SOLVENCY AND FINANCIAL CONDITION REPORT 2016

VHI INSURANCE DAC

Table of Contents

Summary

Vhi Insurance DAC ("Vhi Insurance" or the "Company") is Ireland's leading health insurance company by market share. Vhi Insurance recorded a strong financial performance for the year ending 31 December 2016. It is the Company's first full financial year since it secured authorisation as an insurance undertaking from the Central Bank of Ireland (the "Central Bank"). This is also the first year that the Company has reported under Solvency II, which came into effect on 1 January 2016.

In 2016 Vhi Insurance continued to provide a range of innovative health insurance services to its customers. The Company has a comprehensive network of professional healthcare providers, delivering the highest quality of healthcare to support its customers to live longer, stronger and healthier lives. In addition to the Company's focus on assuring the highest quality of care and medical outcomes, it also seeks to ensure affordability of private medical insurance ("PMI") in Ireland, therefore, continuously pursuing cost containment and efficiency programmes.

The Irish PMI market is community rated. This means that an 80 year old is charged the same as a 25 year old, regardless of their health status. More needs to be done to protect the community rated PMI market with legislation that ensures that it is equally attractive to insure an 80 year old as it is to insure a 25 year old. Risk Equalisation is a common mechanism used in countries with community rated health insurance systems, to equitably spread the higher claims costs associated with older and sicker customers, across all private health insurers. Typically insurers with higher numbers of younger and healthier customers make transfer payments to other insurers who bear higher claims costs associated with a disproportionate number of older and sicker customers. Risk equalisation transfers are between insurance companies, therefore, there is no incremental cost to policyholders.

Community rated PMI markets all over the world are supported by robust risk sharing schemes that eliminate the incentive to compete on the basis of risk selection. The focus of health insurance companies should be on the efficient management of customers' healthcare needs, as well as healthcare innovation to drive improved clinical outcomes and increased efficiencies across the system. This requires the introduction of a robust health status measure within the Risk Equalisation Scheme ("RES"), which provides incentives for insurers to manage claims efficiently while also delivering better healthcare outcomes for patients. The current market dynamics in Ireland do not incentivise the right behaviours, as health insurers now compete on risk pool selection, seeking to attract the younger, profitable age segments, with less focus on the effective management of quality and cost of care. While Vhi Insurance welcomes the changes announced in November 2016, the RES requires further and continued enhancement to ensure the Irish PMI industry is focused on healthcare quality and efficiency for customers.

Ireland has one of the youngest populations in Europe, however, its population is also ageing faster than any other country in the EU. This means that Ireland will experience a growth of people aged 65 and over of approximately 40% in the next ten years. This pace of ageing will raise a number of challenges for Ireland in funding and delivering high quality healthcare.

Vhi has agreed a strategic direction for the next 5 years, which will offer customers a distinct healthcare proposition that meets their needs for convenient and affordable access to the best quality care and well-being services that are relevant to their stage in life. As Ireland's leading health insurance provider, Vhi Insurance is already driving change and developing solutions which it is believed can be progressively rolled-out across the market to the benefit of all.

Business and Performance

In 2016, Vhi Insurance grew its PMI membership and continued to invest in product innovation and customer engagement platforms. The successful execution of the annual operations plan which supports Vhi Insurance's multi-year business strategy helped to contribute to these positive results. These successes have been achieved despite the on-going challenges presented by persistent low yields, population ageing and medical inflation.

Vhi Insurance generated a profit for the financial year of €31,368k, compared with €20,365k during 2015. It achieved this strong result through improved gross written premium of €1,447,809k (2015: €1,426,569k) contributed to by achieving a PMI membership increase to 1,069k (2015: 1,068k). In addition, through focus on claims cost management, Vhi Insurance paid claims of €1,353,251k (2015: €1,392,183k), delivering a high quality service to customers.

