditor of the Company is PricewaterhouseCoopers LLP, Chartered Accountants. The audit partner responsible is Mr. Andrew Moore. Their address is:

PricewaterhouseCoopers LLP
7 More London Riverside
London
SE1 2RT
Telephone: +44 (0) 2075 835 000
www.pwc.co.uk

Product Lines and Geographical locations

The Company does not underwrite any Product Lines. Further details relating to the Solvency II Product Lines and Gross Written Premium by location is found in the SFCR for QBE Insurance (Europe) Limited and QBE Reinsurance (Europe) Limited.

Significant Events

The Group delivered a strong underwriting performance during a year of challenging trading conditions, an industry wide increase in large risk and catastrophe claims, and unprecedented currency fluctuation.

The Group completed several reinsurance transactions in order to reduce exposure to UK long tail liabilities during the year, benefitting net claims incurred and reducing net earned premium by £122 million.

The Group has been applying the Prudential Regulation Authority (PRA) approved internal capital model from 1 January 2016. The internal model is an integrated framework to support its objectives by managing risk and capital across the business. The internal model has broad scope including: capital modelling; risk identification; mitigation; assessment and monitoring, and is used in the day to day operation of the Group.

The internal model is used to help assess risk and calculate the appropriate level of risk-based capital to allocate to risks to which the Group is exposed. The assessment of risk-based capital enables us to make decisions that involve quantitative risk reward trade-offs. The allocation of risk-based capital helps ensure that the level of risk taken is commensurate with the required returns and is within the approved risk appetite and tolerance.

On 19 November 2016 the Company reduced the nominal value of the ordinary shares from £1 each to £0.38 resulting in a reduction to share capital of £1,625,180k, with a corresponding increase in accumulated profits. The called up, allotted and fully paid share capital of the Company at year end was £996,078k (2015 £2,621,258k)

In December 2016, the Board approved a Capital Appetite Framework designed to ensure that the Group operates within a target range of capital, which exceeds the regulatory solvency capital requirements.

On the 27 February 2017, the Ministry of Justice announced a change in the Ogden discount rate which is applied to certain lump sum bodily injury claims. The pre-tax impact of this adjusting post balance sheet event is a loss of approximately £95,027k and this is reported within the 2016 financial statements and claims ratio.

On 1 June 2017 the $550,000k capital securities issued to a fellow QBE Group subsidiary were called for redemption by the Company on the securities first call date. The securities were redeemed in full at fair value. This non adjusting post balance sheet event completed during June 2017.

In conjunction with the redemption of the capital securities, a subsidiary undertaking agreed to receive early settlement of its £522,850k loan previously issued to QBE Insurance Group Limited. This non adjusting post balance sheet event was completed during June 2017. These two post balance sheet events reduced QBE EO's exposure to the wider QBE Group.

Brexit planning is well advanced to restructure the Group's business. The Group has recently announced its intention to establish a Belgian subsidiary to ensure that the QBE Group continues to have access to the European single market.

2. Underwriting Performance

The underwriting result of the Group, split by Solvency II line of business, is shown in the table below.

The underwriting result is calculated by using the following formula:

Net premiums earned *less* Net claims incurred *less* Expenses equals Underwriting result.

As this is the first year of full Solvency II reporting, and in compliance with regulatory guidance, prior year comparative values are not shown. Prior period comparatives will be shown in future years.

The figures below are shown by Solvency II lines of business. The total values are consistent with IFRS, however they do not directly reconcile to the QBE EO Plc financial statements as the IFRS basis financials consolidate QBE's share of its Lloyd's participations.

Solvency II product lines	Type	Gross Written Premium* (£'000)	Net premiums earned (£'000)	Net claims incurred (£'000)	Expenses incurred (£'000)	Underwriting result (£'000)
Motor vehicle liability insurance	Direct	222,317	202,910	185,753	70,707	(53,550)
Other motor insurance	Business	47,996	44,285	36,080	15,590	(7,385)
Marine, aviation and transport insurance	And	75,538	64,795	17,327	20,091	27,377
Fire and other damage to property insurance	Accepted	325,553	244,331	107,064	102,162	35,105
General liability insurance	Proportional	577,709	398,009	222,030	188,140	(12,161)
Credit and suretyship insurance	Reinsurance	66,165	58,187	23,160	30,578	4,449
Legal expenses insurance		10,776	7,384	4,528	2,346	510
Casualty	Accepted non-	103,201	79,412	55,850	27,739	(4,177)
Marine, aviation and transport	proportional	33,755	(1,632)	5,099	2,699	(9,430)
Property	reinsurance	144,914	115,446	41,207	31,888	42,351
Annuities stemming from non-life insurance contracts	Life insurance	0	0	0	0	0
Other	Other	60,167	34,196	21,773	11,513	910
Total		**1,668,091**	**1,247,323**	**719,871**	**503,453**	**23,999**

**Direct business and reinsurance accepted*

Analysis of underwriting performance by Solvency II lines of business

An analysis of the underwriting performance of the Regulated Companies within the Group by Solvency II lines of business is disclosed in the following publicly available documents:

- QBE Insurance (Europe) Limited Solvency and Financial Condition Report, Section A.1.
- QBE Re (Europe) Limited Solvency and Financial Condition Report, Section A.1.

Analysis by geographic area

A geographical analysis of the gross written premiums and profit/loss before taxation of the regulated entities within the Group, QBE Insurance (Europe) Limited and QBE Re (Europe) Limited, can be found in the statutory accounts of those companies for the year ended 31 December 2016, in the sections headed 'Segmental information'.

3. Investment Performance

The Group's investments are primarily held in fixed income bonds and money market instruments; with modest exposure to growth assets through investment funds in developed market equities, unlisted property, emerging market equities, emerging market debt, high yield debt and social impact bonds.

The majority of fixed income portfolios have an average credit rating equivalent to or better than Standard & Poor's "A". The minimum permitted credit quality per the guidelines is "BBB-" grade instruments.

During 2016 most asset classes performed well, supported by monetary policy and continued economic expansion. It was a fairly volatile, risk averse start to the year as concerns over the Chinese economy and European banks came to the fore. Equity markets fell sharply by mid-February whilst developed market government bonds produced strong returns through to the summer. Geopolitical surprise dominated the second half of the year following the UK's 'Brexit' vote in June and the election of Donald Trump as US President in November. Earlier strong returns in developed market bonds were pared back in the last quarter as global yields rose and investor's switched attention to riskier assets.

Throughout the reporting period, return is measured and reported at an asset class level for the Group. A summary of this information is provided to the European Operations Investment Committee (EOIC) on a monthly basis.

Total fixed income investment return was 1.79%, driven by additional credit exposure and longer duration added in the first half of 2016, although returns were pared back slightly in Q4 as a result of the significant rise in global bond yields. Investment in infrastructure delivered 2.90% for the year; credit spread was a positive contributor.

Total growth asset investment return was 4.33% for the year, enhancing overall investment return by 16 basis points. Asset class performance was mixed with notable variances in Developed Market Equities delivering 0.89%, Emerging Market Equities returning 17.94%, and High Yield Debt yielding 9.30%.

Details of interest received, investment income received, other income, and realised and unrealised returns in the period are shown in the table below.

Asset Category	Dividends (£'000)	Interest (£'000)	Net Gains and Losses (£'000)	Unrealised Gains and Losses (£'000)
Equity	793		(1,484)	(4,743)
Government Bonds	-	6,143	5,880	(2,009)
Corporate Bonds	-	41,720	244	21,393
Collective Investment Undertakings	8,076		2,152	9,200
Collateralised Securities	-	6,201	1,064	2,990
Cash and Deposits	-	1,761	-	-
Mortgages and Loans	-	1,768	90	50
Futures	-		(477)	-
Derivatives			154,267	(15,868)
Total	**8,869**	**57,593**	**161,736**	**11,013**

**The details of investment income by asset category are consistent with the requirements of QRT S.09.01*

The total investment returns achieved for the year are set out below. The combined currency total return for the year was 1.95%.

Yield by Asset Type	2016 (%)
Fixed income	1.79
Equities	0.89
Infrastructure loans	2.90
Unlisted property trusts	7.26
High yield debt	9.30
Emerging market equity	17.94
Emerging market debt	1.11
Social impact bonds	8.90

Investment Manager

Day to day management of the Group's investment portfolio is outsourced to QBE Group Investments via an Investment Management Agreement.

Where appropriate, specialist investment managers are employed in order to gain access to areas of investment markets that require specific expertise.

Those responsible for investing the Group's assets do so in line with the Investment Guidelines and Restrictions approved by the Boards and the Investment Management Agreement.

The performance of the investment manager is monitored against an absolute return mandate, using other reference benchmarks or peer group performance as key performance indicators.

Foreign Exchange Management

The Group operates a policy to minimise foreign exchange risk by holding assets in foreign currencies in order to match underwriting liabilities in such currencies where size is deemed material. The residual net asset value in all material currencies is then hedged to mitigate foreign exchange risk.

Investments in securitisation

The Group's Investment Guidelines and Restrictions impose certain criteria for investment in relation to securitised assets in addition to that which exists for fixed income investment in general. Specifically and to comply with Article 135 2(a) of the SII Directive 2009/138/EC the fund manager shall when investing in products specified as structured, ensure that:

- The originator of the product at all times retains a net economic interest of no less than 5%
- That a dual rating is retained by each issue in order to avoid that issue being treated as having no rating
- Shall not invest in securities that are classified as 're-securitised' products

Exposure within the Group's portfolio is currently comprised of ABS (Asset Backed Securities, RMBS (Residential Mortgage Backed Securities) and MBS (Mortgage Backed Securities).

4. Performance of other activities

The Company has a number of intra-group funding arrangements within the Group and also inter-group funding arrangements with other companies within the wider QBE Group, arrangements which lead to interest receivables and payables.

5. Any other information

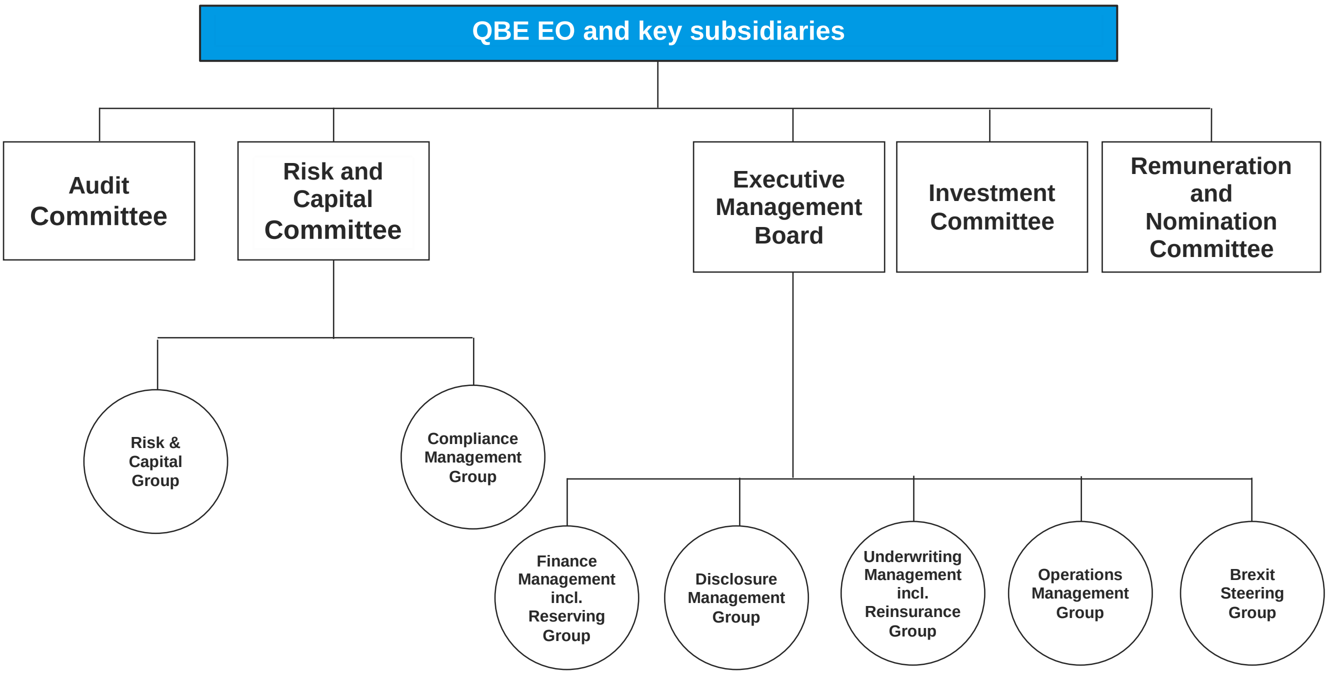
On 19 November 2016 the Company reduced the nominal value of the ordinary shares from £1 each to £0.38 resulting in a reduction to share capital of £1,625,180k, with a corresponding increase in accumulated profits. The called up, allotted and fully paid share capital of the Company at year end is £996,078k (2015 £2,621,258k).

Section B: System of governance

1. General information on the system of governance

The Board charter of the Company states that the Board of Directors of the Company is responsible for the long term success of the Company and its subsidiaries. The role of the Board is to provide leadership; to oversee the design and implementation of Group strategy and to set a framework of prudent and effective controls which enable risk to be assessed and managed within it. The Board ensures that the necessary financial and human resources are in place for the Group to meet its objectives and reviews the performance of management in delivering on Group strategic aims. The Board should set and instil Group values and culture in the light of those set by the QBE Group, the ultimate holding company of the Group, and ensure that its obligations to its shareholder and other stakeholders are understood and met.

The Board and Committee structure of the Group is illustrated below:



Until 1 March 2016, the Board was chaired by John Neal, Chief Executive Officer (CEO) of QBE Group. With effect from 1 March 2016, Tim Ingram, was appointed Chairman of the Company, with John Neal remaining as a member of the Board. The Board comprises two executive directors, one independent non-executive director and the QBE Group CEO as an additional non-executive director.

The role of the Chairman of the Board is distinct from that of the Chief Executive Officer, and each role is clearly established. The Board considers that the experience and areas of focus which each Board member brings to the Company results in a strong and balanced leadership team to set and monitor the strategy and values of the Group.

Apart from the Company, there are three key operating entities within the Group, namely: QBE Re (Europe) Limited; QBE Insurance (Europe) Limited; and QBE Underwriting Limited (the EO Regulated Companies).

The Boards of the EO Regulated Companies have four non-executive directors, including the Chairman of the Company, all of whom are members of the audit committee. All the non-executive directors of the Regulated subsidiaries are considered to be independent of management and free from any relationship that could materially interfere with the exercise of the independent judgement.

In conjunction with QBE Group and supported by the Remuneration and Nomination Committee, succession planning is undertaken in accordance with the world-class talent objective, which forms part of the strategic priorities of both the Group and QBE Group.

Board Committees

The Boards of the Company and the EO Regulated Entities have jointly constituted Board Committees. The Committees all comprise appropriately skilled members and are supported by attendees as necessary.

The Group's key Committees comprise:

- Audit Committee
- Executive Management Board (EMB)
- Investment Committee
- Remuneration and Nomination Committee
- Risk and Capital Committee

In addition, the following Management Groups operate in support of the above Committees:

- CMG and RCG, accountable to the RCC and the QBE EO Boards
- Disclosure Management Group (DMG), Finance Management Group (including Reserving) (FMG), Underwriting Management Group (UMG), OMG, and Brexit Steering Group accountable to the EMB

Delegation of responsibilities to the Committees and Management Groups is undertaken through Board or Committee approved Terms of Reference which are regularly (at least annually) reviewed.

The membership of the Boards, Board Committees and Management Groups of the Group are regularly (at least annually) reviewed.

The Company and its key subsidiaries has a robust System of Governance which includes Board Charters and Committee and Management Group Terms of Reference; functional Terms of Reference for all Control Functions; a structured Board, Committee and Management Group meetings calendar (with a forward plan of regularly recurring items for review and approval); agendas, minutes and action points for all Boards, Committees and Management Groups; and key Board approved policies and documents including the ORSA, Internal Control Framework, Outsourcing Policy, Fit & Proper Policy and Governance maps. The Board of the Company considers the system of governance to be appropriate in light of the Company's business strategy and objectives.

Key Function Roles and Responsibilities

A description of the main roles and responsibilities of the key functions of the Group are shown below:

Key Function	Main Roles and Responsibilities

Actuarial	• Adhere to sound actuarial policies and procedures
	• Establish and maintain a robust Actuarial control framework to ensure that the Company:
	    • Complies with all material legal and regulatory requirements
	    • Adheres to relevant Actuarial standards and best practice
	    • Meet all internal QBE EO and/or global internal reporting requirements
	• Minimise the risk of business discontinuity
	• Provision of reserving data and analysis
	• Calculation of technical provisions
	• Pricing
	• Benchmarking
	• Portfolio analysis
	• Support for business planning
	• Calculation of capital requirements

Risk Management	• Establishment and maintenance of robust enterprise risk management frameworks • Responsible for the production and performance of the Company's ORSA • Keep track of risks the business faces and ensuring the adequacy of capital should these risks materialise • Support for business planning

Internal Audit	• Evaluate the adequacy and effectiveness of the risk management framework
	• Evaluate management's assessment of risk exposures relating to QBE's governance, operations, and information systems regarding the:
	    • reliability and integrity of financial and operational information
	    • effectiveness and efficiency of operations and programs
	    • safeguarding of assets
	    • compliance with laws, regulations, policies, procedures and contracts
	• Evaluate the adequacy, effectiveness and efficiency of controls in responding to the above risk exposures
	• Evaluate the potential for the occurrence of fraud based and how QBE manages fraud risk

Claims Management	• Ensure the cost effective delivery of an agreed claims service • Implement and maintain effective leading edge practices and processes to provide maximum value to the business and excellent customer service • Work closely with underwriters and other business functions and lead the development of processes to ensure that the function is aligned to the needs of the business • Adopt best practice and meet regulatory requirements • Ensure adherence to the corporate reserving philosophy and claims

Key Function	Main Roles and Responsibilities
	handling philosophy to deliver claims excellence • Support decision making by developing and maintaining effective control reports based on the claims environment and claims activity
Operations	• Implement change programmes related to IT outsourcing, service management, and cost savings to achieve cost, service and scalability targets • Execute and manage the operations strategy of the business • Establish contractual servicing where appropriate, deliver workflow tools and create process efficiencies • Support business planning

Investments	Through the EOIC:
	• Implement and monitor the effectiveness of local investment strategies
	• Monitor investment performance and investment risks, and the use of derivatives (where applicable)
	• Oversee and monitor the effectiveness of the asset-liability strategy with respect to the matching of:
	    • investment assets
	    • the liabilities generated by insurance activities
	• Make recommendations in respect of investment policy, investment guidelines, target returns and asset-liability strategy
	• Support business planning
	Through related support roles and functions:
	• Maintain the investment governance framework
	• Continually review investment guidance, assumptions, policy and process to ensure procedures remain appropriate and meet industry best practice
	• Monitor compliance with all relevant regulation
	• Provide management, regulatory and statutory reporting

Finance	• Establish and maintain a robust financial control framework • Comply with all relevant legal and regulatory requirements • Adhere to relevant accounting standards and good practice • Meet all internal European and/or global internal reporting requirements • Identify and effectively control financial risks (credit, market liquidity, commercial etc.) • Align financial planning, reporting and budgetary controls to corporate goals • Adopt consistent financial processes and/or technologies where appropriate to optimise resources and investment
Underwriting	• Establish and maintain a robust underwriting control framework • Comply with all material legal and regulatory requirements • Adhere to relevant underwriting standards and best practice • Meet internal European and/or global internal reporting requirements • Identify and effectively control their insurance risks • Adopt consistent U/W and Claims processes and/or technologies where appropriate

Legal & Regulatory	• Identify legal and regulatory risks and propose solutions to mitigate
	• Pro-actively monitor and evaluate legal and regulatory risks, emerging/pipeline legal and regulatory developments, alert the business to specific associated risks and extend principles around legal and regulatory risk management into wider business
	• Provide high quality document execution, retention and administrative services to the Boards and business to ensure legal compliance, good internal governance and document control, including:
	    • Corporate and regulatory filings
	    • Issuing corporate certificates as required

<table>
<tr><th>Key Function</th><th>Main Roles and Responsibilities</th></tr>
<tr><td></td><td>Certification of documents and procuring notarisation
Execution of deeds
Ensuring continuing obligations under documents owned by the function are recorded
Ensuring aherence to document retention policies
The main roles and responsibilities of the Compliance function, which forms part of Legal & Regulatory, are further detailed in section B.4
One other key function is the ‘function of effectively running the firm‘, which is undertaken by the EMB</td></tr>
<tr><td>EMB</td><td>Effectively running the firm</td></tr>
<tr><td>Human Resources</td><td>Establish and maintain a robust HR control framework to ensure the Company:
Complies with all material legal and regulatory requirements
Adheres to relevant HR standards and good practice
Meets all internal European and/or global internal reporting requirements
Identifies and effectively controls People risks
Adopts consistent HR processes and/or technologies where appropriate</td></tr>
</table>

During 2016, the following changes were made to the System of Governance:

Structural Changes

- The formalisation of the RCG as a sub-group of the RCC and the adoption of requisite Terms of Reference
- The constitution of a CMG as a formal sub-group of the RCC and the adoption of Terms of Reference
- The update to the Solvency II Steering Group Terms of Reference following approval of the Internal Model and the subsequent dissolution of the Solvency II Steering Group, formally a sub group of the RCC, as all Solvency II related matters are now being considered, as appropriate, by other Committees and Management Groups in the formal corporate governance structure
- The constitution of a Brexit Steering Group as a formal sub-group of the EMB, and the adoption of requisite Terms of Reference

Remuneration

General

The Group, as part of the wider QBE Group, has a remuneration and reward framework and associated governance arrangements. This framework is designed to:

- align remuneration and reward with robust risk management practices and strong governance principles; and
- provide a market competitive remuneration structure that attracts, retains and motivates high quality and talented people whilst aligning their remuneration with the creation of sustained shareholder value

The remuneration and reward framework is regularly reviewed to ensure that it evolves and remains appropriate in the context of:

- QBE Group's vision, values and strategy
- the environments in which QBE Group operates
- QBE Group's business model and geographical exposure
- local market needs and regulatory requirements

Within the framework is a remuneration policy, adopted by the Board of the Group, that is underpinned by QBE's remuneration strategy which integrates the various components of remuneration, reward and risk across QBE Group.