Vhi Insurance is the first health insurance company to conclude and sign a Memorandum of Understanding ("MoU") with the Health Service Executive ("HSE") and publicly funded hospitals in relation to submission of claims. This arrangement provides earlier visibility of claims, leading to more certainty and accuracy in claims provisioning, overall reducing the Company's risk profile.

The Company seeks to manage its underwriting risk and associated capital requirements through a number of measures, including reinsurance and subordinated debt. During 2016, as part of a multi-year arrangement with National Indemnity Company, part of the Berkshire Hathaway group, expiring during 2017, Vhi Insurance has ceded 30% of its premium. In addition, the Company raised subordinated debt of €90,000k during 2015, of which €38,900k was repaid early without penalty during 2016.

Administration cost, the cost the Company incurs in running its business was €124,801k during 2016, approximately similar to 2015. This represents a significant achievement considering the range of demands on its business as Vhi Insurance invests to deliver for customers and implements change to comply with the evolving regulatory environment.

Vhi Insurance had total financial investments at 31 December 2016 of €1,142,899k. This represented an increase of €8,324k compared with 2015 and was impacted by the decision to repay €38,900k subordinated debt. As always, preserving asset value, as well as maintaining sufficient allocation in liquid assets to meet commitments and claims payments, dictated investment philosophy. During 2016, the Company transferred all of its investments onto a single consolidated custodial platform, enhancing its ability to monitor, control and report on its investments.

Overall, the Company's reserves increased by €57,368k or 11.6% to €551,936k during 2016. This comprises share capital and retained earnings which were enhanced during the year by profit of €31,368k and a capital contribution from Vhi Insurance's holding company, Vhi Group DAC.

+ Further Information Section A. Business and Performance

System of Governance

Vhi Insurance is subject to regulatory oversight by the Central Bank together with associated European and national legislation. The Company developed and implemented appropriate systems of governance prior to its authorisation to enable it to comply with these requirements, including the Central Bank's Corporate Governance Requirements for Insurance Undertakings.

The Company has fully engaged in a programme of thematic and company specific reviews as well as inspections (on site and desk based) undertaken by the Central Bank and conducted across the business. The Company has participated in the implementation of Central Bank findings and recommendations.

As a subsidiary of a state body (through its immediate parent Vhi Group DAC) the Company is subject to and complies with the provisions of the Code of Practice for the Governance of State Bodies that are applicable to it. This Code was published in 2009 and revised during 2016. Vhi Insurance complies with the 2009 Code and has availed of an option to effect compliance with the revised code in respect of its financial reporting for year ending 2017 and thereafter.

The Health Insurance Authority ("HIA") is a statutory regulator of the PMI market, its principal responsibility is to ensure that health insurers operate in compliance with the key principles of community rating, open enrolment, lifetime cover and minimum benefits. Vhi Insurance's PMI products are subject to HIA regulation.

In accordance with the Companies Act 2014, the directors have issued a Directors Compliance Statement in the Annual Report for year ending 31 December 2016.

+ Further Information Section B. System of Governance

Risk Profile

The principal risks and uncertainties of Vhi Insurance have been determined by assessing potential risks to capital, value, investments, insurance, operations and reputation, compliance and conduct. The Company's risk tolerance levels are recorded in the Risk Appetite Statement which is approved by the Board of Vhi Insurance. Risks are monitored and managed on an ongoing basis and overseen by the Board. In 2016, the outlook for operational risk increased in the area of cyber-attack risk. Competition and inadequate Risk Equalisation are factors which have increased the Company's value risk. "Brexit" and the risks from protectionist politics have added to economic uncertainty and market risk. From an underwriting and insurance risk perspective the risk of under reserving for unidentified claims liabilities has reduced.

Vhi Insurance's ORSA

Solvency II requires that Vhi Insurance conduct an Own Risk and Solvency Assessment ("ORSA"), the purpose of which is to identify Vhi Insurance's risks, conduct stress tests on these and, thereby, determine an appropriate level of solvency capital to protect policyholders and other beneficiaries. This capital level is referred to as the Solvency Capital Requirement ("SCR").