QBE Group's global remuneration framework is intended to apply to all individuals employed by QBE Group to the extent possible and subject to local market conditions and regulatory requirements. An individual will be included if they are employed directly by QBE Group (including any controlled entity) on a permanent or contractual basis.

The Policy is designed to align with QBE Group's risk management framework. Some key components of that framework include:

- the QBE Group Risk Management Strategy (Group RMS) that outlines the principles, framework and approach to risk management adopted by QBE Group and is embedded across the Group providing a consistent approach to managing risk
- an extensive system of delegated authorities that support the structured and measured cascade of risk appetites set by the relevant Boards, empower employees to make decisions within clearly defined risk limits and therefore control the extent to which individuals can commit the current or future assets of QBE Group
- QBE Group policies - employees are required to adhere to a range of policies to ensure risk-taking is well managed, strong governance structures are in place and high ethical standards are maintained

Remuneration Committees

The role of the Group Remuneration Committee is to support the QBE Group Board in overseeing the design and operation of QBE Group's remuneration and reward framework. This includes conducting regular reviews of, and making recommendations to the Group Board, on Remuneration Policy.

A QBE EO Divisional Remuneration Committee is responsible for overseeing the local implementation of the global remuneration and reward framework ensuring compliance with local regulatory requirements.

Principles

The guiding principles which promote robust risk management practices and are applied effectively to manage remuneration and reward across QBE Group are:

ONE QBE values	**Simple**	• at-risk reward methodology is easily understood by internal stakeholders with transparency for external shareholders
	Linked to strategy	• incentive performance measures provide significant alignment and linkage to QBE's key strategic priorities
	Globally competitive	• responsibly competitive when setting fixed remuneration by considering the appropriate market data, diversity and expertise of individual roles and the complexity of each operating environment • common global remuneration design that provides flexibility to calibrate local financial targets, enabling QBE to compete in key markets
	Motivating	• at-risk reward schemes combine 'stretch' targets and performance measures linked to statutory disclosures and business plans, which improves the line of sight and leverages participant motivation • locally competitive and flexible benefits designed to provide value to the employee and QBE
	Shareholder aligned	• achievement of risk-adjusted statutory Group ROE and divisional ROAC targets aligned to shareholder value • delivery of equity awards with significant levels of deferral and financial measures linked to key investor metrics align reward arrangements to shareholder interests • executive minimum shareholding requirements further link executive interests to those of shareholders

Further information on remuneration is available in the 'QBE Group Annual Report 2016', in section 'Remuneration Report', on pages 68 to 102 inclusive.

Material Transactions

The Company declared and paid an interim dividend of £75,000k on the ordinary shares during the year (2015 nil).

The Group and Company monitor their operational net asset positions and hedge material exposures. Foreign currency hedges are affected by physically matching assets and liabilities, supplemented by the use of derivative contracts.

The Group has recognised a foreseeable dividend of £120m in its Annual Submission to the PRA, expected to be paid in Q2 2017.

2. Fit and proper requirements

There is an established Board approved Fit and Proper Policy in place which is reviewed annually and updated as required. The Policy and supporting Guidelines incorporate the requirements of the Senior Insurance Managers Regime (SIMR) in respect of those individuals performing roles and functions within the scope of the Regime.

The Fit and Proper Policy establishes the minimum position required for all Directors and key employees, in particular that:

All directors and employees of the Group should be of good repute and integrity, and possess the requisite competence, knowledge, qualifications and experience to comply on an ongoing basis with all requirements (including regulatory requirements where applicable) relevant to their roles.

Assessment of an individual’s fitness and propriety will include confirmation that they:

- Possess the level of competence, knowledge and experience
- Have the qualifications
- Have undergone or are undergoing all relevant trainingrequired to enable them to perform their role or function effectively, in accordance with all relevant regulatory requirements, and to enable sound and prudent management of the Company

Appointments to the Board, and those otherwise identified as Solvency II staff, are also subject to:

- Confirmation by the Remuneration & Nomination Committee that it is satisfied all relevant internal policies and procedures have been followed
- Meeting the minimum standards set out by the regulatory authority for fitness and propriety and conduct
- Receipt of the regulatory authority’s approval (where applicable)

Collectively, the Fit and Proper Policy, Guidelines and Procedures implement controls around:

- Background checks. These are completed using a risk-based approach. These checks will be completed for all roles within the following categories: Finance, Payroll, defined senior management roles and PRA/FCA controlled functions
- Performance Management Process (appraisals) - continually review the appropriateness of an individual's training and competency to fulfil their role
- Reviews of Board and Committee effectiveness and the Company’s system of governance consider the fitness and propriety of Directors and senior managers

These procedures will, on an ongoing basis, inform senior management of ongoing fit and proper requirements and performance. Key functions are identified in accordance with relevant rules published by the PRA. These include ERM, Compliance, Internal Audit and Actuarial.

Assessment

The Fit and Proper Guidelines detail the processes that have been implemented for establishing an individual's fitness for carrying out a role. This assessment applies to all prospective employees as part of the Group recruitment process and is ongoing throughout employment. Assessment encompasses the person’s previous experience, knowledge and qualifications. A risk-based approach is adopted in all cases and will take into account

- The level of a person’s authority, influence or control
- The reliance of the Company on a person’s role as an internal control (e.g. ERM, Compliance, Underwriting Governance, Actuarial and Internal Audit)

- For Board Appointments, Controlled Functions and other Solvency II staff, the regulatory and/or legal requirements for the role

The frequency of reassessment and specific degree of verification sought will vary according to the person's role and will include seeking regulatory references where appropriate.

The assessment process will encompass a number of stages, namely:

- Pre-employment - with the individual's fitness and propriety assessed prior to commencement of the role
- Review - regularly recurring fit and proper reviews will take place in line with the risk-based approach described above. This will include performance and development reviews as per the current QBE Performance Management Process for all employees and periodic reassessments for directors and those roles which are deemed to also have a significant risk weighting as described above
- Internal moves - where a change to a person's role may prompt a reassessment of their suitability

The Group's Internal Control Functions (Actuarial, Compliance, ERM, Internal Audit and Underwriting Governance) are also required to ensure that they set out and maintain the competencies necessary to deliver the function to an adequate standard.

The framework of controls in this regard may include:

- Appropriate experience and skills mix
- Role profiles
- Training and development
- Centres of excellence (i.e. development of subject matter experts)
- In-sourcing (e.g. joint projects, secondments etc.)

The competency frameworks are subject to ongoing review by the Leadership and Learning department, Compliance, Internal Audit and relevant regulators and form part of the ongoing assessment of the Group's Internal Control Framework.

Where matters affecting a person's suitability are identified, the Group will consider the relevance to the person's role and the circumstances and seriousness of the matter. If a person is not deemed to be fit and proper, disciplinary action may be taken and regulators notified where appropriate.

As outlined above, more rigorous scrutiny is applied in respect of key roles, particularly for Board Directors. The Group recruitment process includes extensive validation of qualifications and references, and comprehensive background checking in all cases.

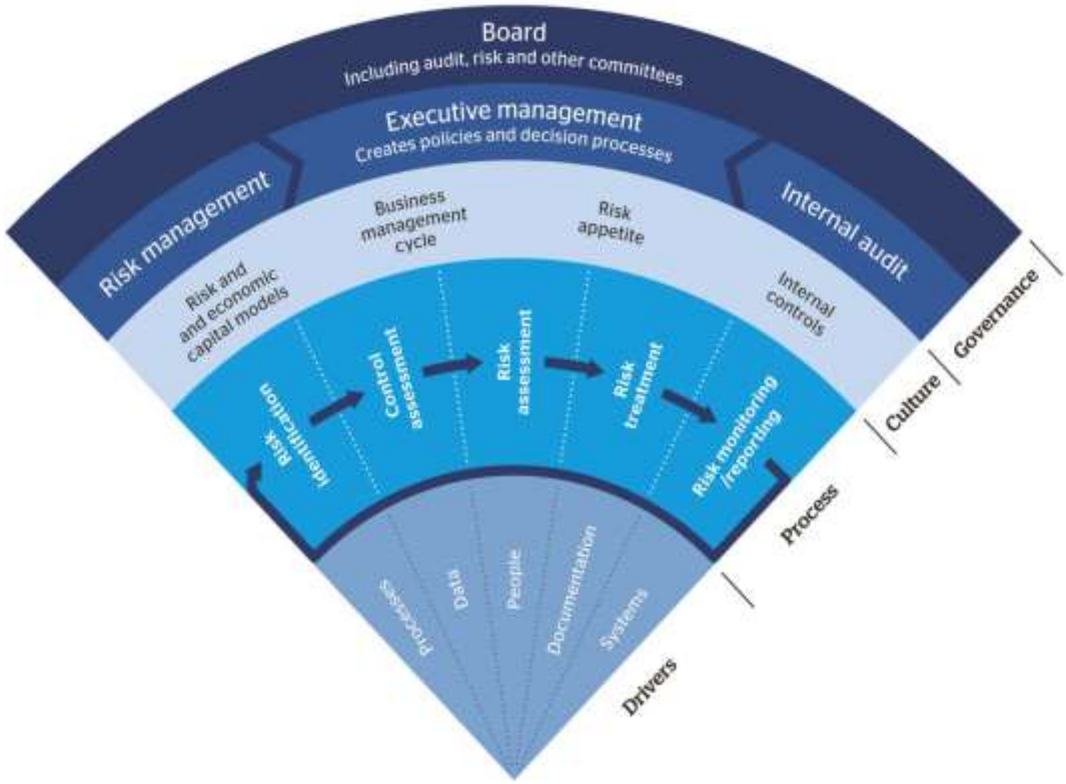
Reviews of Board and key Committee effectiveness and the Group's System of Governance may consider the fit and proper requirements for all Directors in the context of their specific responsibilities as Board members, and the Fit and Proper Policy establishes the minimum requirements for those roles within the Group that are covered by a regulatory regime.

Supervisory approval is required for those individuals with responsibility for effectively running the Company (Senior Insurance Manager Functions (SIMFs) and Controlled Functions (CFs)). These individuals (known as Approved Persons) (and the allocation of prescribed responsibilities to them where applicable) are identified and recorded in the required Board approved Governance Maps. Key Function Holders (KFHs) and Key Function Performers (KFPs) within the business are also identified within the Governance Maps. The rules and principles around

Approved Persons, contained within the FCA and PRA regulations, have been implemented within the Group's Fit and Proper regime for Approved Persons and the Policy and supporting Guidelines have been updated to accommodate the requirements of SIMR alongside those of Solvency II. In practice, all Directors of the Company, the Chief Actuarial Officer, Compliance Director and the Head of Internal Audit are all Approved Persons under the SIMR regime.

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

The Group Risk Management Strategy (RMS) outlines the Group's strategy for managing risk and the key elements of the Group's risk management framework that implement this strategy. It is approved by the Board of the Company and sets out the governance arrangements and key roles and responsibilities relating to risk management and also identifies the key risk processes and reporting mechanisms as outlined below:



Risk categories

QBE identifies and actively manages the risks to delivering on its strategic and business objectives. These risks are then allocated into one of seven categories for aggregation, monitoring, reporting and measurement purposes and are each managed through a specific risk policy. Risk categories and sub categories are formally reviewed on an annual basis to ensure they continue to reflect the key risks faced by the Company. The seven risk categories are as follows:

Strategic risk: the current and prospective impact on earnings and/or capital arising from strategic business decisions and responsiveness to external change.

Insurance risk: the risk of fluctuations in the timing, frequency and severity of insured events and claims settlements, relative to expectations.

Credit risk: the risk of not recovering money owed to QBE by third parties as well as the loss of value of assets due to deterioration in credit quality. QBE's exposure to credit risk results from financial transactions with securities issuers, debtors, brokers, policyholders, reinsurers and guarantors.

Market risk: the risk of adverse impacts on earnings resulting from changes in market factors. Market factors include but are not limited to: interest rates, credit spreads, foreign exchange rates, equity prices and commodity derivatives.

Liquidity risk: the risk of insufficient liquid assets to meet liabilities as they fall due to policyholders and creditors or only being able to do so at excessive cost.

Operational risk: the risk of financial loss resulting from inadequate or failed internal processes, people and systems or from external events.

Group risk: the risk arising specifically from being part of the wider QBE group, including any financial impact and loss of support from the parent company.

Risk Appetite

The Group's appetite for risk sits at its core, across every area of its business. QBE defines risk appetite as "the level of risk that the Board and management are prepared to take in pursuit of the organisation's objectives". It is therefore essential that risk is defined, quantified and supported by a robust risk framework which includes a set of risk appetite statements.

Risk appetite is formally set by the QBE Group and then by the Boards of the Company and all underlying (re)insurance entities within the Group on at least an annual basis and is reviewed following a material change in risk profile.

The Group's risk appetite framework includes both high level appetite statements and more detailed metrics monitored through the Group's governance structure. All breaches of risk appetite are reported to the RCC and Board through the ORSA process.

Risk Culture

QBE defines risk culture as "observable patterns of behaviour in the way employees perform their work, as it relates to risk, and the judgements they take". Risk culture underpins QBE's ERM Framework. QBE's approach to managing risk culture is comprised of three key elements:

- Defining target risk culture – the behaviours and attitudes QBE Group expects from all employees
- Measuring risk culture – using Line 1 self-assessment, Line 2 independent assessment, Line 3 independent assessment and risk culture reporting. Assessments are conducted at least annually
- Influencing culture – the actions and initiatives at an organisational or individual level that are undertaken to either maintain a positive risk culture or to remediate a situation where culture is not operating in line with expectations.

Risk culture metrics are reported regularly to the Group RCC to ensure appropriate escalation of cultural issues and trends.

Internal Model

The Group has developed an Internal Model that can be used to identify and assess risk to ensure that adequate capital is held in relation to the risks faced by the business.

All business lines written within the Group are included within the scope of the Internal Model and are treated in a consistent manner, with differences only arising due to the specific risk profile of the business rather than a different approach to risk assessment. The Internal Model is supported by the ERM Framework, a number of processes within which feed the Internal Model directly as part of the Group's regulatory capital assessment.

There are five key processes that make up the Internal Model:

- Internal Model governance
- Risk identification and emerging risks
- Internal control framework
- Risk assessment
- The economic capital model

Internal Model governance

The high level and detailed governance of the Internal Model is the responsibility of the RCC and the ERM function respectively.

The RCC is a formal committee of the Boards and meets at least on a quarterly basis. The RCC is attended by members of the ERM function to ensure that adequate information regarding the Internal Model is reported to and disseminated from the RCC. A memo outlining the main points of discussion at each RCC meeting is presented to the QBE EO Boards to ensure that matters regarding the Internal Model are documented and escalated to the appropriate forum.

Risk identification and emerging risks

The Group identifies key risks that have the potential to affect the business' ability to achieve its objectives on a continuous basis. Each risk is assigned a risk owner, who is responsible for the overall management of that particular risk. Once a risk has been formally identified and included within the Framework, it then becomes fully integrated into the Group's risk and capital management processes.

Risk identification is carried out through the Boards, committees and the business facilitated by the ERM team, and is also supported by the emerging risks process.

Annual formal Risk and Control Assessments (RCAs) are conducted with all business functions in the Group to identify the risks to the function achieving its objectives, the controls to mitigate these risks, and finally the effectiveness of the controls in managing the risk. The Group has established an Emerging Risk Group, as a sub group of the RCC that identifies and facilitates the effective management of risks that are perceived to be potentially significant, but which may not be fully understood or allowed for in decision making activities.

Internal control framework

An established control framework is in place to ensure that risks are managed to support the achievement of the Group's objectives. The risk management system provides further structure to the control framework, ensuring that risks have the appropriate controls in place with the appropriate owners. Control assessments are validated by the appropriate committee as part of the risk assessment process and are verified through Internal Audit testing.

Risk assessment

Risks are assessed by committees using a combination of qualitative and quantitative techniques. The assessment process brings together key information to support the assessment decision, including key management concerns, stress and scenario tests, key risk indicators, control assessments, loss data and issues and actions.

The Group's risk profile is aggregated and summarised through the ORSA report. The ORSA contains the Group's risk assessments and the control effectiveness rating for each risk within the Framework, including non-quantifiable risks and those not mitigated with capital. The ORSA is considered in conjunction with any breaches of appetite to ensure that the Group can respond quickly to changes in its risk profile and take appropriate mitigating action where required.

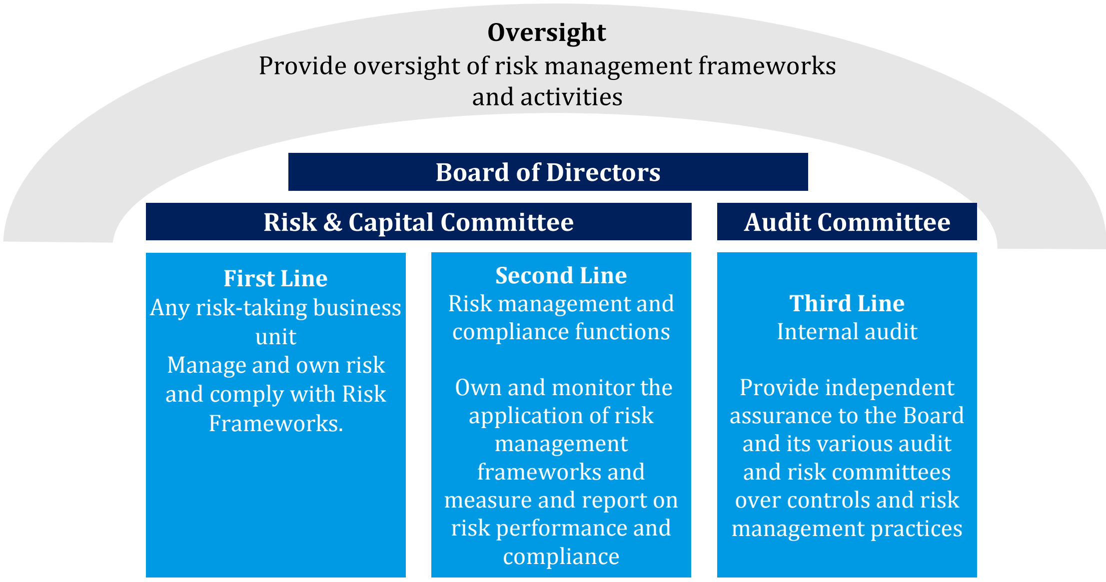
Reporting

QBE's governance framework is supported by risk reporting, which is used to provide complete, accurate and timely risk data and analysis that can be used to support day-to-day business decisions. Key stakeholders for risk reporting include Boards, committees, forums, risk owners, business management and support functions. In particular, risk and performance-related information is routinely reported to the Boards and RCC.

A key element of the Group's risk reporting consists of the ORSA report. This is discussed in more detail on the following pages.

Risk management system

Everyone within the Group has the responsibility for managing risks and as a result a large number of people are involved in the risk management process. QBE's risk governance framework reflects a 'three lines of defence' approach to risk management as outlined in the diagram below:



First line (1a)

Overall first line activities are those which are undertaken within the business to ensure that risks are identified and controlled, regardless of second and third line activities.

First line 1a activities refer to the controls that are implemented by those who are directly responsible for accepting, managing and mitigating risk.

First line (1b)

First line 1b activities are those which review, challenge or provide oversight of 1a risk management activity. Although 1b functions are not fully independent of 1a, they are one step removed from decision making activities and are therefore able to provide an objective view or they may provide a specialist service to 1a such as training or legal advice.

Second line

Second line activities independently review, challenge and provide oversight of first line risk management activities. This is achieved through monitoring controls and ensuring that control verification mechanisms are designed and operating effectively. The second line is independent of first line activities and is therefore entirely objective in its assessment of risk.

Third line

Third line activities evaluate the effectiveness of the organisation's risk management, control and governance processes, providing assurance that both first and second line control and assurance activity is effective and appropriate.

Economic capital model

The Group has developed an Internal Model that can be used to identify and assess risk to ensure that adequate capital is held and informed decisions are made in relation to the risks faced by the business. All elements of the Internal Model involve the consideration of risk and/or capital, and as a result the Internal Model is embedded into the day-to-day operation of the business.

The Economic Capital model is therefore used to support specific business decisions, examples of which include:

- underwriting strategy through the business planning process
- setting regulatory capital requirements for regulated entities
- business unit capital allocation and return on allocated capital targets
- remuneration of staff and executives (based on return on allocated capital)
- information as part of Part VII applications
- reinsurance. e.g. alternative reinsurance strategies consider change in return on capital to maximise potential return / minimise potential losses
- business planning sensitivity testing and acquisition processes
- new products and associated risk and capital requirements
- analysis of proposed changes in the Strategic Asset Allocation of the business
- the ORSA report
- acquisitions, associated risk and capital requirements and purchase strategy

The ERM Function

The primary role of the Enterprise Risk Management function (ERM function) is to assist the Board and its management team in achieving QBE's vision and values by pursuing opportunities and managing risk effectively. The ERM function aims to enrich decision-making to optimise return on capital by delivering an Enterprise Risk Management framework (ERM framework), reviewing and supporting its application and providing independent insight and challenge to the Group's risk assessment and risk management processes.

The ERM function reports to the Chief Risk Officer (CRO), who is a member of the Company Board, the Boards of all EO Regulated Companies and key decision making governance forums. Output from all ERM activities are reviewed by the CRO and are escalated to the RCC and Boards, as appropriate, for review and incorporation into decision making activities.

The Own Risk and Solvency Assessment

The Group has adopted a working definition of the ORSA to be "the entirety of the processes and procedures employed to identify, assess, control, manage, and report the short and long term risks QBE faces or may face and determine the own funds necessary to ensure that the undertaking's overall capital needs (solvency and economic) are met at all times."

A single ORSA is prepared for the Group as this most appropriately reflects the manner in which the Group manages its risks and also the commonality of risk assessment, governance, systems and control processes across its subsidiary undertakings and its Internal Model. This ensures that risk management procedures are implemented consistently across all the undertakings within the scope of the Group.

A single ORSA also provides the Company and EO Regulated Companies with a more succinct report by removing substantial duplication, thereby improving the effectiveness of the ORSA as a decision making tool. The report is reviewed and discussed by the RCG and RCC, both of which in combination contain all the Directors of the EO Regulated Companies, prior to recommendation to the Boards for review and approval. This process ensures that detailed discussion and review can be effected at the level of both individual subsidiaries and the Group as a whole.

Functions that are consistent across the Group include:

- A risk management system which is applied consistently across all trading entities
- Risk assessment processes (e.g. business planning, reserving, exposure management, capital modelling) which are conducted by common functions using a consistent process across all trading entities
- Key systems including Underwriting, IT, HR and Risk Management operate consistently across all trading entities
- Control functions such as Compliance, ERM and Underwriting Governance operate consistently across all trading entities. Where identified control failures are legal entity specific, they are escalated to the appropriate legal entity Board as appropriate
- A consistent Internal Model is operated across the two solo entities and at the level of the Group. Outputs from these models are reviewed by the same governance forums before being reported to the relevant entity Boards

The ORSA provides the link between the Group's risk profile, risk appetites and overall solvency needs and confirms that:

- The risk profile in the context of its business plans and enterprise risk management framework is understood
- The regulatory and economic capital requirements can be met based on the current business plan and over the longer term, taking into account severe events
- Management actions that may be necessary to reduce risk and subsequent capital requirements, (including contingency plans associated with a stressed environment) have been considered
- The Internal Model continues to be considered adequately suitable and robust to support the above assessment of risk and capital, and specifically to set regulatory capital

The ORSA process has been designed to ensure that the Group's Boards will be provided with the relevant risk and capital information they require and at appropriate frequency, to enable them to act in the best interest of their stakeholders. The following describes the key elements of the ORSA process in relation to the production of:

- Regular ORSA updates
- The annual ORSA report
- Ad hoc ORSA updates (as required)

Regular ORSA updates

Regular ORSA updates are run during the year at a Group level and include analysis of:

- Business strategy
- Risk profile
- Areas of management concern

- Financial position and solvency ratios, including under stressed conditions
- The current and projected SCR for each (re)insurance entity
- The ongoing suitability of the Internal Model for capital setting purposes

Although the regular ORSA updates are conducted at the level of the Group, to demonstrate continuous compliance with SII regulations, the solvency position of each of the underlying EO Regulated Companies is also presented.

Annual ORSA

An annual ORSA report is produced for each calendar year for the Group. The annual ORSA report captures changes in the Group's risk profile that have occurred during the previous year and incorporates detailed analysis of the Group's risk and capital position both current and in the future, split by risk type, incorporating all the Group's trading entities.

Ad-hoc ORSA updates

The ORSA is updated quarterly, and therefore the ORSA will only be run on an ad hoc basis outside its normal cycle following a significant change in the Group's risk and capital profile, such as:

- Material acquisitions or business re-organisation
- A significant change in the Group's business plan e.g. entering into new markets, products etc.
- A significant loss event
- Material change in Group's capital base
- Identification of a critical issue

ORSA governance

The ORSA is reviewed and approved as follows:

QBE EO Boards: The QBE EO Boards have the ultimate responsibility for the ORSA. This includes responsibility to review and approve the ORSA report on an annual basis. This constitutes the formal ORSA sign-off.

RCC: The Boards delegate their risk management oversight and monitoring activities to the RCC. The RCC is the primary forum for challenging both the ORSA content and process, approval of the ORSA Policy, quarterly ORSA updates and review and recommendation of the ORSA annual report to the Board for approval.

RCG: The RCG is a sub group of the RCC and consists of the Group's Executive Management Board. The primary responsibility of the RCG is to review and challenge risk related papers prior to submission to the RCC.

Other Committees and Groups: Other Committees of the Boards and Groups also have key roles given their responsibilities to challenge risk information which directly feeds the assessment of risk for the ORSA process. Their responsibilities in relation to risk management are included in the respective committee terms of reference.

The ORSA is integrated within the Group's decision making processes as it incorporates the outputs of a number of key management processes including:

- Articulation of the risk profile, including strategic and business plan setting and monitoring
- Economic capital modelling (to determine the SCR)
- Capital management
- Governance of the Internal Model

In this manner, the ORSA provides the link between the Group's risk profile, risk appetites and overall solvency needs and is reported to the Group's key decision making forums (noted above) to ensure decision/actions are taken where appropriate.

Determination of solvency requirements

The Group uses an Economic Capital Model (ECM), as part of its Internal Model, to measure the material risks to which the business is exposed, including the level of capital required to meet its solvency needs around its future liabilities and to facilitate the Group's strategy. The ECM has been developed to better inform decision making, and to assess the Group's solvency requirements through a deep understanding of business risk profiles.

The ECM is designed to measure the risks faced by the Group as specified in the QBE Group Risk Management Strategy (RMS), and uses the risk management assessment process as the basis. The ECM captures the risks identified in the risk assessment and monitoring process, other than elements of strategic risk which are captured through the ORSA process.

This output is used to assist the Board and senior management in evaluating risk and understanding the capital implications. Use of the ECM has been approved by the QBE EO Boards and PRA following approval of the Group's Internal Model in December 2015.

The strategy for ensuring adequate capital is maintained over time is primarily driven by the risk profile of the Group, the QBE EO Board's risk appetite and applicable regulatory capital requirements. Other relevant strategic and business objectives are also taken into account.

The ECM is a key input for setting the capital adequacy targets, examples of which include the probability of meeting policyholder liabilities and the probability of regulatory capital falling below a level acceptable to the regulator.

The ECM and risk management framework are integrated through the following processes:

- *Decision making*: the use of the ECM in decision making is evidenced within the processes and principles of the risk management framework
- *Capital management*: elements of the SCR are derived directly from the output of both the ECM and risk management processes
- *Risk appetite*: the risk appetite for the entities is directly linked to capital metrics and monitored using outputs from the ECM through the risk management framework
- *Reporting*: the outputs of the ECM are used in the reporting of risk assessments and appetites in the risk management framework. For example the assessment of reserve risk in an entity
- *Operational risk*: the parameterisation of operational risk for the ECM is conducted as part of the risk management process and a direct feed into the ECM.
- *Model risk*: the governance around the ECM is based on the risk management framework principles and concerns regarding the change, use or validation of the model are included in the quarterly ORSA reports to the RCG, Committee and Boards (annual)

4. Internal control system

QBE has implemented an Internal Control Framework and various functional Terms of Reference that reflect how the internal control mechanisms are arranged within the companies to meet all regulatory and legal requirements. The Framework is built around a ‘three lines of defence’ model and is positioned to deliver legal and regulatory minimum standards, i.e.

QBE EO is expected to meet:

The standard required under Article 46 of the Solvency II Directive, the rules contained within the PRA Rulebook, and FCA requirements under SYSC 3.1.1, which state that “a firm must take reasonable care to establish and maintain such systems and controls as are appropriate to its business”.

First Line

The Board, certain Board Committees and Management Groups, underwriting divisions and corporate services (including QBE EO Finance, Actuarial and elements of Legal & Regulatory) collectively form the first line of defence of QBE EO’s risk governance structure in that they have direct responsibility for the management and control of risk.

While the Board has ultimate responsibility for ensuring the existence of an appropriate system of internal control and risk management, senior managers in the Company’s business units will generally have delegated responsibility for:

- identifying and evaluating the significant risks faced by the Company and presenting their conclusions to the Board
- designing and operating the system of internal control and risk management within the policies and parameters defined by the Board
- monitoring the effectiveness of the system and reporting to the Board

Finance

The Finance function is primarily responsible for ensuring the integrity and reliability of financial reporting. Its responsibilities include the preparation of published financial statements, including interim and regulatory returns and other publicly reported financial information. The function is responsible for coordinating the preparation of the Pillar 3 reporting and disclosures required under Solvency II.

Actuarial

The primary responsibility of the Actuarial function is the co-ordination of the calculation of the technical provisions, ensuring that methodologies and assumptions used are appropriate to the line of business, assess the sufficiency and quality of the data provided and compare best estimates against experience.

Operations Management

The OMG oversees the delivery of cost effective and efficient support services to the business, ensuring that such services are fully aligned to business plans and risk strategy.

In particular, the Group monitors, reviews and reports on matters relating to outsourcing and the service performance level of suppliers both directly to the Company and indirectly through the QBE Group global contractual approach (whether provided by intra-group arrangements or from third party service providers). This oversight extends to key service areas including Central Underwriting Support, Claims Operations, Finance Operations, Data Management and Management Information, Human Resources, IT Services, Legal and Procurement.

The Group also has responsibility for confirming annually to the Board that the 'data', 'systems and IT', 'operational risk' and 'documentation framework' elements of the Internal Model are fit for the purposes of assessing capital requirements and, if appropriate, technical provisions; and additionally that there are adequate systems in place for identifying, measuring and mitigating the risks associated with data, systems and IT, operational risk and documentation framework in the model.

Underwriting Management

The UMG reviews and reports to the EMB and Board on matters relating to underwriting strategy, underwriting performance and management, reinsurance arrangements and performance. Specifically, this includes developing and recommending an underwriting strategy to the EMB, reviewing performance and management of underwriting activity, overseeing the performance and use of distribution channels, Claims Management, Aggregate Management, Reinsurance Management, Reinsurance and Underwriting Security, and approving/recommending the cessation of business/Legacy Business Management as required.

The Group also agrees the annual plan of work for the Underwriting Governance and Delegated Underwriting Authority departments, monitors progress in achieving the those plans, receives updates on medium and high risk breaches and material trends, considers the findings of reviews undertaken by both departments and initiates remedial action where required. It also monitors the implementation of agreed recommendations, identifies areas of business risk as they emerge for incorporation into departmental plans and agrees key business controls including minimum underwriting standards and procedures made pursuant to policies.

Further specific responsibilities include confirming annually to the Board that the 'cat risk/realistic-disaster scenarios', 'underwriting gross risk parameterisation' and 'reinsurance programmes parameterisation' elements of the Internal Model are fit for the purposes of assessing capital requirements and, if appropriate, technical provisions; and that there are adequate systems in place for identifying, measuring and mitigating the risks associated with cat risk/realistic-disaster scenarios, underwriting gross risk parameterisation and reinsurance programmes parameterisation in the model.

Second Line

The RCC and its sub-groups (the RCG and CMG), Enterprise Risk Management function and other control functions such as the assurance components of Compliance and Underwriting Governance form the second line of defence in respect of risk governance. They are collectively responsible for the co-ordination, facilitation, oversight and challenge of the effectiveness and integrity of the Framework.

Enterprise Risk Management (ERM)

The ERM function assists in the effective operation of business units and maintains an entity-wide view of risk profile. For the Board and the governance committees it also monitors and provides focused reporting on risk exposures and advise on risk management matters, including strategic, insurance, credit, market, liquidity, operational and group risk.

The ERM framework and the underlying Risk and Control Assessment process provide further structure to the risk and control framework ensuring that risks have the appropriate controls in place with the appropriate owners.
Key features of the process are as follows:

- A formal review of the risks and controls is undertaken on an annual basis and control effectiveness assessed by control owners in terms of control design and performance. These control evaluations exist across all underwriting divisions and the majority of countries within QBE EO as well as for the central functions
- Control owners are also required to identify any material control issues that have occurred in the relevant period
- An overall control assessment is made for the control environment for each risk. This is used as one of the key inputs into the Divisional level risk assessment process
- The overall control assessments are validated by the appropriate committee as part of the risk assessment process
- Control improvements are driven through the risk and control assessment process including the loss event reporting process

Compliance

The core objectives of the Compliance function are to:

- Provide assurance to the Board that regulatory and relevant legal requirements are being met through monitoring activities, knowledge of the business and through regular supply of compliance MI to relevant governance forums
- Promote a robust and consistent compliance culture throughout the business including through on-going training and awareness
- Provide advisory assistance and support to business units on interpretation and impact of; and compliance with, relevant regulatory and legal requirements and obligations
- Monitor regulatory developments and co-ordinate and support business response to proposed regulatory changes
- Develop and embed a framework of policies and procedures designed to support business practices, promote ethical standards and ensure regulatory and legal requirements
- Maintain open and co-operative relationship with regulators and undertake pro-active liaison, including appropriate relevant reporting and responses to deep dive exercises

The function also produces and promotes awareness of the annual Compliance Plan and Compliance Monitoring Plan, and in conjunction with other Group control functions conducts a program of monitoring to challenge and test the effectiveness of internal controls.

Underwriting Governance (including Delegated Underwriting Authority)

The Underwriting Governance Department reports to the Chief Underwriting Officer and undertakes a comprehensive program of reviews and monitoring to ensure that underwriting is conducted in an appropriate manner to deliver agreed business plans, uphold Minimum Underwriting Standards and fulfil all internal and external regulatory obligations.

Third Line

The Audit Committee, External Audit and Internal Audit form the third line of defence in respect of risk governance by providing independent assurance and challenge across all business functions, (including the second line of defence), in respect of the integrity and effectiveness of the Framework.

Internal Audit

The Internal Audit function is primarily responsible for delivering independent and objective control assurance activity and evaluating the adequacy and effectiveness of the internal control system.

Internal Audit is a group-wide function that operates on a globally integrated basis and the divisional Head of Internal Audit reports functionally to the Audit Committee and Group Head of Internal Audit.

This ensures the function is fully independent and it has no responsibility for developing or implementing procedures or systems, except for those related to internal audit. It does not prepare records or engage in original line processing functions or activities and has full, free, and unrestricted access to all QBE activities, records, property and personnel.
The key issues and themes arising from Internal Audit reviews are routinely disclosed to the Audit Committee and senior management.

All Functions

In addition to the specified functions detailed above, the Group relies upon all staff to operate within the internal control framework, with additional controls being:

- A business-wide system of Delegated Authorities (Underwriting, Non-Underwriting and Claims)
- A series of core internal policies and procedures
- Business Performance and Reporting

All of the functions within the Group contribute to informing the internal control framework and ensuring an appropriate degree of oversight, supporting the second line of defence role. The framework also encompasses the Internal Model used within the Group, the key control documents here being the Internal Model Validation Policy, the Expert Judgement Guidelines (and Log), the Internal Model Change Policy, the Data Policy and the Capital Model Overview.

The established Board Charter and Committee and Management Group Terms of Reference provide the Board and the business with a transparent governance structure that clearly identifies lines of reporting and responsibilities.

There are key documents and processes that evidence organisation structure and reporting lines. These are:

- Governance map
- Delegated authorities, providing clear reporting lines and responsibilities
- Key functional Terms of Reference (e.g. Compliance/Underwriting Governance Dept.)

- Information is transferred across the business through the Board, Committee and
- Management Group structure, underwriting management forums, intranet sites and general business forums as well as other groups which regularly meet but which do not fall within the formal corporate governance structure

The Compliance function

The Compliance function consists of three dedicated teams (Regulatory and Advisory; Sanctions and Licensing; and Compliance Monitoring) and reports through the Compliance Director and the General Counsel to the Chief Financial Officer. Collectively, these individuals are members of, and/or report to, the Board and key control committees. They have direct and unfettered access to any member of the Board, senior management and Committees.

The core objectives of the function are set out in the functional Terms of Reference and are shown earlier in this section.

The Compliance Policy outlines the Group's approach to compliance and defines the roles and responsibilities of the Boards, senior management, the Compliance function and business units in achieving a positive compliance culture and effective compliance management. Specifically, the policy details the core day-to-day role of the Compliance function which includes but is not limited to:

- developing, in conjunction with business units, a framework of policies and procedures to support business practices, promote ethical standards and ensure legal and regulatory compliance
- developing, or assisting in the development of, educational and training programs to promote a positive compliance culture and a greater awareness and understanding of the importance of compliance and the Company's legal and regulatory obligations
- providing advisory assistance and support to business units on interpretation and impact of, and compliance with, relevant legal and regulatory requirements and obligations
- implementing an annual Compliance Monitoring Plan (which is approved by the RCC) to test and challenge the ongoing suitability and effectiveness of controls across all relevant risks and business areas
- maintaining and monitoring adherence to a diary system for internal and external reporting deadlines
- monitoring regulatory developments and co-ordinating and supporting the business response to proposed regulatory changes
- maintaining open and co-operative relationship with regulators and undertaking pro-active liaison
- monitoring, assessing and reporting regularly on regulatory risks (via the established Risk and Control Assessment process)
- ensuring that regular compliance management information is supplied to the Board and senior management to enable them to form a reasonable view of the standards of compliance across the business, know whether any material trends or issues have emerged and require redress, and be aware of any regulatory developments that may affect the business

Further specific objectives are also established by the Compliance function annually using a risk-based approach. These are detailed in the annual Compliance Plan and Compliance Monitoring Plan which are reviewed and approved by the RCC and Board. This identifies the key risks that the Company is likely to experience over the coming year and any changes to the function created by specific regulatory developments.

The Board has also asserted its commitment to ensuring that all compliance staff are "trained and competent to enable the function to carry out its objectives". Details of individual member's knowledge and experience are included in the annual compliance plan and competency is routinely assessed and monitored through the internal Performance Management Process (PMP).

In addition to active engagement with market bodies such as the ABI, IUA and LMA as a means of identifying potential areas of change, members of the function regularly participate in conferences, workshops and forums on specific legislative/regulatory developments. The function also routinely monitors legal and regulatory information sources, consultations and official publications to inform risk assessments/gap analyses against proposed changes, co-ordinating and supporting the business response.

The Compliance function has also been designated responsibility for contributing to the assessment and management of 'Improper business practice', 'internal fraud' and 'external fraud' risks on behalf of the Board and works with a number of other key assurance functions including Internal Audit, Legal, Underwriting Governance, ERM and Delegated Underwriting to ensure all significant areas of regulatory risk are addressed.

There is also an established issue reporting process and Guidelines on the identification and reporting of breaches of compliance policies. The reporting requirements include the timely escalation of issues to appropriate senior management or governance bodies at both QBE EO and Group level. The Compliance Director further escalates all material issues to the Board and supervisory body through his regular discussion with the lead supervisors.

QBE EO's governance structure also includes the CMG, which supports the RCC in providing co-ordinated oversight and monitoring of QBE EO's adherence to the Compliance Framework. Key responsibilities include:

- Consideration of new policy requirements and management of existing policies within the Compliance Framework
- Review of relevant policy related management information and reports
- Recommendation of the annual Compliance and Monitoring Plans to the RCC
- Review of Compliance breach and incident reports
- Agreement and recommendation to the RCC of the Conduct Risk Framework

Consideration of relevant Compliance owned risk dashboards including those addressing improper business practices, internal fraud and external fraud.

5. Internal audit function

QBE operates a global internal audit function. The function provides independent assurance that the design and operation of the controls across the QBE Group are effective. The internal audit function operates under a written charter from the Audit Committee, a charter which the Company, as part of QBE EO, has adopted.

The primary role of Group Internal Audit (GIA) is to assist the Board of Directors and senior management in the discharge of their responsibility for the sound and prudent management of QBE. The scope of internal audit is regularly reviewed by the Audit Committee.

The Group Head of Internal Audit is responsible for the GIA and reports functionally to the Audit Committee. The GIA is a group-wide function that operates on a globally integrated basis. The GIA comprises the Group Head of Internal Audit and all of their direct reports. The Group Head of Internal Audit proposes the establishment of a team which has the skills, knowledge and experience to fulfil internal audits responsibilities and ensure the application of due professional care which is expected of a reasonably prudent and competent internal auditor.

GIA's scope is to evaluate and contribute to the improvement of governance, risk management, and control processes. Details of work which may be performed in each of these areas are given below:

- Evaluating the adequacy and effectiveness of the risk management framework
- Evaluating management's assessment of risk exposures relating to QBE's governance, operations, and information systems regarding the:
  - reliability and integrity of financial and operational information
  - effectiveness and efficiency of operations and programs
  - safeguarding of assets
  - compliance with laws, regulations, policies, procedures and contracts
- Evaluating the adequacy, effectiveness and efficiency of controls in responding to the above risk exposures
- Evaluating the potential for the occurrence of fraud and how QBE manages fraud risk

The types of audit activities undertaken by internal audit for the Company are shown in the table below:

Type of Activity	Description
Controls Evaluation	Risk based activities which are planned to assess the key risks and the effectiveness of the key controls in operation.
Follow up audits	Follow up procedures based on a previously issued report or matters. The primary purpose is not to reassess the controls, but to consider whether matters previously reported have been addressed in accordance with the agreed management action plan.
Agreed Upon Procedures	Activities which are undertaken in accordance with an external requirement, often performed in accordance with regulatory requirements.
Health Check	High level review over the key controls and risk management strategies in place.
Project Audits	Assurance activities on change and other initiatives undertaken by the organisation to consider the approach taken to assess, manage and monitor the risk of organisational change.
Special Investigation	Projects and investigations undertaken at the request of management. May be as a result of control failure, error, fraud or other loss.
Advisory	Assignments where the advice or specialist skills of the internal audit function can add value to a management activity. Work is limited to providing input and consulting services as operational management remain responsible for controls design and implementation.

Independence

Independence is essential to the effectiveness of the internal audit function. Internal audit activity must be independent, and internal auditors must be objective in performing their work. Internal auditors must have an impartial, unbiased attitude and avoid any conflicts of interest. The GIA has no direct authority or responsibility for the activities it reviews. GIA has no responsibility for developing or implementing procedures or systems, except for those related to internal audit. It does not prepare records or engage in original line processing functions or activities. The GIA reports functionally to the Audit Committee. The Group Head of Internal Head reports to the Audit Committee at least annually on the organisational independence of the internal audit activity.

6. Actuarial function

Overview

The Actuarial Function is not engaged exclusively in work relating to the Company or subsidiary of the Company but is a centralised function that provides actuarial services for all entities within the Group.

At the core of all actuarial work, mathematical techniques are used to interpret the data that is available. This is collated from a wide variety of sources both internally and externally, including underwriting, claims, reinsurance and financial data.

The role of the Actuarial Function is defined in formal terms of reference.

The following table shows the categories of activity that are in scope of the Actuarial Function.

Activity Category	Summary
Reserving	• Analysis, collation and delivery of reserve estimates • Review and challenge of reserve estimates not produced by the Actuarial Function • Probability of adequacy • Produce ultimates
Technical Provisions	• Calculation of technical provisions by legal entity on a Solvency II basis
Technical Pricing and Rate Adequacy Monitoring	• Pricing and benchmark pricing • Rate adequacy monitoring • Opinion on overall underwriting policy
Support for Business Planning	• Review and challenge of annual Business Plan • Analysis of, and opinion on adequacy of reinsurance arrangements
Performance Monitoring and Miscellaneous Business Support	• Portfolio analysis and reporting • Analysis of actual versus expected performance • Ongoing tracking against Business Plan throughout year to prompt any necessary remediation • Underwriting variability analysis • Ad-hoc analysis of underlying portfolio exposure and experience characteristics to support purchase of reinsurance

Activity Category	Summary
	• Ongoing review of outward reinsurance programmes • Ad-hoc analysis and support for M&A activity
Capital Modelling	• Calculation of capital requirements • Reserve variability • Underwriting variability • Inter-class dependencies
Reporting	• Review and challenge of outputs from other QBE EO functions for inclusion in reports • Produce various internal reports, and to Group • Produce various regulatory reports

The Actuarial Function is free from the external influence of other functions within QBE and the formal terms of reference ensure that reserving analysis is performed independently of Underwriting decisions, which enables objective review and challenge.

Data Self-Assessments

In support of all primary activities, and to provide additional assurance in the completeness, appropriateness and accuracy of all input data received and all data outputs produced, the Actuarial Function will perform data self-assessments in accordance with the Data Policy. This will carried out bi-annually. Results of the data self-assessment, including any issues identified, will be reported in accordance with the standard data management processes.

Validation

As a further layer of assurance in its processes, controls and outputs, the Actuarial Function will perform an annual validation of its activities, typically utilising validation tools such as:

- Reviews of evidence
- Reviews of assumptions
- Benchmarking
- Backtesting
- Sensitivity testing

Internal Business and Governance Forums

Members of the Actuarial Department are members of the relevant internal management and governance forums including:

- FMG
- Data and MI Steering Group
- Business Planning Steering Group
- Rate Adequacy Working Group
- Capital Model Technical Group
- Emerging Risks Group
- Reserve Working Group (RWG)
- Major Loss Review Group
- Claims Technical Group
- Legacy Business Group
- QBE EO Reinsurance Group
- Data Management Group
- Various management meetings such as divisional and claims business meetings

- Attendance and presentations at number of formal committees of the Boards including the Audit Committee and RCC

The Board of the Company does not provide direct feedback on the activities of the Actuarial Function, rather feedback is provided through Committees of the Board (Audit Committee and RCC as above).

Internal Audit

All departments that form the Actuarial Function will be subject to regular internal audits to ensure that the appropriate governance and processes are followed in their operation.

Independent External Review of Reserves

External actuaries are contracted annually to provide an independent reserve review on a central estimate basis. The results will be compared to the Group reserve results and differences discussed. Major differences will be referred to the Reserving Working Group, Finance Management Group and relevant Board sub-committee.

7. Outsourcing

The Group has an established Board approved Outsourcing Policy. The Policy is regularly reviewed and updated where appropriate. The policy details the Company's principles of outsourcing, delineates responsibilities according to business function, provides guidelines regarding the maintenance of the outsourcing register, and sets out the process and requirements for reporting to QBE Group in alignment with the wider Group policy.

The Policy establishes criteria for the recording and management of critical/important outsourcing arrangements, but also requires that the same core principles be applied to all outsourced relationships.

In particular, the Policy states that "the outsourcing of critical or important operational functions shall not be undertaken in such a way as to lead to any of the following:

- Materially impairing the quality of the system of governance
- Unduly increasing the Company's operational risk
- Impairing the ability of the supervising authorities to monitor the compliance of the Company with its obligations
- Undermining continuous and satisfactory service to policyholders

It also establishes obligations around the periodic review of all outsourced arrangements, which will differ according to the nature, scale and scope of those arrangements. The policy requires that that appropriate systems and controls should be in place to manage the outsourcing risk, and sets criteria for the inclusion and monitoring of material contracts on the outsourcing register.

A separate Policy is also in place in respect of Delegated Underwriting/Coverholder arrangements. This details the required due diligence and ongoing monitoring of delegated underwriting arrangements, including assessment of the Coverholder's competence and suitability, regulatory standing and financial strength.

The Procurement function operate a quarterly process to monitor implementation of any key outsourcing agreements and an agreed process and SLAs are in place between Compliance and

Procurement to manage quarterly updates to the outsourcing register.

Critical or important outsourcing

A number of critical or important functions and activities are performed on the Group's behalf by third party providers in accordance with the requirements and principles set out in the Outsourcing Policy:

- Various class of business specific claims handling and loss adjusting services (including investigation and rehabilitation case management);
- These providers are delegated authority to manage claims on the Group's behalf and operate predominantly in the following territories:
  - Australia
  - Canada
  - The European Union
  - South Africa
  - United Kingdom
  - United States
- IT services, including Disaster recovery, IT hosting and data centre services, Infrastructure and operational services, specialist software provision
- These providers are predominantly located in the United Kingdom, though some infrastructure support services are located in India.

Various functions are also outsourced within the QBE Group to a shared services centre located in the Philippines:

- Certain limited claims administration and processing functions
- Financial processing (including basic analysis, internal reporting and administrative reconciliation activities)
- Insurance Administration (including data entry, bordereaux support and some credit control processing)

Additionally, investment management services are also outsourced to the QBE Group Investments Division based in Australia. These are governed by a formal investment management agreement and are subject to ongoing oversight by the Group Investment Committee.

Any such intragroup outsourcings are implemented in accordance with the Group Services Governance Framework and in all cases the Group's Outsourcing Policy is applied in full to ensure a robust contractual framework is put in place.

Delegated Underwriting Authority (DUA) Arrangements

The Group also operates a worldwide network of coverholders which are delegated authority to underwrite business on the Company's behalf. The primary sources of delegated authority business are:

- Australia
- Canada

- The European Union
- UK
- United States

All delegated underwriting arrangements are subject to extensive ongoing oversight and a risk-based control framework which includes extensive due diligence, risk assessment and the ongoing audit and review of coverholder conduct and operations.

8. Any other information

The alignment of the Group's System of Governance and risk management framework to the risks faced by the business is addressed in various sections of this document. In particular, please refer to sections B1(a) and (b), B2, B3(a) and (b), B4 and B7 above.

The Boards of the Company and the EO Regulated Companies were provided with a report on the review of their shared System of Governance for discussion when the Boards met on 1 August 2016. The report considered the changes made during 2015 and 2016 as part of the ongoing review, and continuous improvement, of the System of Governance.

These included the implementation of the SIMR regime and the adoption of Board approved Governance Maps, structural changes to Board, Committees and the Management Groups which support them, updates to Committee and Management Group Terms of Reference and updates to key documents including the Outsourcing policy, the ORSA and Control Function Terms of Reference.

Committee and Management Group reporting templates were also enhanced and an annual report was provided by each Committee to the Board.

Section C: Risk profile

QBE is exposed to various risks and uses a number of methods and techniques to identify, assess, evaluate and mitigate these risks. The main categories of risk are detailed below. The Company uses a number of risk mitigation techniques to mitigate these risks, as described in section B.

1. Insurance risk

Insurance risk is modelled as three separate elements; risk around the proposed underwriting year (underwriting risk), risk around the balance sheet earned reserves (earned reserve risk) and risk around the balance sheet unearned reserves (unearned reserve risk). Each of the risk elements is detailed below.

Underwriting risk

Underwriting risk is the risk that the premiums received for the business written in the year following the model date will not be sufficient to cover future claims and related costs arising from that business. The risk is modelled separately for each class of business and involves an assessment of three main sources:

- The *underwriting cycle and the potential for business to be written at inadequate rates*. This has been based upon the submitted business plans and makes allowance for variability. The data has been reviewed by experts within the business
- The *potential for losses in excess of the business plan* caused by a difference between the frequency and value of assumed claims compared to the frequency and value of actual claims (including inflationary trends). The losses have been split between:
  - **Attritional losses.**
    Historic experience combined with expert judgement is used to parameterise the volatility. Attritional losses are modelled using a gamma distribution
  - **Large losses.**
    The frequency and severity of large loss distributions are modelled separately using negative binomial and generalised pareto distributions respectively. The volatility is based on past experience with expert judgement overlay
  - **Natural catastrophe losses.**
    Catastrophe losses are modelled using a third party catastrophe model combined with QBEs exposure profile. An uplift for catastrophe exposure not catered for by the third party model is also applied
  - *Reinsurance*. Gross large and catastrophe claims are modelled explicitly and are passed through the reinsurance structure. The capital model uses the reinsurance structures that are currently in place to capture both the reinsurance recoveries due and reinstatement premiums payable from the modelled gross losses. Commission and expenses. The commission and expense assumptions are all set consistently with the business plan

Earned reserve risk

Earned reserve risk is the risk that the outstanding claims provisions established are insufficient to cover the future claim payments and associated expenses for loss events which occurred before the balance sheet date. Earned reserve risk is modelled separately for each class of business and claims emerging on the exposures are assumed to follow a lognormal distribution.

To calculate the risk around earned reserves, historic paid and/or incurred triangulations have been analysed using a variety of statistical methods, such as:

- Bootstrapping
- Mack
- Hertig

These statistical techniques are used to project historic variability into the future to estimate the reserving risk for each class of business. A number of adjustments based on expert judgements are then applied to the data to take account of the following risk factors:

- Internal systematic risk, such as data issues
- External systematic risk, such as claims inflation and legislative changes

The Group takes account of, and ensures consistency with, the QBE Group capital allocation model and also makes use of other data available across the QBE Group where that data can improve the accuracy of the variability measure.

The opening reserves used with the capital model are consistent with the technical provision as at the balance sheet date.

Unearned reserve risk

Unearned reserve risk is the risk that the unearned reserve provisions established are insufficient to cover the future claim payments and associated expenses for losses which occur on the unexpired exposures. Unearned reserving risk is modelled separately for each class of business and claims emerging on the exposures are assumed to follow a lognormal distribution. The volatility parameters are derived from the total claims distribution from the underwriting risk section of the model.

Unearned reserve risk is calculated from the latest underwriting risk volatility.

2. Market risk

QBE defines market risk as the risk of fluctuation in the value of investments due to movements in market factors. The company's exposure to market risk arises from movements in investment markets and foreign exchange rates.

Market risk modelling assesses the variability in asset returns, changes in asset values and changes to exchange rates over either a one-year period or a 'to-ultimate' timeframe. The calculation over the one-year period also includes the impact of the change of the discount rate used on the Solvency II balance sheet between the opening and closing liabilities.

The Group adopts relatively conservative investment strategies with the vast majority of assets held in cash equivalents, floating rate notes, government bonds and corporate bonds. The duration of bonds is usually less than three years and the average credit quality is high.

The risk of loss due to default of corporate bonds is considered a market risk. Volatility of the returns on the assets held in the pension fund is considered in the section on pension risk.

The key part of market risk modelling is an Economic Scenario Generator (ESG). The ESG simulates different investment returns for a variety of different asset types and takes account of varying durations and inflation rates (both CPI and wages). QBE uses a market leading 3rd party ESG. A significant amount of work is undertaken by the Group to assess and validate the ESG to ensure it is fit for purpose for the Group and the companies within the Group. This includes making certain overrides to some of the assumptions included within the ESG.

The split of held assets by asset type, on which the current capital assessment is based, are disclosed in the balance sheet reporting template (Appendix A).

Prudent person principle

The Group has a defined approach, risk framework and governance process around the Prudent Person Principle, a principle which states that investments should only be made on behalf of clients that are consistent with the investment decisions that a 'prudent person' would make. The Group's policies are consistent and compliant with this rule.

Restrictions on investments which are set out in specific investment guidelines are primarily based on the PRA's Rulebook and guidance in Supervisory Statements, which gives a sound framework for a prudent approach. Occasionally the Group has applied more conservative limits where this is deemed necessary to better align with risk appetite.

Process

The Boards of the Group delegate their authority to the EOIC, which is comprised of knowledgeable individuals, including at least one non-executive director, to make recommendations to the Boards as to the appropriate investment policy and guidelines for the Group and to take responsibility for the day to day implementation and monitoring of the agreed strategy. All material investment strategy decisions are reserved for the Boards based on recommendations from the Committee.

Day to day management of the investment portfolio is outsourced to specialist investment managers, QBE Group Investments, who are responsible for investing the company's assets. Appointment is formalised in an Investment Management Agreement, which states the terms and conditions applying to the management of company assets including compliance with the Investment Guidelines and Restrictions.

The overall investment objective of the Group is to maximise yield and protect capital through employment of a conservative low risk approach that is set out in detailed Investment Guidelines and Restrictions. The Investment Guidelines and Restrictions address market and credit risks; and are based on local regulatory requirements to ensure that principally all investment assets are admissible for solvency under the Solvency II Directive, the PRA Prudential Rulebook, Supervisory Statements and, where applicable, article 14 of the New York Insurance Department Regulations and the (Canadian) Insurance Companies Act.

The Investment Guidelines and Restrictions, which reflect the Group's strategy, permit the investment manager to procure assets on the basis that they comply with asset specific requirements, such as issuer, credit and asset type constraints. The guidelines and restrictions include detailed limits by asset type, which are aligned to PRA / local regulation, or where appropriate are more restrictive. Derivatives are used for efficient portfolio management and risk reduction purposes, they are not permitted within the guidelines for speculative investment.

The Group's current investment strategy is to hold shorter asset duration compared to liability duration to mitigate interest risk. However duration strategy will gradually change over the next few years to introduce an asset-liability management policy (ALM) that sees the duration of assets move closer to that of (re)insurance liabilities. The average portfolio credit quality for the company's portfolio is AA.

Under the terms of the Investment Management Agreement the Investment Manager is required to adhere to the Investment Guidelines and Restrictions and have the systems in place to monitor the portfolio's compliance with them, reporting any breaches as they occur. Independently, the company obtains security level analysis of the various portfolios at each month end and performs its own tests for compliance. Based on the output findings and the compliance reports from the Investment Manager, a monthly compliance report is sent to the EOIC.

Immediately following a breach, the investment manager is expected to contact the EOIC to ascertain whether or not they should take immediate action to resolve the breach or whether the EOIC will issue a waiver with additional clauses. Waivers are only issued where the additional risk is deemed acceptable and in doing so does not conflict with local regulatory requirements. Where waivers are issued, the breached holdings are monitored against any revised requirements and reported to the EOIC. Waivers are reviewed and re-issued each quarter subject to the approval of the EOIC via delegated authority from the Board.

The Group utilises the expertise of the investment manager in assessing the credit risk of counterparties in which to invest. Credit assessment reports will include detailed information obtained from credit rating agencies, primarily S&P. Exposures through derivatives are included when calculating the company's overall exposure to a counterparty.

Absolute counterparty limits are set for Treasury balances. Treasury financial instruments with the exception of Letters of Credit (LOC) are recorded in the Treasury Management System (TMS), Quantum. Counterparty exposure details are fed from Quantum and combined with investments into a central reporting system, QBE Group Investments, Investment Data Warehouse (IDW), which reports total global exposures to QBE's banking group. Exposure to treasury FX derivatives and LOC are reported in IDW. In addition, there are specific settlement limits in place for FX derivatives relating to volumes executed with the QBE Treasury banking group.

The QBE Treasury team monitors all its counterparty exposures on a daily basis and there is also a pre-deal check of limits. QBE Treasury exposures are also reported in a monthly Treasury Report.

Risk dashboards within the ORSA link risks across the Group, including liquidity, capital and investment dashboards. In addition, all reports from business areas outlining identification and management of individual risks are reported and assessed by QBE committees, in particular the Investment Committee and the RCC.

ALM risks are managed through the Economic Capital Model process, which calculates the capital requirement for the liabilities and assets of the Group based on the inter-dependencies of the insurance risk, market risk, credit risk, liquidity risk and operational risk to which the Group's assets and liabilities are exposed. Various scenarios are assessed as part of the determination of the appropriate level of capital.

An input into the Economic Capital Model is the actuarial assessment of the payment pattern of liabilities for each portfolio within each entity within the Group. These are monitored and formalised by the Group FMG. Whilst there is not an explicit link to the investment strategy, the current focus is on investment grade quality bonds which can be liquidated within three days from request to QBE's internal asset management division.

Derivatives are only used for risk reduction purposes or for efficient portfolio management to reduce interest rate risk, foreign exchange movements and equity price movement, the restrictions on use are outlined in the Group's Investment Guidelines and Restrictions. They are not used for speculative purposes and must be fully covered. Derivatives may be used to reduce or increase exposure as an alternative to transacting in the underlying securities, but such use must not result in gearing of the fund. Derivatives are recorded by Group at a gross level and performance of the derivatives is included in reports submitted to the EOIC on a monthly basis. Ultimately, the success of the derivatives is preserving the value of the investment portfolio against adverse movements in markets. The exception is foreign exchange where the Group's investment strategy is to eliminate foreign exchange gains and losses.

Application of the prudent person principle to market risk

The Group's investment philosophy is to protect the value of capital with a focus on gaining exposure to assets that are capable of producing a consistent and recurring flow of income over time, that also meet internally-set targets.

The Group mitigates the level of market risk using the following:

- Active asset management
- Diversified portfolio
- Hedging of net asset exposures

The Enterprise Risk Management (ERM) function reports on the adherence to the market risk appetite statements to the RCC on a quarterly basis as part of the ORSA process.

The CFO reports the following information to the Investment Committee on a quarterly basis:

- ESG modelled risk evaluation and probability of scenario outcome under certain stress tests via risk dashboards
- Detailed investment performance and market information including modified duration, spread duration, return versus business plan at an asset class level, asset distribution data and compliance versus the Group's Investment and Regulatory Guidelines

Foreign Exchange

A report on the foreign exchange position of the Group is provided by the CFO on a quarterly basis through the CFO FX Memo to the FMG. This report outlines movements in foreign exchange and the corresponding impact on operational results and the foreign exchange translation reserve (FCTR). The report also outlines major currency exposures.

3. Credit risk

Credit risk is the risk that losses will arise in respect of either reinsurance recoveries, due to default by a reinsurer, or premiums, due to default by a broker. The credit risk arising from reinsurer defaults is much more material than the credit risk arising from broker defaults. Losses arising from the default of corporate bonds are considered in the market risk section.

Reinsurance credit risk

Credit risk arising from potential defaults by reinsurers is modelled from two sources as set out below:

- Credit risk on reinsurance recoveries arising from future business. The capital model underwriting module for reinsurance protections considers each individual layer on each programme in force. The model includes the participation of each reinsurer on this business, and therefore at any point within the model, it is possible to calculate the aggregate reinsurance recoverable attributed to any one reinsurer. Credit risk percentiles, used by QBE for assessing reinsurance bad-debt provisions, are applied according to the Standard and Poor's rating of that particular reinsurer to generate the potential for a reinsurer to default on recoveries that are owing to the company (note that these include allowance for the risk of downgrade of a reinsurer over time by using more than single year default probabilities). These default probabilities are linked between reinsurers, so one reinsurer defaulting makes it more likely that other reinsurers will default. There is also a link between the catastrophe losses incurred by the entire QBE European Operations and the default probabilities, making it more likely for reinsurers to default when there is a large natural catastrophe
- Credit risk on the existing reinsurance asset. The model includes the amount of reinsurance recoveries due from each reinsurer at the outset of the model. Combining this with the payment patterns for each class enables, at any point within the model, the calculation of the aggregate reinsurance recoverable attributed to any one reinsurer assuming a constant proportion of recoverable with each reinsurer is maintained. The modelling of potential credit risk then follows the same approach as for future reinsurance recoveries above. Thus if a reinsurer defaults the impact on both the current reinsurance asset and the future recoveries can be modelled thereby ensuring appropriate dependencies between the credit risks on past and future business

Premium credit risk

The approach to modelling broker credit risk is very similar to the approach used to model reinsurer credit risk. The brokers are initially divided into groups, default probabilities are selected for each group, loss given default distributions are selected and the resulting credit losses are simulated.

Application of the prudent person principle to credit risk

The Group defines credit risk as the risk of default by borrowers and transactional counterparties as well as the loss in value of assets due to deterioration in credit quality. The Group's exposure to credit risk arises from:

- Reinsurance counterparty credit and other recoveries
- Premium and other counterparty credit
- Investment counterparty default

The Group has an appetite for credit risk to the extent that accepting this risk allows it to optimise the risk-adjusted investment return. The Group has limited appetite for large losses from counterparty failures.

The Group mitigates credit risk using the following:

- Exposure limits for approved counterparties in relation to deposits and investments

- Maximising placement of reinsurance with highly rated and regarded counterparties and limiting concentration of exposures
- Exposure to investment counterparties is regularly monitored against limits set out in the Group Investment and Regulatory Guidelines

Reinsurance counterparty

Counterparty monitoring is conducted on a regular basis through dedicated systems and procedures to manage and control exposure to reinsurance counterparties.

First loss exposure and Realistic Disaster Scenario (RDS) by reinsurer and (Reinsurance debtors and recoveries) RIDAR are monitored on an ongoing basis.

Financial information and external ratings are monitored on an ongoing basis and QBE Group ratings are reviewed and updated as appropriate. A formal quarterly review of ratings is also conducted by the Group Security Committee.

Premium and other counterparties

The Group regularly reviews receivables, the collectability of these debts and the adequacy of associated impairments. Outstanding premium debtor balances are monitored by the credit control teams on a monthly basis, as a minimum. Concentration risk is also monitored for large brokers.

Broker balances are monitored on the basis of uncollected debt and debt outstanding in excess of six months. Debt over three months is pursued at an individual item level. Debt overdue by 12-18 months is allocated a bad debt provision. Brokers are also subject to due diligence.

4. Liquidity risk

The Group defines liquidity risk as the risk of insufficient liquid assets to meet liabilities, as they fall due, to policyholders and creditors.

The Group ensures that a minimum percentage of consolidated investments are held in liquid, short-term money market securities to ensure that there are sufficient liquid funds available to meet obligations to policyholders and other creditors, as they fall due.

In addition, there is a continual flow of inward premiums. Further, capital is held to cover unforeseen adverse situations. Hence, liquidity risk is considered to be small.

The Group mitigates liquidity risk using the following:

- Holding minimum levels of liquid, short term securities
- Asset/liability matching of major currency positions

Results of liquidity stress tests are reported on a regular basis to the FMG through the Liquidity Risk Dashboard.

Regular monitoring of the ratio of liquid assets to liabilities is undertaken via the Group's Risk Appetite Statement, the output of which is reported to the Investment Committee and RCC on a quarterly basis.

5. Operational risk

Operational risk relates to unexpected losses relating to people, processes, systems and external events that are not included within the budgeting process.

Operational risk is a significant risk in the capital model, albeit one that is notably less important than underwriting and reserving risks.

Operational risk is of similar magnitude to credit risk and is modelled using the following seven sub categories:

- Internal fraud
- External fraud
- Employment practices
- Improper business practice
- Disaster and other events
- Technology and infrastructure failure
- Business and transaction processing

Each sub-risk is modelled using a compound distribution with a frequency and severity element. The frequency distribution is modelled using a Poisson distribution and the severity distribution is modelled using a lognormal distribution.

The input parameters for the model are set through the Total Risk Assessment (TRA). The output from this process is, for each sub-risk category above, a frequency and lognormal distribution of operational risk loss amounts.

The input parameters for the model are estimated in the TRA process for all entities within the Group and allocated at an entity level using a weighted average of net reserves and premiums for the entities. For external fraud, improper business practice and business and transaction processing, the frequency parameter is allocated by entity but the severity parameters are unchanged. For internal fraud, employment practice, disaster and other events and technology and infrastructure failure the frequency parameter is left unchanged and it is the severity which is allocated by entity. This reflects the fact that internal fraud, employment practice, disaster and other events and technology and infrastructure failure events are likely to impact all entities within the Group simultaneously whereas external fraud, improper business practice and business and transaction processing events may impact only a single legal entity.

The distributions for each sub-risk are then aggregated assuming independence to determine the overall operational risk distribution.

The expense and claims amounts in the business plan include allowance for small day to day operational risks. As the insurance risk modelling is consistent with the business plan, an allowance has already been made for smaller operational losses and there is a danger of double counting these losses. In order to avoid this, all operational risk losses below the 80th percentile have been set to zero.

Operational risk losses are assumed to be in local currency and take place in the first model year.

Application of the prudent person principle to operational risk

The Group defines operational risk as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events, including legal risk. The Group’s exposure to operational risk arises from internal and external fraud, employment practices, improper business practice, technology and infrastructure failures, and business and transaction processing.

The Group recognises that certain operational risks are unavoidable and arise from a multitude of areas across the entire business. The Group seeks to limit exposure to operational risks through ensuring that an effective infrastructure, robust systems and controls and appropriately experienced and qualified individuals are in place throughout the organisation.

The Group mitigates operational risk using the following:

- Active monitoring of key processes
- Scenario reviews to identify and quantify potential exposures for mitigation
- Effective segregation of duties, access controls, authorisation and reconciliation procedures

The Group uses a number of key processes to monitor operational risk, as follows:

Total Risk Assessment Process

The Total Risk Assessment brings together key risk assessment information for each of the Group's operational risks, both at an extreme level (scenarios) and over the business planning period (Risk and Control Assessments).

Risk Control Assessments

The first line undertakes regular assessment of their operational controls. The results of these assessments are reflected in RCAs and audit reviews. Control assessments are designed to evaluate the effectiveness of controls in terms of their design and operating performance. Weaknesses, issues or opportunities to improve controls are captured by the issues and actions process and tracked through the Risk Management platform, infoRM.

Scenario Analysis

Scenario analysis is a tool within the risk management framework that builds upon loss reporting and the RCAs and is used to identify unexpected, low-frequency, high-severity operational risk events.

Key Risk Indicators

The Group monitors its risk through KRIs, defined as "metrics that inform users about changes in the frequency or consequence of a risk." These changes may require action to manage the risk level back within operational risk tolerance.

Internal Loss Events

The RCA process identifies expected operational risks. The ILE process applies to operational risks that have materialised, i.e. events.
QBE classifies ILEs into three categories:

- actual loss events
- events that lead to fortuitous gains
- near-misses

A key component of the ILE process is event recording. The Group records ILEs with a financial impact of £10,000 or greater within a risk management system. A loss exceeds this threshold if the total loss prior to recoveries exceeds £10,000.

On a quarterly basis, the ERM team collates internal loss data with analysis and reports this to the RCC.

6. Other material risks

The other material risks to which the Company is exposed are detailed below.

Group Risk

Group risk is the risk of financial or reputational damage to entities within the Group from being part of the QBE Group and Lloyd's of London. This includes potential default on inter-company loans. Note, however, that group risk excludes Equator Re reinsurance credit risk that gets incorporated in the credit risk assessment.

Group risk has little impact on the overall capital. The assessment of group risk is based on the following scenarios which are identified as most significant group risks within the Group and, in aggregate, representative of the overall group risk.

- A group company conducts business unlicensed/in breach of conduct rules in the name of another group company
- Failure of other QBE entities to pay dividends on the loan from the Group financing companies
- Action taken in another division of QBE Group causes S&P to issue a one notch downgrade, from A+ to A
- Action taken in another division of QBE Group causes S&P to issue a two notch downgrade, from A+ to A-

These scenarios emerge from the Group Risk Dashboard which identifies the material group risks. The FMG are responsible for the Group Risk Dashboard and have specific responsibilities for assessing and validating group risk assessments. Each scenario is modelled as a binary event and assumed to be independent.

Pension Risk

Pensions risk captures the risk of adverse balance sheet movements associated with the defined benefit pension schemes. The Group bears the economic and demographic risks associated with these schemes.

The Group's subsidiaries operate four defined benefit pension schemes. The Iron Trades scheme relates to certain employees of QBE Insurance (Europe) Limited; the Janson Green scheme relates to certain employees of QBE Underwriting Limited; the QBE Re (Europe) Ltd Pension & Life Assurance Plan relates to certain employees based in Ireland; and the Secura NV scheme relates to certain employees of the Belgium branch of QBE Re (Europe) Limited.

The UK and the QMIL schemes are run independently of the sponsoring company by scheme trustees, and are subject to the relevant local legislation.

The QBE Re scheme is funded by the employer via group insurance contracts with KBC, a Belgian insurance company.

Pension contributions relating to each scheme are assessed in accordance with the advice of independent qualified actuaries in order to spread the cost over the service lives of employees.

The Group also operate defined contribution pension schemes. The risk associated with these schemes are borne by the employee. Hence, the associated risk is not considered in the capital model.

As at 31 December 2016, the amounts recognised in the Company's accounts for defined benefit plans is as follows:

	Fair Value of Pension Assets (£'000)	Present value funded obligations (£'000)	Surplus / (Deficit) (£'000)
Defined Benefit Schemes	404,804	408,661	(3,857)

7. Any other information

The Group has no material risk transfer to special purpose vehicles.

Concentration Risk Management

Reinsurance

The Group uses a range of well rated reinsurance providers. The regulated entities in the Group have reinsurance exposures with Equator Re, an internal captive of the QBE Group.

To mitigate this risk, the Group has $250m of collateral backing the exposure to Equator Re.

To manage the counterparty concentration risk the Group operates under guidelines set down by the QBE Group Security Committee (GSC). Within those guidelines distinction is made between the length of tail of the exposure of the underlying business portfolio (short, medium and long tail), with the aim to match the best security to the longer tail exposures. The GSC will assign length of tail definitions to each portfolio using a mixture of actuarial analysis and expert knowledge. Any use of a reinsurer outside of the guidelines must be approved by the GSC prior to use, any unapproved use of a reinsurer is reported to both local and Group Boards.

The guidelines also contain recommendations in respect of the maximum cumulative exposure that should be ceded to a single reinsurer. The GSC will further assess, using the expert judgement of the committee members, whether the actual exposure ceded is acceptable and will make recommendations accordingly. Any use of a reinsurer that exceeds the recommended level of use that has not been approved by the GSC is reported to both local and Group Boards. The Group uses a reinsurance reporting system to monitor and report on the concentration of risk. The system holds details of all reinsurances purchased by QBE from 2003 onwards.

The GSC guidelines also contain provision for the assessment of the accumulated exposure potential due to possible contagion lines.

At the first Group Security Meeting of each year the reinsurer exposures are reported on and approved by the committee. At the second Group Security Meeting of each year the RDS reinsurer exposures are reported on and approved by the committee.

Catastrophe

The Group has material exposure to natural catastrophe events. Extensive monitoring of aggregates and reinsurance are in place to control this risk.

A variety of methodologies are used to monitor aggregates and manage catastrophe risk on a gross, net and final net basis and can be evidenced in the UMG Terms of Reference, as well as the other evidence documents.

Methodologies include:

- The use of catastrophe models from third party vendors such as RMS
- Realistic disaster scenarios (RDS) - which may be property related events (e.g. windstorms and earthquakes), but can also be liability based events such as a collapse in the housing market
- The QBE Group aggregate methodology (GAM)

The output of each is monitored and measured internally against internal limits which are allocated aggregate limit as delegated by Group to the Chief Executive Officer and any external thresholds specified. The outputs are reported via a number of control processes, in particular, via reports to the Aggregate Management Group, through to the UMG which supports the Executive Committee. This risk is reviewed at a summary level via the Exposure Management risk dashboard. In addition, catastrophe risk is reviewed at Group level via the Group Aggregate Management Committee (GAMC).

Specific details from the evidence includes:

- Aggregate Management Group terms of reference set out their responsibilities for monitoring catastrophe risk; monitor material movements in key RDS gross exposures on a monthly basis, review RDS methodologies and the validity of PML factors used, review key parameters from modelling output on at least a quarterly basis, monitor the utilisation and allocation of aggregate limits across the Group on a quarterly basis, review data submitted to QBE Group for aggregate monitoring purposes, monitor the impact of changes to the reinsurance programme on RDS and aggregate limits
- UMG terms of reference sets out their responsibilities for monitoring aggregates; monitor aggregate accumulations across all classes of business, review and recommend to the Board Realistic Disaster Scenario (RDS) calculations on both a gross and net basis, and monitor the accumulation of Maximum Event Retentions (MERs) across the Group and report on changes as applicable

Investments

The Group’s asset holdings are relatively diverse by asset provider, asset type and currency. The maximum exposure to a single counterparty (excluding sovereign debt) is less than 5% of funds under management.

The Group's Investment Guidelines and Restrictions identify issuer constraints for fixed income securities and each of the growth asset classes introduced through the strategic asset allocation model. These limits focus on the counterparty itself as well as the ultimate counterparty, credit quality and overall asset class.

Limits are monitored on a day-to-day basis by the fund manager; a breaches memo is produced and sent to the Group from the Group Investments Risk and Compliance department each month. An escalation process is in place to ensure that any investment breaches are subsequently communicated to the Group’s Investment team who are then responsible for investigating the breach on behalf of the Group’s Investment Committee. The Group Investment function also perform independent monthly verification of compliance within investment portfolios. A summary compliance report is circulated each month to the Investment Committee and related interested parties.

The Group’s guidelines with respect to fixed income securities and growth assets are aligned to PRA regulations. Growth asset exposure is aligned to Board appetite and approved Board exposure limits. These limits are set using market and capital criteria e.g. maintaining a realistic margin of capital, liquidity considerations and related risk / reward ratios. It is usual to seek PRA ‘No Objection’ clearance when introducing major changes to the asset allocation model and this will include sharing proposed limits.

Whilst no specific industry sector restrictions are applied by the Group, concentration is monitored at the Group level via a Market Risk dashboard which is submitted to the EOIC on a quarterly basis.

The QBE Treasury function also monitor treasury managed assets against a counterparty limit report, issued by QBE Group, on a daily basis.

Risk sensitivity

As part of the validation of the Internal Model extensive stress and sensitivity testing is performed around all of the risk types. The 1 year SCR is examined resulting from a range of sensitivities applied to the input assumptions.

Scenario analysis is used to help validate the overall level of capital and the following three approaches have been considered:

- Reverse stress testing. A series of 'extreme' reverse stress tests are already conducted within QBE and this considers their impact in relation to the capital distribution calculated as part of the Internal Model
- Scenario analysis. This is an extension of the reverse stress testing but considers a specific scenario, covering multiple risk types, to test the modelled level of capital
- Return periods of diversified capital by risk type. The diversified capital by risk type has been compared against the undiversified risk distributions

Section D: Valuation for Solvency Purposes

1. Assets

The Company's holds total assets of £8,156,092k at 31 December 2016 valued on a Solvency II basis. The table below shows the split of assets by asset class.

	Value (£'000)
Corporate Bonds	3,010,356
Government Bonds	987,509
Collective investment undertakings	444,769
Holdings in related undertakings	1,180,675
Other loans and mortgages	83,150
Collateralised securities	422,613
Deposits other than cash equivalents	78,974
Other investments	22,591
Total investments	**6,230,637**
Reinsurance recoveries	834,285
Insurance and intermediary receivables	256,064
Receivables (trade not reinsurance)	308,417
Reinsurance receivables	112,851
Cash and cash equivalents	144,163
Other assets	269,673
Total other assets	**1,925,453**

A full Solvency II balance sheet is included in Appendix A.

Investments

Day to day management of the investment portfolio is outsourced to specialist investment managers, QBE Group Investments, who are responsible for investing the Group's assets.

Valuation of the Group's investment assets is delegated to QBE Group Investments via a formalised Investment Management Agreement. QBE Group Investments employs the services of external pricing vendors; Interactive Data (Australia) Pty Ltd (IDC) and Bloomberg L.P.; IDC is the primary source of pricing, with Bloomberg utilised as a secondary or alternative vendor.

Valuation methods

The Solvency II valuation bases for investments and for other assets held by the Group are detailed in the table below:

Balance sheet item	Valuation in Financial Statements (£'000)	Valuation for Solvency Purposes (£'000)	Comparison of Solvency II Valuation Basis with IFRS	Solvency II Valuation Basis and Asumptions
Goodwill / Intangible assets	216,024	-	Under IFRS purchased goodwill is recognised as an asset and valued as the difference between the fair value of the asset(s) acquired and the consideration paid for those assets.	Solvency II regulations require that no value is ascribed to purchased goodwill.
Deferred acquisition costs	289,072	-	Deferred acquisition costs are valued at nil under Solvency II as all cash-flows arising from expenses that will be incurred in servicing recognised (re)insurance obligations over the lifetime are taken into account in the Solvency II technical provisions.	Solvency II regulations require that no value is ascribed to DAC.
Holdings in related undertakings	-	1,180,675	The valuation basis differs under Solvency II in respect of the treatment of entities within the group.	Regulated entities are fully consolidated under Solvency II, the starting point for which is the IFRS balance sheet. For participations in non-regulated undertakings carrying out financial activities and other related undertakings are valued based on the adjusted equity method. Holdings in other related undertakings are therefore required to be valued based on the share of net assets (valued at the amount for which they could be exchanged, transferred or settled between knowledgeable willing parties in an arm's length transaction held by the participating undertaking)
Government Bonds and Corporate Bonds and Collateralised Securities	7,443,740	4,420,478	The valuation basis is the same as IFRS except that accrued interest is included in the asset valuation in the Solvency II balance sheet.	Sovereign bonds - Mark to market in an active market • Sovereign government bond prices are quoted on a regulated bond market/exchange. Regional or Municipal bonds – Mark to market in an active market for similar assets • Debt issued by municipal / regional governments (semi governments) and authorities, along with supranational institutions are valued using prices quoted in an active regulated bond market, or in the case of less active markets securities will be priced using broker quotes, local exchanges / central banks or other valuation models Short term treasury bonds (discounted securities) • Issued by sovereign governments are valued using an external pricing source, where a price is not available a value may be calculated using a Bloomberg yield curve utilising observable input

Balance sheet item	Valuation in Financial Statements (£'000)	Valuation for Solvency Purposes (£'000)	Comparison of Solvency II Valuation Basis with IFRS	Solvency II Valuation Basis and Asumptions
				Common corporate bonds (including agency bonds and covered bonds) • Are valued using prices quoted in an active regulated bond market, or in the case of less active markets, securities will be priced using broker quotes • Money market instruments (accumulating certificates of deposit, and discounted securities) are valued using an external pricing source, where a price is not available a value may be calculated using a Bloomberg yield curve utilising observable input
Equities and Investment funds	-	458,667	Equities The valuation basis is the same as IFRS. Investment funds The valuation basis is the same as IFRS.	Equities Mark to market in an active market • Listed equities (including equity trusts and ETF's) are valued according to quoted prices in active markets. Investment funds CMT – Mark to market in an active market Unlisted property trusts and others - Mark to market in an active market for similar assets • Cash managed trusts, emerging market debt and high yield debt CIS (listed and unlisted) are valued as per the current unit price, which is derived from underlying fund securities being priced as per government and corporate bonds above. In the case of unlisted property trusts, fair value is determined by using the current unit price as advised by the responsible entity, trustee or equivalent of the investment management scheme. Year-end valuations are supplemented by independent third party valuations being carried out on the underlying property portfolio. Due to the timing of data released from the scheme, period end valuations are one quarter in arrears.
Derivatives	26,461	8,693	The valuation basis is the same as IFRS. However, in the Statutory Accounts some grouping of positions is carried out. In contrast, in Solvency II every derivative position is recognised separately. Hence, the value of the derivative assets and liabilities may differ between the two bases. The net position is the same.	Investment derivatives (equity and fixed income) are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently stated at fair value using Exchange quoted prices obtained from an external pricing vendor

Balance sheet item	Valuation in Financial Statements (£'000)	Valuation for Solvency Purposes (£'000)	Comparison of Solvency II Valuation Basis with IFRS	Solvency II Valuation Basis and Asumptions
Loans and mortgages	-	83,150	The valuation basis is the same as for IFRS except that accrued interest is included in the asset valuation in the Solvency II balance sheet.	Mark to model. Infrastructure loans are valued using quoted prices if available; observable prices if known or carried book value (par plus accrued interest).
Cash and cash equivalents and Deposits other than cash equivalents	320,602	223,137	The valuation basis is the same as IFRS.	<u>Cash equivalents</u> Measured at fair value, taking into account the risk that amounts due will not be paid (default or credit risk of the counterparty) based on the rating of the bank counterparty. Cash current accounts (including collateral and futures margin accounts) are stated as the reconciled general ledger balance. Term deposits and overnight accounts are valued at par plus accrued interest. <u>Deposits other than cash equivalents</u> Measured at fair value.
Reinsurance recoverable (Reinsurers' share of technical provisions)	2,869,687	834,285	The Best Estimate in the Solvency II balance sheet is calculated in accordance with Article 77(2) of the Solvency II Directive.	Further detail on the valuation of technical provisions is included in section D.2 of this document.
Reinsurance receivables	132,260	112,851	In the Solvency II balance sheet reinsurance receivables comprising cash flows relating to future premiums are taken into account in technical provisions.	Premiums receivable from insured parties in relation to incepted contracts.
Insurance and intermediaries receivables	1,253,072	256,064	In the Solvency II balance sheet insurance receivables comprising cash flows relating to future premiums are taken into account in technical provisions.	Premiums receivable from insured parties in relation to incepted contracts.
Receivables (trade, not insurance)	1,553,997	308,417	The valuation basis is the same as IFRS. Under Solvency II accrued interest has been re-allocated across Solvency II investment lines.	Measured at fair value. For assets with a short-term maturity, the IFRS valuation basis is considered a close approximation to fair value. For other assets, the maturity and recoverability of those receivables will be taken into account when assessing fair value.
Any other assets, not shown elsewhere	217,435	269,673	The valuation difference relates to the change in the value of deferred tax, caused by the impact of adjustments made to balance sheet items in compliance with Solvency II regulations.	

2. Technical provisions

The Group's Solvency II technical provisions amounted to £3,715,364k at 31 December 2016, after adjusting for the reinsurance recoverable amount.

Technical provisions are defined as the probability weighted average of future cashflows, discounted to take into account the time value of money [considering all possible future scenarios]. The key components of the technical provisions comprise:

- Claims provisions: Best Estimate of future gross and reinsurance claims, premium and expenses relating to the earned exposure on insurance policies
- Premium provisions: Best Estimate of future gross and reinsurance claims, premium and expenses relating to the unearned exposure, i.e. based on unearned premium and policies that are bound but not incepted (BBNI) at the valuation date
- Risk margin: additional provision to bring the Best Estimates to the level required to transfer the obligations to a third party undertaking[1]

A quantitative breakdown of the technical provisions, split by Best Estimate liability and Risk Margin, for all Solvency II lines of business, is available in the SFCR documents (Appendix A, QRTs S.12.01 and S.17.01) for the regulated entities QBE Insurance (Europe) Limited and QBE Re (Europe) Limited.

The Best Estimate liabilities are calculated in accordance with Article 77(2) of the Solvency II Directive. The claims and premiums provisions are derived from the IFRS Best Estimate reserves and the unearned premium reserve respectively, and are adjusted to incorporate the following:

- Future premiums: Represents cashflows relating to future premiums, i.e. receivable but not overdue. These cashflows are reclassified from the IFRS balance sheet to technical provisions
- Bound but not Incepted (BBNI) policies: Represents premiums, expenses and claims relating to policies that the Group has entered into that have not incepted at the valuation date
- Future claims costs: Unearned claims are obtained by applying unearned loss ratios to unearned premiums
- Expenses: Assumed expenses incurred in servicing (re)insurance obligations are derived using expense assumptions provided by the Finance Department. These expense loadings are applied separately to the earned and unearned future cash flows to obtain separate expense provisions for earned and unearned business
- ENIDs: The Directive requires the Best Estimate to include allowance for "all possible outcomes", e.g. latent claims or extreme high severity, low probability claims. An ENID provision is calculated to allow for all possible scenarios where historical data may be lacking. ENIDs are calculated by using a statistical approach, taking the 5% tail from the lognormal distribution consistent with the variability assumptions in the Internal Model
- Discounting: Article 77(2) requires the Best Estimate to be discounted using the relevant risk-free interest rate term structure. Future cashflows are discounted using the 31 December risk free yield curves provided by EIOPA. The yield curves used exclude the Volatility Adjustment. Future cash flows have been obtained by applying projected payment patterns derived for the Core Reserving process
- Risk Margin: Article 77(2) of the Directive requires Technical Provisions to be calculated using 'realistic assumptions and adequate methods'. Article 77(3) extends this

[1] Any references to the risk margin are unaudited

requirement to the calculation of the risk margin. The Risk Margin is calculated using a cost of capital approach by applying the Best Estimate cash-flow runoffs and the prevailing yield curve (as provided by EIOPA) to the Internal Model SCR capital measure

Currency

The Directive requires that the best estimate is calculated separately for obligations in different currencies to enable the calculation of discounted liabilities.

Currency allocations are performed by class of business via the Core Reserving process; each reserving class is typically analysed in one currency.

For Solvency II the claims and premiums by currency provided in the data are derived by Finance using the outputs from the Core Reserving process, and no additional judgement is required.

Reinsurance Correspondence

The Directive requires that reinsurance recoveries from outwards reinsurance (and special purpose vehicles (SPVs)) are allowed for in the claims and premium provisions with an explicit allowance for counterparty default risk.

Regarding the principle of correspondence, the reinsurance recoveries are calculated such that they are consistent with the gross premium forecasts and implicitly allow for expected recoveries in respect of losses occurring during (LOD) and risks attaching during (RAD) policies. In line with regulatory guidance, the Group's approach is as follows.

- Incepted and bound reinsurance valued to the extent that it covers existing (i.e. incepted and bound) inwards business
- Adjusted to allow for reinsurance minimum premium terms
- Allowance for future reinsurance purchase management actions to protect the run-off to expiry of existing inwards business, consistent with the current reinsurance structure

Options and Guarantees

We have assessed that the Group does not have any exposure to any options and guarantees. Hence no allowance is made in the technical provisions with regard to these.

Uncertainty in Technical Provisions[2]

There are a number of uncertainties in the technical provisions, particularly in respect of the best estimate of unpaid claims and future premiums.

Some of the main uncertainties are listed below:

- Claim cost inflation, in particular for classes of business with long terms to settlement
- General levels of future new claim notifications
- Prior year large natural or man made catastrophic events, to the extent that claims have not been fully settled
- Periodic Payment Orders
- New future, and as yet unknown and unquantifiable, large market loss events that could impact the Group
- Future premiums, especially for the most recent underwriting year, are based on the Companies' business plans and discussions with underwriters. Actual written premiums achieved are impacted by general market conditions and therefore may ultimately differ from those estimated
- Plan loss ratio estimates

[2] Any references to uncertainty in technical provisions are unaudited

- Estimates for Events not in Data
- Timing of claim, premium, reinsurance and expense Cashflows
- The appropriateness of the development tail factors applied to the Group's classes , in particular where these have been derived from external information in the absence of a fully mature claims development history directly relevant to the Group

No material simplifications have been used in the calculation of technical provisions.

Matching adjustment[3]

The Group does not apply a matching adjustment.

Volatility adjustment[4]

The Group does not apply a volatility adjustment.

Transitional risk free interest rate term structure[5]

The Group does not apply a transitional adjustment.

Recoverables from reinsurance contracts and special purpose vehicles

Provisions are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable from reinsurers based upon the gross provisions and having due regard to collectability.

An initial estimate is made of the reinsurance recoveries as a proportion of gross. This is derived originally from the reinsurance pricing basis and the business plan, along with a review that considers catastrophe/large/attritional losses and non treaty cover. Any known large outstanding claims are considered on a case by case basis. Reinsurance IBNR is unwound in line with the gross to maintain a suitable net provision.

The technical provisions have been reviewed by members of the Actuarial Function to ensure that they adhere to the relevant Solvency II articles and texts. In particular, the technical provisions have been calculated as per Directive Articles 76-84, including an allowance for reinsurance bad debt.

[3] Any references to matching adjustments are unaudited
[4] Any references to volatility adjustments are unaudited
[5] Any references to transitional adjustments are unaudited

3. Other liabilities

The Group's other liabilities, i.e. excluding technical provisions, were valued, on a Solvency II basis, at £539,891k at 31 December 2016. The valuation of other liabilities is addressed in the section below.

Balance sheet item	Valuation in Financial Statements (£'000)	Valuation for Solvency Purposes (£'000)	Comparison of Solvency II Valuation Basis with IFRS	Solvency II Valuation Basis and Asumptions
Provisions other than technical Provisions	5,452	5,393	The valuation basis is the same as IFRS	IAS 37 is consistent with Solvency II measurement principles for provisions as stated in the Final Report on public consultation No. 14/065 on Guidelines on Recognition and Valuation of Assets and Liabilities other than Technical Provisions. Generally there is no difference between UK GAAP and IFRS in recognition and measurement of provisions.
Deposits from Reinsurers	996,525	23,671	The valuation basis is the same as IFRS	For the short term deposits from reinsurers, the carrying value of these liabilities is deemed to be a close approximation to fair value and therefore no adjustment is made.
Insurance and intermediaries payables	222,281	61,610	In the Solvency II balance sheet insurance payables are adjusted for cash flows relating to future premiums which are taken into account in technical provisions. These are considered to be technical cash flows to which the company is not yet entitled to under Solvency II.	Insurance and intermediary payables are valued consistently with IAS 39 fair value measurement principles except for subsequent adjustments to take into account the undertaking's own credit risk. The carrying value of these liabilities is deemed to be a close approximation to fair value and therefore no adjustment is made.
Reinsurance payables	406,077	25,925	In the Solvency II balance sheet reinsurance payables are adjusted for cash flows relating to future premiums which are taken into account in technical provisions. These are considered to be technical cash flows to which the company is not yet entitled to under Solvency II.	Reinsurance payables are valued consistently with IAS 39 fair value measurement principles except for subsequent adjustments to take into account the undertaking's own credit risk. The carrying value of these liabilities is deemed to be a close approximation to fair value and therefore no adjustment is made.
Payables (trade, not insurance)	2,075,225	370,968	The valuation basis is the same as IFRS	Other payables should be valued at fair value by discounting expected cash flows using a risk free rate. However in the Company's case, book value as per IFRS is used as a proxy to the fair value for Solvency II balance sheet purposes as the impact of discounting is not material because the balances are mostly due/payable within one year.

Balance sheet item	Valuation in Financial Statements (£'000)	Valuation for Solvency Purposes (£'000)	Comparison of Solvency II Valuation Basis with IFRS	Solvency II Valuation Basis and Asumptions
Derivatives	27,762	27,762	The valuation basis is the same as UK GAAP. However, in the Statutory Accounts some grouping of positions is carried out. In contrast, in Solvency II every derivative position is recognised separately. Hence, the value of the derivative assets and liabilities may differ between the two bases. The net position is the same.	Derivatives are measured at fair value under UK GAAP, which is consistent with Solvency valuation policy.
Any other liabilities, not elsewhere shown	12,254	15,141	The valuation difference relates to the change in the value of deferred tax, caused by the impact of adjustments made to balance sheet items in compliance with Solvency II regulations.	The Guidelines on the valuation of assets and liabilities other than technical provisions indicate that IAS 12 discloses "consistent measurement principles for deferred taxes calculated based on the temporary difference between Solvency II values and the tax values" with the measurement principles of Article 75. Deferred tax liabilities are calculated based on the temporary difference between Solvency II values and the tax values.

Finance and operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight line basis over the period of the lease.

The Group has a number of lease commitments, principally in relation to office space, details of which are below:

Leases payable	2016 Value (£'000)
Land and Buildings	
Not later than one year	12,663
Later than one year but not later than five years	40,362
Later than five years	45,836
Total future minimum lease payments under non-cancellable operating lease	**98,861**

Leases payable	2016 Value (£'000)
Other	
Not later than one year	136
Later than one year but not later than five years	195
Total future minimum lease payments under non-cancellable operating lease	**331**

Expected timing of outflows of economic benefits

Payables, the largest balance within other liabilities have a mean term for payment of less than 1 year. As these are expected to be settled in the short term no deviation risk has been applied.

Employee Benefits

The Group operates both defined contribution and defined benefit pension plans.

In respect of the defined benefit plans, each scheme is run independently of the sponsoring company by scheme trustees, and is subject to relevant local legislation.

Pension contributions relating to each scheme are assessed in accordance with the advice of independent qualified actuaries in order to spread the cost over the service lives of employees.

Changes to the valuation of liabilities in the period

There have been no changes to the recognition and valuation bases used or to estimations during the reporting period.

Insurance contracts

The main source of estimation uncertainty concerns the valuation of Technical Provisions, which are discussed in section D2. Estimates have to be made for expected future claims. It can take a significant amount of time before the claims cost can be established with certainty. For some contracts premium is initially written based on estimates of ultimate premiums.

Estimates might be derived from underwriter experience, historical data and broker estimation. These estimates are judgemental and could result in misstatements.

Taxation

The Group establishes provisions based on reasonable estimates, for possible consequences of audits by the tax authorities of the countries in which it operates. The amount of such provisions is based on various factors, such as experience with previous tax audits and differing interpretations of tax regulations by the tax authority. Management estimation is required to determine the amount of deferred taxes that can be recognised, based upon likely timing and level of future taxable profits together with an assessment of the effect of future tax planning strategies.

4. Alternative methods for valuation

All assets and liabilities are valued using standard methodologies as previously described in sections D.1 to D.3. No alternative valuation methods are applied.

5. Any other information

No other information.

Section E: Capital Management[6]

1. Own funds

The Group's available own funds, eligible own funds and ratio of eligible own funds over SCR and MCR are disclosed in QRT S.23.01 in Appendix A.

The primary objective of the business from a capital management perspective is to maintain sufficient own funds to cover the SCR and MCR with an appropriate surplus. These should be of sufficient quality to meet the eligibility requirements in Article 82 of the Delegated Regulation.

The Group has adopted a Capital Appetite Framework, setting out the target levels of capital and potential remediation actions in the event that capital falls below the stated appetite. The Capital Appetite Framework has been approved by the Group's Board and senior management hold regular meetings, on at least a quarterly basis, to monitor the ratio of eligible own funds over SCR.

The SCR Coverage Ratio of 126% presented in the Group's Annual PRA submission includes a foreseeable dividend payable in Q2 2017. This dividend is included in the Annual Return as an adjusting post balance sheet event as it is foreseeable at the date of board approval of submission.

The SCR coverage ratio at 31 December 2016 would be disclosed as 135% in the absence of this foreseeable dividend.

The regulated entities within the Group have the following credit ratings, as determined by S&P Global Ratings:

- QBE Re (Europe) Limited has a financial strength rating of A+, with a positive outlook
- QBE Insurance (Europe) Limited has a financial strength rating of A+, with a positive outlook and a long-term public issue credit rating of A+

There were no material changes over the reporting period.

Method of calculating own funds

The Group uses the accounting consolidation based method to determine the Group's basic own funds and follows four steps:

- Own funds are calculated on the basis of consolidated data
- Own funds are classified into tiers
- Available own funds are calculated net of adjustments at group level
- Eligible own funds are determined, subject to tiering limits, in order to determine the amount of own funds eligible to cover the Group's SCR and MCR

Consolidated group own funds

The Group's own funds comprise the sum of its basic own funds and ancillary own funds. Basic own funds comprise:

- The excess of assets over liabilities, determined from the Solvency II consolidated balance sheet calculated on the basis of the consolidated data in accordance with the accounting consolidation based method and Solvency II guidelines, less adjustments

[6] Any references in 'Section E: Capital Management' to the SCR are unaudited

- Subordinated liabilities to the extent that these satisfy the Solvency II rules for recognition as part of basic own funds

Different undertakings within the Group are treated in different ways, as described below:

- Fully-consolidated entities constitute the (re)insurance undertakings, insurance holding companies and ancillary services undertakings
- Financial institutions are valued in accordance with Article 335(1)(e) of the Solvency II Delegated Acts in accordance with the "relevant sectoral rules" and included as a single line item as "participations" in the Solvency II balance sheet. Consistent with calculation of the SCR for these entities which has been determined based on "sectoral rules" applicable to banks and investment firms, the "relevant sectoral rules" for the purposes of determining own funds are also those applicable to banks and investment firms
- Other related undertakings are included under adjusted equity method

Classification into tiers

Tier 1

Own fund items are assessed and classified into tiers in accordance with criteria defined by Solvency II regulations. The majority of Group own funds are classified as Tier 1 based on the following:

- they rank after all other claims in the event of winding-up proceedings regarding the insurance or reinsurance undertaking
- they do not include features which may cause the insolvency of the insurance or reinsurance undertaking or may accelerate the process of the undertaking becoming insolvent
- they are immediately available to absorb losses and do not hinder any recapitalisation
- the nominal or principal are written down in such a way that all of the following are reduced: the claim of the holder of that item in the event of winding-up proceedings; the amount required to be paid on repayment or redemption of that item; the distributions on that item
- they are undated
- they are only repayable or redeemable at the option of the insurance or reinsurance undertaking and shall not include any incentives to repay or redeem that item
- they provide for the suspension of repayment or redemption of that item in the event that there is non-compliance with the SCR or repayment or redemption would lead to such non-compliance until the undertaking complies with the SCR and the repayment or redemption would not lead to non-compliance with the SCR
- they allow for the distributions in relation to that item to be cancelled, either under the legal or contractual arrangements governing the item or under national legislation, in the event that there is non-compliance with the SCR or the distribution would lead to such non-compliance until the undertaking complies with the SCR and the distribution would not lead to non-compliance with the SCR
- they may only allow for a distribution to be made where there is non-compliance with the SCR or where distribution would lead to such non-compliance where all the following conditions are met: the supervisory authority has exceptionally waived the cancellation of dividends, the distribution does not further weaken the solvency position of the insurance or reinsurance undertaking; the MCR is complied with after the distribution is made
- the insurance or reinsurance undertaking has full flexibility over the distributions on the basic own-fund item
- the basic own-fund item is free from encumbrances and is not connected with any other transaction

Tier 2

The Solvency II consolidated balance sheet includes capital securities issued by the Company to subsidiary undertakings within the Group. These securities take the form of capital securities and subordinated debt.

The capital securities were historically treated as Innovative Tier 1 capital in the Group Capital Adequacy Return (GCAR) under Solvency I (limited to 15% of Tier 1 after deductions with the balance included as Tier 2). As regards the Solvency II treatment, these securities will not meet the Solvency II criteria to be treated as Tier 1 capital, however they will be eligible for transitional relief. Hence, as per Article 308b(9) of the Directive, these securities shall be included as Tier 1 Capital for up to 10 years after 2016.

The subordinated debt is eligible for inclusion as Tier 2 capital. This debt comprises two separate sets of notes, one denominated in sterling and the other denominated in US dollars. The two sets of notes are constituted by separate deeds of covenant made by the Group by way of deed poll. The two deeds are, save for minor differences relating exclusively to their differing currencies, identical.

Reconciliation reserve

The reconciliation reserve is comprised of the excess of assets over liabilities on a Solvency II valuation basis, less other basic own fund items and an adjustment for restricted own fund items in respect of immaterial ring fenced funds. Other basic own fund items include ordinary share capital, related share premium account and an amount equal to the value of net deferred tax assets.

Availability at group level of own funds

An amount equal to the excess of the solo SCR of QIEL and QBE Re over each entity's allocation of the group SCR will be treated as non-available own funds at group level. This represents the entity's share of the diversification benefit included in the group SCR.

While the assessment of availability of group own funds is not specifically required to be carried out in relation to ancillary services undertakings, pension surpluses recognised by ancillary services undertakings under IAS 19 will be treated as not available at group level.

The amount of non-available own funds for the Company, Holdings (EO), QBE Insurance (Europe) Limited, QBE Re (Europe) Limited and MSUK will be compared to their respective contributions to the Group SCR. Any excess of non-available own funds over the contribution to Group SCR will be deducted from the group available own funds.

Eligibility of group own funds

The eligibility of own funds to cover the Group SCR and MCR is subject to tiering limits, specifically:

- The eligible amounts of Tier 1 items must be at least 50% of the SCR and 80% of the MCR
- The eligible amounts of Tier 3 items must be less than 15% of the SCR
- The sum of the eligible amounts of Tier 2 and Tier 3 items must not exceed 50% of the SCR or 20% of the MCR

Equity in the financial statements and the excess of assets over liabilities for solvency purposes

The Group's Own Funds position is different from the equity stated in the financial statements due to the differences in Solvency II regulations. Adjustments were made to the data disclosed in the financial statements to ensure compliance with the new regulations, further details of which are provided in section D.1.

Deductions from own funds

The following restrictions in relation to Ring Fenced Funds apply:

- Letters of credit - Reflecting the margin required by the issuer over the level of LOCs issued. The level of restriction to own funds has been calculated on the basis that actual liabilities are equal to the LOCs issued and therefore that the only restriction relates to the margin required by the issuer
- Capital required to be held locally by the Dubai regulator in respect of the local operations of subsidiary QBE Insurance (Europe) Limited
- As a condition of writing US Excess and Surplus lines business, the Group is required to deposit cash, readily marketable securities or letters of credit into Trust with a "United States Qualified Financial Institution"

Group diversification benefits

The key driver of the capital requirement for the Group is insurance risk. Earned reserving risk and underwriting risk also constitute key elements. As noted below, credit and operational risks are important on an undiversified basis, but the dominance of the insurance risk makes these risks less important on a diversified basis. Market risk is negative on a diversified basis as there remains some positive investment return in the scenarios driving the capital. Liquidity, group and pension risks have less impact on the overall capital requirements.

Undertakings in the scope of the Internal Model used to calculate the Group SCR

The following entities write insurance and reinsurance business within the Group and are covered by the Group internal model:

- QBE Insurance (Europe) Limited
- QBE Re (Europe) Limited

The Lloyd's Syndicates capacity (Syndicates 386 and 2999) is owned through QBE Corporate Limited, the managing agent being QBE Underwriting Limited. The Group SCR treats QBE Corporate as an investment and its non-regulated financing subsidiaries based around their sectoral capital requirements. These additional elements contribute to an increase to the Group SCR.

The total Group SCR, at £1,466,930k, is lower than the sum of these individual elements due to a diversification benefit in respect of regulated subsidiaries QBE Insurance (Europe) Limited and QBE Re (Europe) Limited.

The difference between the entity level Internal Model and the Group level Internal Model

QBE Insurance (Europe) Limited and QBE Re (Europe) Limited follow the same risk drivers as the Group. This is as expected since the Group is a consolidation of the risks from the underlying subsidiaries.

However there are some key differences between the internal model used at individual undertaking level and the internal model used to calculate the group SCR. They are:

- The Group and its subsidiaries operate four defined benefit pension schemes. This is allowed for in the Group SCR
- The Group SCR also allows for the following items:

- QBE Corporate is treated as an investment and its value is assumed to be completely written off for the purpose of assessing capital
- The capital for non-regulated financing companies is calculated based on sectoral requirements
- The Group's net financing cost is allowed for as an outwards cashflow from the model

2. Solvency Capital Requirement and Minimum Capital Requirement

The SCR for the Group at 31 December 2016, calculated using the company's fully approved Internal Model, was £1,466,930k.   Further detail, including the breakdown by risk type, is provided in QRT S.25.03.21 (Appendix A). Eligible Own Funds of £1,980,311k at 31 December 2016 gave rise to an SCR coverage ratio of 135%. Deduction of a Q2 2017 foreseeable dividend reduced the EOF in the Annual PRA submission to £1,840,961k, which explains the SCR coverage ratio of 126% as presented in the own funds QRT.

The MCR was £583,188k. The MCR is calculated using inputs for the net (of reinsurance/SPV) Solvency II best estimate and the net (of reinsurance SPV) written premium in the last 12 months. Factors are applied to these inputs based on the technical specifications from the long-term guarantees package. The MCR coverage ratio as presented in the QRT and including EOF relating to financial institutions is 209.9%.

The Group MCR is constituted of the MCR of the Group's Regulated Companies, the values of which are as follows:

QBE Insurance (Europe) Limited: £403,549k

QBE Re (Europe) Limited): £179,639k (€210,777k)

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

The Group has a fully approved Internal Model and therefore does not use the duration-based equity risk sub-module.

4. Differences between the standard formula and the Internal Model used[7]

The Internal Model is comprised of a number of underlying processes, each of which can be used for a variety of different purposes as can the Internal Model results as a whole.

The Internal Model reflects the risk assessment processes that have been within the business for a number of years. There is a strong alignment between the Internal Model and the core business processes. At the beginning of the year a plan for Internal Model usage is drawn up by the ERM Director and business owners. This plan includes "business-as-usual" usage, and also planned new uses for the forthcoming year. These plans are then monitored by the ERM team on a quarterly basis. The following are some of the key business processes that currently use Internal Model output:

[7] Any references to differences between the Standard Formula and the Internal Model are unaudited

- Underwriting strategy. The business planning process (which is part of the Internal Model) underpins the Group's underwriting strategy, with key decisions being made with reference to the impact on the business plan and return on allocated capital
- Historic Performance Analysis. The reserving process (which is also part of the Internal Model) produces historic loss ratio performance analysis for each line of business. These are then reviewed for trends that lead to "deep dive" investigations into individual classes of business as necessary
- Capital allocation. Capital is allocated to each line of business based on the output from the Internal Model. This then feeds into the business plans so that decision making is based on return on allocated capital (ROAC)
- Remuneration. Incentives are based upon performance relative to plan, and therefore the Internal Model has a strong link to remuneration
- Acquisitions. Each area of the Internal Model is considered within an acquisition process, so that the decision to go ahead with the acquisition or not is made with reference to the risks inherent in the acquired business and how they fit with the existing business
- Calculating regulatory capital. The Internal Model has been used for a number of years to assess regulatory capital and catastrophe modelling reporting requirements
- Risk MI including risk dashboards have been developed to distil complicated risk information into simple measurements that feed into decision making processes
- Probability of Adequacy. The Internal Model is used to assess and monitor the ongoing adequacy of the booked reserves

Scope of the Internal Model

All classes of business are within the scope of the capital model in all business units within the Group. The business units contained within the Company are as follows:

Business unit	Description
Credit	This business unit consists of Trade Credit, Surety and Bonds business written through the UK, French, German and Swiss offices.
International	The international markets division consists of a diverse range of international wholesale business including energy, marine, property and liability.
Retail	The retail division is the largest division and focusses on UK and European business. Classes of business include motor, property, liability and financial and specialty markets.
Reinsurance	The global reinsurance division includes business largely written through Belgium, UK and Dublin. There is a large amount of long-tailed treaty business, including non-proportional casualty and general liability.
Legacy Business Management (LBM)	This business unit consists of run-off business, including medical malpractice, long tail disease, financial institutions, liability, casualty and motor.
Central and Eastern European business	This business unit consists of the run-off of all the Central Eastern European countries - QBE has been reducing its exposure in all of these countries and a large proportion of this business has been sold. The business is an even mixture of Property, Motor and Liability, plus some small exposure on Aviation and Marine.

The Internal Model incorporates underwriting risk, reserving risk (both unearned and earned), credit risk, market risk, liquidity risk, operational risk, group risk and pension risk (where applicable).

Probability distribution forecast and the Solvency Capital Requirement using the Internal Model

The Internal Model brings together the entire probability distribution forecasts for each risk, and therefore produces an entire probability distribution forecast of profits or losses that could arise across the business. The capital assessment carried out within the capital model is specifically selected as the 99.5 percentile deterioration in the balance sheet that can occur over a single year (99.5% VaR), which matches the required Solvency II calibration standard. The model also produces capital to ultimate which is used for ORSA and, in Group's Lloyd's Syndicates, for Lloyd's purposes. This is calculated as the 99.5 percentile deterioration in the balance sheet that can occur to ultimate which is assumed to be a 10 year run off.

All modelling is carried out at a detailed level, so profit and loss can be considered at class and/or risk type level, enabling comparisons between the modelled results and the actual balance sheet, as well as ranking of risks.

Standard formula and Internal Model differences

The standard formula and Internal Model are based on two very different data sets, resulting in differences in outputs. Some of the main differences, and similarities, are noted below.

Market risk

There are a number of differences within the components of market risk. In particular, the Group has exposure to currency risk (i.e. net asset exposure in any non GBP currency). Within the Internal Model, currency risk is modelled as the difference between the net assets at the end of the period converted at the end of period stochastic FX rates less the net assets at the end of the period converted at the average of the stochastic FX rates at the end of the period. The currency splits on the assets and liabilities are modelled separately and they are not forced to match within the model.

Concentration risk is implicitly allowed for in the Internal Model; the distributions in the ESG are based on the assets held, and the concentration of assets.

The overall level of market risk (excluding currency risk) between the standard formula and Internal Model are broadly similar.

Counterparty default credit

The Internal Model and standard formula capitalise against reinsurance and premium defaults in two very different ways.

- The standard formula includes a very small capital requirement against reinsurance default, whereas the Internal Model includes more capital on a stand-alone basis. The Internal Model assumes 5 year default rates during the first year, which is a very conservative assessment for credit risk. The standard formula is more based around the expected change in bad-debt provisions from credit rating migrations, with minimal actual default during the first year. Note, however, that the reinsurance credit risk diversifies well in the Internal Model, which gives rise to a larger diversification benefit from this one item
- The standard formula applies a material capital charge against premium debtors, taking 90% of any debts over-due by 3 months or more, and 15% of all other debtors. Broker balances (which are the main part of the debtor exposure) are subject to a separate set of regulation, for example in the UK the FCA regulates brokers and constrains how their monies are handled. This means that the risk is well mitigated, and the Internal Model capital assessment reflect this

Non-life underwriting risk

There is only a small difference between the total assessment of insurance risk when the health and life risk is included in the standard formula calculations. The methodology differences between the two models include:

- The Internal Model considers insurance risk as an absolute loss amount, so any profit in the plan acts as an offset against capital. The standard formula just does a relative assessment, in essence assuming that the business has a 100% net combined ratio
- The Internal Model does not separate out lapse risk, but it is included in the risk around the level of business written in the new underwriting year. When business does lapse, it both removes the profit associated with this anticipated business (which the standard formula and Internal Model both capture), and also the risk associated with the business (which the standard formula does not capture)
- The overall level of catastrophe risk is broadly consistent between the two models, although the modelling treatment is different. The Internal Model allows for the full features of the reinsurance protections, whereas the standard formula approximates them, most notably through the lack of multiple reinstatements on protections, and the use of maximum line size losses within the man-made catastrophe component

Health underwriting risk

The Internal Model does not capture this separately from the non-life underwriting risk.

Operational risk

The capital model allows operational risk to diversify against other risk types, whereas it is additive in the standard formula. If the diversified operational risk is calculated in the Internal Model then the differences are smaller. This different treatment of operational risk also gives rise to an increased level of diversification benefit in the Internal Model compared to the standard formula.

Diversification benefit. Because of the differences between risk types, the standard formula has less diversification between risk types than the Internal Model. A large contributor to this is the high level of reinsurance credit risk in the Internal Model which diversifies quite well against the other risk types (reserve risk in particular) compared against the standard formula that has a lower level of reinsurance credit risk.

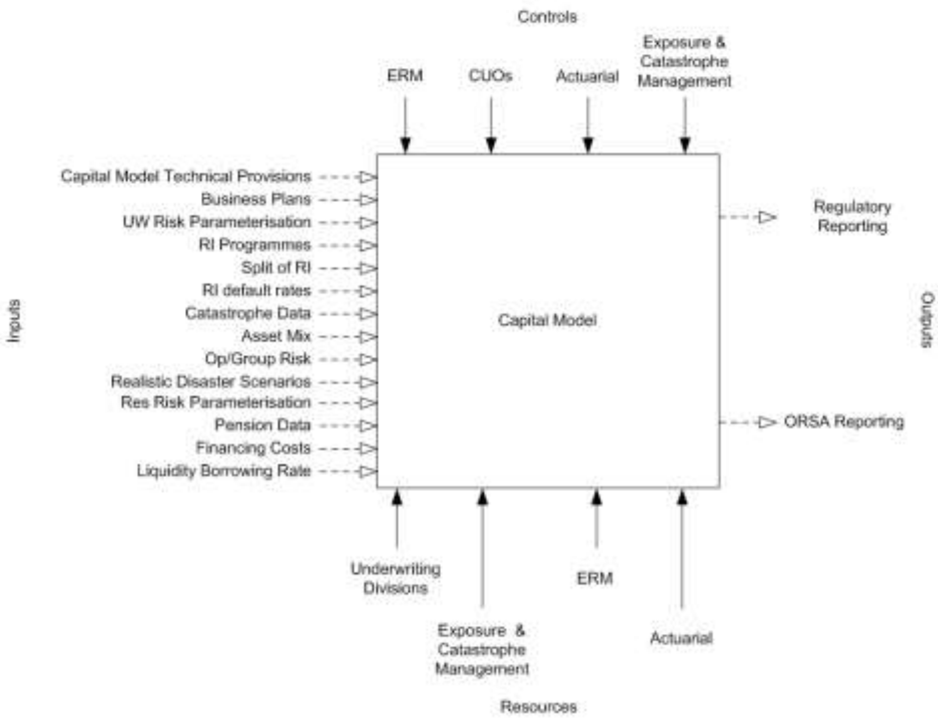
The standard formula does not capture group risk, whereas it does appear in the Internal Model. This risk is assumed to diversify well against the other risks, so it also increases the size of the diversification benefit in the Internal Model compared to the standard formula.

Data used in the Internal Model

The data flows within the capital model are documented within a Internal Model Dataflow Map. As part of data quality management in QBE, a Data Governance Team carry out a self-assessment exercise regularly with those business areas that provide data flows into the capital model. The results of this work, in particular any areas for remediation, are recorded on a Data Quality Issues Log which is reviewed and managed by the Data Quality Group, a sub-Group of the OMG.

The technical specification details of the data extracts that form the inputs to the capital model are held in a Data Directory, which is also verified by business owners as part of the self-assessment review. This ensures that the data specifications are regularly kept up-to-date.

An overview of each of the data flows is illustrated below.



There are a number of pieces of data that feed into the capital model. Each of these sources of data is subject to all of the requirements of the internal model:

- **Technical provisions**. These are provided by the Actuarial Function and comprise of undiscounted paid, incurred and ultimate premium and claims, by class, currency and year of account
- **Claims development patterns**. These are taken from the actuarial technical provisions. They comprise of paid and incurred patterns by class of business and currency to support discounting of the liabilities in the capital model
- **Reserve risk parameterisation**. This takes the output from the reserve variability analysis carried out by the Actuarial Function, with the parameters held at class of business level
- **Business plans**. These are taken from the business planning database, and comprises the full business plan by class of business
- **Large and attritional loss parameterisation**. This is the output from the large and attritional loss parameterisation process, which is currently carried out by the Actuarial Function
- **Reinsurance programmes**. This is the data detailing the outwards reinsurance programmes that QBE EO has in place, and is taken from the reinsurance schematics produced by the Underwriting and Reinsurance Review Department
- **Split of reinsurers on technical provisions**. This is taken from a query in the Group's reinsurance reporting system that produces the split of the reinsurance asset on the balance sheet at any quarter end by legal entity. The system itself is supported by QBE Group, although the Underwriting and Reinsurance Review Department maintain Group ownership for the data
- **Reinsurer and broker default rates**. These are taken from Standard and Poor's reports on the default probabilities for differently rated companies and overlaid with any judgement by the Group Security Committee

- **Natural catastrophe model output**. This is the output from RMS, which comprises of event loss tables for different classes of business, and is received from the Exposure and Catastrophe Management team. Group Aggregate Monitoring (GAM) data is also used to assess the risk from regions and perils not modelled by RMS
- **Realistic disaster scenarios**. This data is the output from the RDS exercise conducted twice a year. This is used to help validate the catastrophe losses generated within the capital model, parameterise the man-made catastrophe risks and parameterise the non-modelled classes within the natural catastrophe risk
- **Asset mix**. This data lists the different investments held by each legal entity within Group. These assets are input into the model as the opening asset position
- **Total Risk Assessment (TRA).** This data is taken from within the ERM team and provides the operational risk parameters
- **Group Risk Dashboard.** Used to parameterise the group risk distributions. Data is taken from within the ERM team
- **Asset model output**. This data is the output from the asset model, which is the distribution of asset returns split by asset type, currency and term (as well as inflation and currency exchange rates in the future). This is currently taken from Willis Towers Watson's Economic Scenario Generator (ESG), following review (and adjustments if necessary) from the fund manager (Group Investments) and the Group's Investment Committee
- **Liquidity borrowing rate**. This is the rate at which money can be borrowed to cover short term cashflow restraints
- **Pension data**. This comprises of the pension assets and liabilities, longevity stress tests and benefit payment proportions
- **Financing costs and other capital requirements**. These are the expected debt servicing costs for the Group and any capital to support the non-regulated financing companies

Where data is taken from other processes, the capital model assumes that it is complete and accurate (these processes will additionally check that their input data is complete and accurate).

5. Non-compliance with the Minimum Capital Requirement and non-compliance with the Solvency Capital Requirement

When EOF from all entities is included, the Group satisfies and complies with the MCR and SCR requirements.[8]

6. Any other information

None noted.

[8] Any references to non compliance with the SCR are unaudited

Appendix A. QRTs

Template code	Template name
S.32.01.22	Undertakings in the scope of the group
S.02.01.02	Balance sheet
S.05.01.02	Premiums, claims and expenses by line of business – Non-Life
S.05.01.02	Premiums, claims and expenses by line of business - Life
S.05.02.01	Premiums, claims and expenses – Non-Life
S.05.02.01	Premiums, claims and expenses - Life
S.22.01.22	Impact of long term guarantees measures and transitionals
S.23.01.01	Own Funds
S.25.03.22	Solvency Capital Requirement - for undertakings on Full Internal Models

S.32.01.22

Undertakings in the scope of the group

Country	Identification code of the undertaking	Type of code of the ID of the undertaking	Legal Name of the undertaking	Type of undertaking	Legal form	Category (mutual/non mutual)	Supervisory Authority	Criteria of influence: % capital share	Criteria of influence: % used for the establishment of consolidated accounts	Criteria of influence: % voting rights	Criteria of influence: Other criteria	Criteria of influence: Level of influence	Criteria of influence: Proportional share used for group solvency calculation	Inclusion in the scope of Group supervision: YES/NO	Inclusion in the scope of Group supervision: Date of decision if art. 214 is applied	Group solvency calculation: Method used and under method 1, treatment of the undertaking
C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0180	C0190	C0200	C0210	C0220	C0230	C0240	C0250	C0260
CH	213800CH00002	2 - Specific code	ANEX JENNI & PARTNER AS	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	2138008RZQUZIMI	1 - LEI	QBE INSURANCE (EUROPE) LIMITED	2 - Non life insurance undertaking	Company limited by shares or by guarantee or unlimited	2 - Non-mutual	The Prudential Regulation Authority	100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800ADAKQM58	1 - LEI	QBE RE (EUROPE) LIMITED	3 - Reinsurance undertaking	Company limited by shares or by guarantee or unlimited	2 - Non-mutual	The Prudential Regulation Authority	100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
CA	213800CA00024	2 - Specific code	QBE SERVICES INC.	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
DE	213800DE00003	2 - Specific code	GREENHILL BAIA UNDERWRITING GMBH	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800GB00015	2 - Specific code	STANDFAST CORPORATE UNDERWRITERS LIMITE	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800G4VF3APWE	1 - LEI	QBE UNDERWRITING LIMITED	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800GB00004	2 - Specific code	GREENHILL STURGE UNDERWRITING LIMITED	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800GB00005	2 - Specific code	GREENHILL UNDERWRITING ESPANA LIMITED	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
HU	213800HU00010	2 - Specific code	QBE ATLASZ INGATLANKEZELO ZRT	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
AU	213800AU00013	2 - Specific code	QBE INVESTMENTS (AUSTRALIA) PTY LIMITED	8 - Credit institution, investment firm and financial institution	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		4 - Method 1: Sectoral rules
CZ	213800CZ00017	2 - Specific code	LIFECO S. R. O.	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800GB00019	2 - Specific code	QBE HOLDINGS (EUROPE) LIMITED	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
DK	213800DK00020	2 - Specific code	QBE DENMARK A/S	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
SG	213800SG00023	2 - Specific code	QBE MARINE AND ENERGY SERVICES PTE LIMITE	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800GB00026	2 - Specific code	QBE UK FINANCE GP	8 - Credit institution, investment firm and financial institution	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		4 - Method 1: Sectoral rules
GB	213800GB00009	2 - Specific code	QBE INSURANCE SERVICES (REGIONAL) LIMITED	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
IE	213800CDFJ12UGM	1 - LEI	QBE MANAGEMENT (IRELAND) LIMITED	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	2138001VJLIGBUFE	1 - LEI	QBE HOLDINGS (EO) LIMITED	5 - Insurance holding company as defined in Article 212(1) (f) of Directive 2009/138/EC	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800F6M2ZYHXY	1 - LEI	QBE MANAGEMENT SERVICES (UK) LIMITED	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800GB00011	2 - Specific code	QBE PARTNER SERVICES (EUROPE) LLP	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800GB00012	2 - Specific code	QBE SERVICES (EUROPE) LIMITED	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
SK	213800SK00007	2 - Specific code	QBE SK, S. R. O.	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
JE	213800JE00014	2 - Specific code	QBE JERSEY FINANCE LIMITED	8 - Credit institution, investment firm and financial institution	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		4 - Method 1: Sectoral rules
CZ	213800CZ00006	2 - Specific code	QBE, S. R. O.	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800GB00016	2 - Specific code	GREENHILL INTERNATIONAL INSURANCE HOLDIN	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	2138001YKXKPQ6D	1 - LEI	QBE FINANCE HOLDINGS (EO) LIMITED	8 - Credit institution, investment firm and financial institution	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		4 - Method 1: Sectoral rules
GB	213800M5ZP1KSX9	1 - LEI	QBE CORPORATE LIMITED	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
AU	213800AU00022	2 - Specific code	QBE EUROPEAN UNDERWRITING SERVICES (AUST	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800GB00025	2 - Specific code	QBE UNDERWRITING SERVICES LIMITED	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
IE	213800IE00027	2 - Specific code	QBE UNDERWRITING SERVICES (IRELAND) LIMITE	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800GB00028	2 - Specific code	QBE UNDERWRITING SERVICES (UK) LIMITED	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	213800GB00029	2 - Specific code	QBE EUROPEAN SERVICES LIMITED	99 - Other	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		3 - Method 1: Adjusted equity method
GB	21380023SZB3A8TI	1 - LEI	QBE UK FINANCE III LIMITED	8 - Credit institution, investment firm and financial institution	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		4 - Method 1: Sectoral rules
GB	2138003HAOJ2X4P	1 - LEI	QBE UK FINANCE IV LIMITED	8 - Credit institution, investment firm and financial institution	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		4 - Method 1: Sectoral rules
GB	213800791EF5XP7V	1 - LEI	QBE EUROPEAN OPERATIONS plc	5 - Insurance holding company as defined in Article 212(1) (f) of Directive 2009/138/EC	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		0.00%	0.00%	0.00%			0.00%	1 - Included in the scope		1 - Method 1: Full consolidation
GB	213800GB00008	2 - Specific code	RIDGWELL FOX AND PARTNERS (UNDERWRITING	10 - Ancillary services undertaking as defined in Article 1 (53) of Delegated Regulation (EU) 2015/35	Company limited by shares or by guarantee or unlimited	2 - Non-mutual		100.00%	100.00%	100.00%		1 - Dominant	100.00%	1 - Included in the scope		1 - Method 1: Full consolidation

S.02.01.02

Balance sheet

	Solvency II value
Assets	C0010
Intangible assets	
Deferred tax assets	86,356
Pension benefit surplus	21,947
Property, plant & equipment held for own use	34,014
Investments (other than assets held for index-linked and unit-linked contracts)	6,147,488
Property (other than for own use)	0
Holdings in related undertakings, including participations	1,180,675
Equities	13,898
Equities - listed	0
Equities - unlisted	13,898
Bonds	4,420,478
Government Bonds	987,509
Corporate Bonds	3,010,356
Structured notes	0
Collateralised securities	422,613
Collective Investments Undertakings	444,769
Derivatives	8,693
Deposits other than cash equivalents	78,974
Other investments	0
Assets held for index-linked and unit-linked contracts	0
Loans and mortgages	83,150
Loans on policies	0
Loans and mortgages to individuals	0
Other loans and mortgages	83,150
Reinsurance recoverables from:	834,285
Non-life and health similar to non-life	811,663
Non-life excluding health	779,788
Health similar to non-life	31,875
Life and health similar to life, excluding index-linked and unit-linked	22,622
Health similar to life	0
Life excluding health and index-linked and unit-linked	22,622
Life index-linked and unit-linked	0
Deposits to cedants	127,357
Insurance and intermediaries receivables	261,132
Reinsurance receivables	107,567
Receivables (trade, not insurance)	308,417
Own shares (held directly)	0
Amounts due in respect of own fund items or initial fund called up but not yet paid in	0
Cash and cash equivalents	144,163
Any other assets, not elsewhere shown	0
Total assets	8,155,875

	Solvency II value
Liabilities	C0010
Technical provisions - non-life	4,453,398
Technical provisions - non-life (excluding health)	4,375,959
TP calculated as a whole	0
Best Estimate	3,950,053
Risk margin	425,906
Technical provisions - health (similar to non-life)	77,439
TP calculated as a whole	0
Best Estimate	66,855
Risk margin	10,584
Technical provisions - life (excluding index-linked and unit-linked)	96,252
Technical provisions - health (similar to life)	393
TP calculated as a whole	0
Best Estimate	41
Risk margin	352
Technical provisions - life (excluding health and index-linked and unit-linked)	95,859
TP calculated as a whole	0
Best Estimate	82,495
Risk margin	13,364
Technical provisions - index-linked and unit-linked	
TP calculated as a whole	0
Best Estimate	0
Risk margin	0
Contingent liabilities	0
Provisions other than technical provisions	5,393
Pension benefit obligations	25,803
Deposits from reinsurers	23,671
Deferred tax liabilities	1,959
Derivatives	24,561
Debts owed to credit institutions	
Financial liabilities other than debts owed to credit institutions	
Insurance & intermediaries payables	64,469
Reinsurance payables	22,849
Payables (trade, not insurance)	370,968
Subordinated liabilities	1,592,677
Subordinated liabilities not in BOF	0
Subordinated liabilities in BOF	1,592,677
Any other liabilities, not elsewhere shown	0
Total liabilities	6,682,001
Excess of assets over liabilities	1,473,875

S.05.01.02

Premiums, claims and expenses by line of business

Non-life

	Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)												Line of business for: accepted non-proportional reinsurance				Total
	Medical expense insurance	Income protection insurance	Workers' compensation insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Credit and suretyship insurance	Legal expenses insurance	Assistance	Misc. financial loss	Health	Casualty	Marine, aviation and transport	Property	
	C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130	C0140	C0150	C0160	C0200
Premiums written																	
Gross - Direct Business	0	2,510		217,021	44,370	73,365	271,023	565,368	52,463	10,776	753	430					1,238,078
Gross - Proportional reinsurance accepted	909	42,391		5,296	3,626	2,174	54,530	12,342	13,702			-97					134,871
Gross - Non-proportional reinsurance accepted													13,271	103,201	33,755	144,914	295,141
Reinsurers' share	39	1,192		14,491	2,008	5,695	34,010	146,989	5,122	1,356	755	16	511	17,765	32,152	23,845	285,946
Net	870	43,709		207,826	45,987	69,843	291,542	430,721	61,043	9,420	-1	317	12,760	85,436	1,604	121,069	1,382,146
Premiums earned																	
Gross - Direct Business	0	1,698		216,521	43,113	71,947	271,447	552,445	51,798	10,435	997	977					1,221,377
Gross - Proportional reinsurance accepted	909	19,676		5,288	3,811	2,122	54,181	12,892	13,137			-97					111,919
Gross - Non-proportional reinsurance accepted													12,905	98,907	28,034	148,977	288,822
Reinsurers' share	39	1,206		18,899	2,639	9,274	81,297	167,327	6,748	3,051	992	109	521	19,495	29,666	33,531	374,795
Net	870	20,168		202,910	44,285	64,795	244,331	398,010	58,187	7,384	4	770	12,383	79,412	-1,632	115,446	1,247,323
Claims incurred																	
Gross - Direct Business	245	725		234,844	40,043	29,523	133,511	310,839	17,991	5,295	41	6,251					779,307
Gross - Proportional reinsurance accepted	1,307	10,869		3,954	2,216	1,141	26,032	10,634	5,245			9					61,408
Gross - Non-proportional reinsurance accepted													924	74,513	21,995	39,141	136,572
Reinsurers' share	6	129		66,166	8,317	15,234	60,701	117,672	945	1,037	30	-1,271	23	19,465	18,438	-1,901	304,989
Net	1,546	11,465		172,632	33,942	15,430	98,843	203,801	22,291	4,259	11	7,531	901	55,048	3,558	41,042	672,298
Changes in other technical provisions																	
Gross - Direct Business																	0
Gross - Proportional reinsurance accepted																	0
Gross - Non-proportional reinsurance accepted																	0
Reinsurers' share																	0
Net																	0
Expenses incurred	-473	8,010		70,707	15,590	20,091	102,162	188,141	30,578	2,346	103	1,000	2,873	27,739	2,699	31,888	503,453
Other expenses																	0
Total expenses																	503,453

S.05.01.02

Premiums, claims and expenses by line of business

Life

	Line of Business for: life insurance obligations						Life reinsurance obligations		Total
	Health insurance	Insurance with profit participation	Index-linked and unit-linked insurance	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	Health reinsurance	Life reinsurance	
	C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0300
Premiums written									
Gross							1,361	28,433	29,794
Reinsurers' share								2,106	2,106
Net							1,361	26,327	27,688
Premiums earned									
Gross							1,361	28,433	29,794
Reinsurers' share								2,106	2,106
Net							1,361	26,327	27,688
Claims incurred									
Gross						9,402	1,161	20,344	30,907
Reinsurers' share						1,642		1,431	3,073
Net						7,760	1,161	18,913	27,834
Changes in other technical provisions									
Gross									0
Reinsurers' share									0
Net									0
Expenses incurred							125	6,295	6,420
Other expenses									0
Total expenses									6,420

S.05.02.01

Premiums, claims and expenses by country

Non-life

	Home Country	Top 5 countries (by amount of gross premiums written) - non-life obligations			Top 5 countries (by amount of gross premiums written) - non-life obligations		Total Top 5 and home country
	C0010	C0020	C0030	C0040	C0050	C0060	C0070
		FR	IT	ES	BE	DE	
	C0080	C0090	C0100	C0110	C0120	C0130	C0140
Premiums written							
Gross - Direct Business	962,065	107,570	48,039	31,665	713	30,849	1,180,902
Gross - Proportional reinsurance accepted	2,018	16,523	5,049	15,080	25,041	3,698	67,409
Gross - Non-proportional reinsurance accepted	16,464	40,610	6,220	5,229	19,761	8,729	97,013
Reinsurers' share	153,560	31,132	10,577	9,905	3,521	8,250	216,944
Net	826,987	133,571	48,730	42,070	41,995	35,026	1,128,379
Premiums earned							
Gross - Direct Business	949,083	105,666	47,437	31,103	709	30,542	1,164,540
Gross - Proportional reinsurance accepted	1,861	15,612	5,030	8,601	16,702	2,860	50,665
Gross - Non-proportional reinsurance accepted	16,896	39,307	5,994	4,802	19,401	8,294	94,695
Reinsurers' share	209,258	37,560	14,980	11,840	3,999	11,363	289,001
Net	758,582	123,025	43,481	32,665	32,813	30,333	1,020,899
Claims incurred							
Gross - Direct Business	669,261	30,728	51,871	5,660	1,633	6,131	765,284
Gross - Proportional reinsurance accepted	738	18,749	488	-2,334	-15	2,327	19,953
Gross - Non-proportional reinsurance accepted	12,589	28,291	1,873	439	21,584	3,926	68,703
Reinsurers' share	225,405	13,568	22,338	2,182	2,878	2,287	268,658
Net	457,182	64,201	31,895	1,584	20,323	10,097	585,281
Changes in other technical provisions							
Gross - Direct Business							0
Gross - Proportional reinsurance accepted							0
Gross - Non-proportional reinsurance accepted							0
Reinsurers' share							0
Net							0
Expenses incurred	312,153	50,799	18,376	13,792	10,095	12,057	417,272
Other expenses							0
Total expenses							417,272

S.05.02.01

Premiums, claims and expenses by country

Life

	C0150	C0160	C0170	C0180	C0190	C0200	C0210
	Home Country	Top 5 countries (by amount of gross premiums written) - life obligations			Top 5 countries (by amount of gross premiums written) - life obligations		Total Top 5 and home country
		BE	ES	FR	US	JP	
	C0220	C0230	C0240	C0250	C0260	C0270	C0280
Premiums written							
Gross	873	10,475	3,220	2,256	2,127	2,100	21,050
Reinsurers' share	65	776	239	167	158	55	1,459
Net	809	9,699	2,981	2,088	1,969	2,046	19,592
Premiums earned							0
Gross	873	10,475	3,220	2,256	2,127	2,100	21,050
Reinsurers' share	65	776	239	167	158	55	1,459
Net	809	9,699	2,981	2,088	1,969	2,046	19,592
Claims incurred							0
Gross	85	8,872	1,470	3,791	2,733	2,353	19,304
Reinsurers' share	1,033	110	103	267	192	84	1,790
Net	-948	8,762	1,366	3,525	2,541	2,269	17,514
Changes in other technical provisions							
Gross							0
Reinsurers' share							0
Net							0
Expenses incurred	193	2,319	713	499	471	289	4,484
Other expenses							0
Total expenses							4,484

S.22.01.22

Impact of long term guarantees measures and transitionals

	Amount with Long Term Guarantee measures and transitionals	Impact of transitional on technical provisions	Impact of transitional on interest rate	Impact of volatility adjustment set to zero	Impact of matching adjustment set to zero
	C0010	C0030	C0050	C0070	C0090
Technical provisions					
Basic own funds					
Eligible own funds to meet Solvency Capital Requirement					
Solvency Capital Requirement					

S.23.01.22

Own Funds

Basic own funds before deduction for participations in other financial sector	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
	C0010	C0020	C0030	C0040	C0050
Ordinary share capital (gross of own shares)	996,078	996,078			
Non-available called but not paid in ordinary share capital at group level		0		0	
Share premium account related to ordinary share capital					
Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings					
Subordinated mutual member accounts					
Non-available subordinated mutual member accounts at group level			0	0	0
Surplus funds		0			
Non-available surplus funds at group level		0			
Preference shares					
Non-available preference shares at group level			0	0	0
Share premium account related to preference shares					
Non-available share premium account related to preference shares at group level			0	0	0
Reconciliation reserve	111,418	111,418			
Subordinated liabilities	1,592,677		448,230	1,144,447	
Non-available subordinated liabilities at group level			0	0	0
An amount equal to the value of net deferred tax assets	84,397				84,397
The amount equal to the value of net deferred tax assets not available at the group level	49,331				49,331
Other items approved by supervisory authority as basic own funds not specified above					
Non available own funds related to other own funds items approved by supervisory authority		0	0	0	0
Minority interests (if not reported as part of a specific own fund item)		0	0	0	0
Non-available minority interests at group level		0	0	0	0
Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds					
Deductions for participations in other financial undertakings, including non-regulated undertakings carrying out financial activities	1,165,439	1,165,439	0	0	
whereof deducted according to art 228 of the Directive 2009/138/EC		0	0	0	
Deductions for participations where there is non-availability of information (Article 229)		0	0	0	0
Deduction for participations included by using D&A when a combination of methods is used		0	0	0	0
Total of non-available own fund items	49,331				49,331
Total deductions	1,214,770	1,165,439			49,331
Total basic own funds after deductions	1,569,800	-57,942	448,230	1,144,447	35,066
Ancillary own funds					
Unpaid and uncalled ordinary share capital callable on demand					
Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand					
Unpaid and uncalled preference shares callable on demand					
A legally binding commitment to subscribe and pay for subordinated liabilities on demand					
Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC					
Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC					
Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC					
Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC					
Non available ancillary own funds at group level					
Other ancillary own funds					
Total ancillary own funds					
Own funds of other financial sectors					
Credit Institutions, investment firms, financial insitutions, alternative investment fund manager, financial institutions	1,165,439	1,165,439	0	0	
Institutions for occupational retirement provision		0	0	0	0
Non regulated entities carrying out financial activities		0	0	0	
Total own funds of other financial sectors	1,165,439	1,165,439			

S.23.01.22

Own Funds

Basic own funds before deduction for participations in other financial sector	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
	C0010	C0020	C0030	C0040	C0050
Own funds when using the D&A, exclusively or in combination of method 1					
Own funds aggregated when using the D&A and combination of method		0	0	0	0
Own funds aggregated when using the D&A and combination of method net of IGT		0	0	0	0
Total available own funds to meet the consolidated group SCR (excluding own funds from other financial sector and from the undertakings included via D&A)	1,569,800	-57,942	448,230	1,144,447	35,066
Total available own funds to meet the minimum consolidated group SCR	1,534,734	-57,942	448,230	1,144,447	
Total eligible own funds to meet the consolidated group SCR (excluding own funds from other financial sector and from the undertakings included via D&A)	675,522	-57,942		733,465	0
Total eligible own funds to meet the minimum consolidated group SCR (group)	58,695	-57,942		116,638	
Minimum consolidated Group SCR	583,188				
Ratio of Eligible own funds to Minimum Consolidated Group SCR	209.90%				
Total eligible own funds to meet the group SCR (including own funds from other financial sector and from the undertakings included via D&A)	1,840,961	1,107,496		733,465	0
Group SCR	1,466,930				
Ratio of Eligible own funds to group SCR including other financial sectors and the undertakings included via D&A	125.50%				

Reconcilliation reserve	C0060
Excess of assets over liabilities	1,473,875
Own shares (held directly and indirectly)	0
Forseeable dividends, distributions and charges	120,000
Other basic own fund items	1,080,475
Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	21,887
Other non available own funds	140,095
Reconciliation reserve	111,418
Expected profits	
Expected profits included in future premiums (EPIFP) - Life business	16,374
Expected profits included in future premiums (EPIFP) - Non- life business	305,146
Total Expected profits included in future premiums (EPIFP)	321,520

S.25.03.22

Solvency Capital Requirement - for groups on Full Internal Models

Unique number of component	Component description	Calculation of the Solvency Capital Requirement
C0010	C0020	C0030
10300I	Interest rate risk	91,526,695
10400I	Equity risk	31,773,674
10600I	Property risk	13,282,837
10700I	Spread risk	116,076,912
10900I	Currency risk	68,241,674
11040I	Other market risk (Liquidity risk)	6,065,964
19900I	Diversification within market risk	-146,222,339
20100I	Type 1 counterpart default risk (Reinsurance credit risk)	247,812,118
20200I	Type 2 counterparty default risk (Premium credit risk)	16,713,487
29900I	Diversification within counterparty risk	-16,535,023
50130I	Premium risk	470,850,377
50240I	Reserve risk	733,986,882
50300I	Non-life catastrophe risk	397,892,781
59900I	Diversification within non-life underwriting risk	-494,704,152
70190I	Operational risk (excluding group risk)	178,249,633
70110I	Group risk	60,900,018
79900I	Diversification within operational risk	-45,206,451
8049AI	Net asset value of QBE Corporate	25,370,000
8049BI	Debt servicing costs net of loan repayments	109,673,380
8049CI	Capital supporting financing companies	133,546,090
8049DI	Capital adjustments	22,572,451
80110P	Total pension risk including market and pension benefit risks	169,642,555

S.25.03.22

Solvency Capital Requirement - for groups on Full Internal Models

Calculation of Solvency Capital Requirement	C0100
Total undiversified components	2,191,510
Diversification	-724,580
Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	0
Solvency capital requirement excluding capital add-on	1,466,930
Capital add-ons already set	0
Solvency capital requirement	1,466,930
Other information on SCR	
Amount/estimate of the overall loss-absorbing capacity of technical provisions	0
Amount/estimate of the overall loss-absorbing capacity ot deferred taxes	0
Total amount of Notional Solvency Capital Requirements for remaining part	0
Total amount of Notional Solvency Capital Requirement for ring fenced funds	0
Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	0
Diversification effects due to RFF nSCR aggregation for article 304	0
Minimum consolidated group solvency capital requirement	583,188
Information on other entities	
Capital requirement for other financial sectors (Non-insurance capital requirements)	
Credit institutions, investment firms and financial institutions, alternative investment funds managers, UCITS management companies	0
Institutions for occupational retirement provisions	0
Capital requirement for non- regulated entities carrying out financial activities	0
Capital requirement for non-controlled participation requirements	0
Capital requirement for residual undertakings	0

Appendix B. Glossary

The following table details the definition of the terms and acronyms used in this document:

Term or Acronym	Definition
SFCR	Solvency and Financial Condition Report
RSR	Regular Supervisory Report
QRT	Quantitative Reporting Template
QBE EO	QBE European Operations plc
IFRS	International Financial Reporting Standards
IDW	Investment Data Warehouse
EOIC	European Operations Investment Committee
RCC	Risk and Capital Committee
RCG	Risk and Capital Group
ORSA	Own Risk & Solvency Assessment
CMG	Compliance Management Group
RDS	Realistic Disaster Scenario
FMG	Finance Management Group
UMG	Underwriting Management Group
AMSB	Administrative, Management or Supervisory Body
IBNR	Incurred but not reported reserve
IBNER	Incurred but not enough reported reserve
RMS	Risk Management Solutions
Bootstrapping	An actuarial modelling technique
Mack	An actuarial modelling technique
Hertig	An actuarial modelling technique
CPI	Consumer Price Index
SIMR	Senior Insurance Managers Regime
CRO	Chief Risk Officer
OMG	Operations Management Group
ERM	Enterprise Risk Management

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