The conclusion of this assessment is that the standard formula, adjusted for Vhi Insurance's own assessment of risk, is appropriate for the Company. The capital cover projected over the medium term demonstrates that the Company is well capitalised and projects continued compliance with Solvency II capital maintenance requirements and risk appetite tolerances approved by the Board. The Company will continue to progress its risk management plans consistent with risk appetite.

Health underwriting risk is the biggest contributor to the level of solvency capital required to be held by Vhi Insurance and relates to the risk of premiums and reserves for insurance liabilities being insufficient to pay claims and for the risk of catastrophic events. Market risk refers principally to the risks to which the Company's investment portfolio is exposed, including equity risk, concentration risk, spread risk, interest rate risk and property risk.

+ Further Information Section C. Risk Profile

Valuation for Solvency Purposes

Vhi Insurance prepares its financial statements in accordance with Financial Reporting Standards 102 & 103 ("FRS 102 & FRS 103") issued by the Financial Reporting Council for use in Ireland ("GAAP").

For Solvency II, all assets and liabilities held at the reporting date are valued according to the rules prescribed in the Solvency II regulations. Additionally, the prescribed headings required for Solvency II disclosures differ from those used by the Company in its statutory financial statements. These differences are immaterial with the exception of the insurance technical provisions, reinsurance recoverables and deferred tax assets and liabilities.

The valuation bases for technical provisions differ between the statutory financial statements and Solvency II. This valuation is detailed in section D.2. The revaluation of the technical provisions under Solvency II gives rise to a revaluation of the related reinsurance and deferred tax assets and liabilities and these are detailed in sections D.1 and D.3.

+ Further Information Section D. Valuation for Solvency Purposes

Capital Management

It is a regulatory requirement that Vhi Insurance maintain a prudent level of capital which will not compromise its ability to meet its current or future commitments to policyholders and other beneficiaries. The Company acknowledges that the maintenance of an appropriate level of capital is fundamental to meeting its regulatory and legal obligations to policyholders, shareholders and its ongoing business objectives.

Capital management is used to determine the optimal mix of capital by type (i.e. common equity, reinsurance, subordinated debt) given the risk profile and performance objectives for the Company. In order to support this objective a Medium Term Capital Plan is prepared by the Company annually and approved by the Board. Vhi Insurance's ORSA and its Medium Term Capital Plan were approved by the Board during April 2016.

It is currently the policy of the Board that any distributions in the form of dividends are kept within the Vhi group and not made externally. No distributions were made by Vhi Insurance during 2016.

The capital coverage at year end 2016 is within the preferred risk appetite range for the Company and exceeds the minimum requirement under Solvency II.

At 31 December 2016, the Company had Eligible Own Funds of €772,170k, comprising Tier 1 funds generated principally from accumulated insurance underwriting profits of €735,118k and €5,000k in equity and Tier 3 own funds of €32,052k, comprising the eligible portion of the Company's subordinated debt instrument.

The Company's Basic Own Funds (the nominal value of its regulatory capital instruments) and its Eligible Own Funds (that portion of Basic Own Funds permitted as regulatory capital under Solvency II) for the year ending 31 December 2016 were €791,218k and €772,170k, respectively.

A capital contribution of €26,000k from Vhi Group DAC was made in December 2016 and €38,900k of Tier 3 basic own funds (subordinated debt) was repaid in December 2016. Of the balance of subordinated debt outstanding at 31 December 2016 of €51,100k, €32,052k is eligible as regulatory capital under Solvency II.

+ Further Information Section E. Capital Management

A.
BUSINESS AND PERFORMANCE

A.1 Business

This is a solo Solvency and Financial Condition Report ("SFCR") for Vhi Insurance Designated Activity Company trading as "Vhi Insurance" for year end 31 December 2016. This report is required annually in accordance with Solvency II requirements to disclose information with regard to the solvency and financial condition of Vhi Insurance.

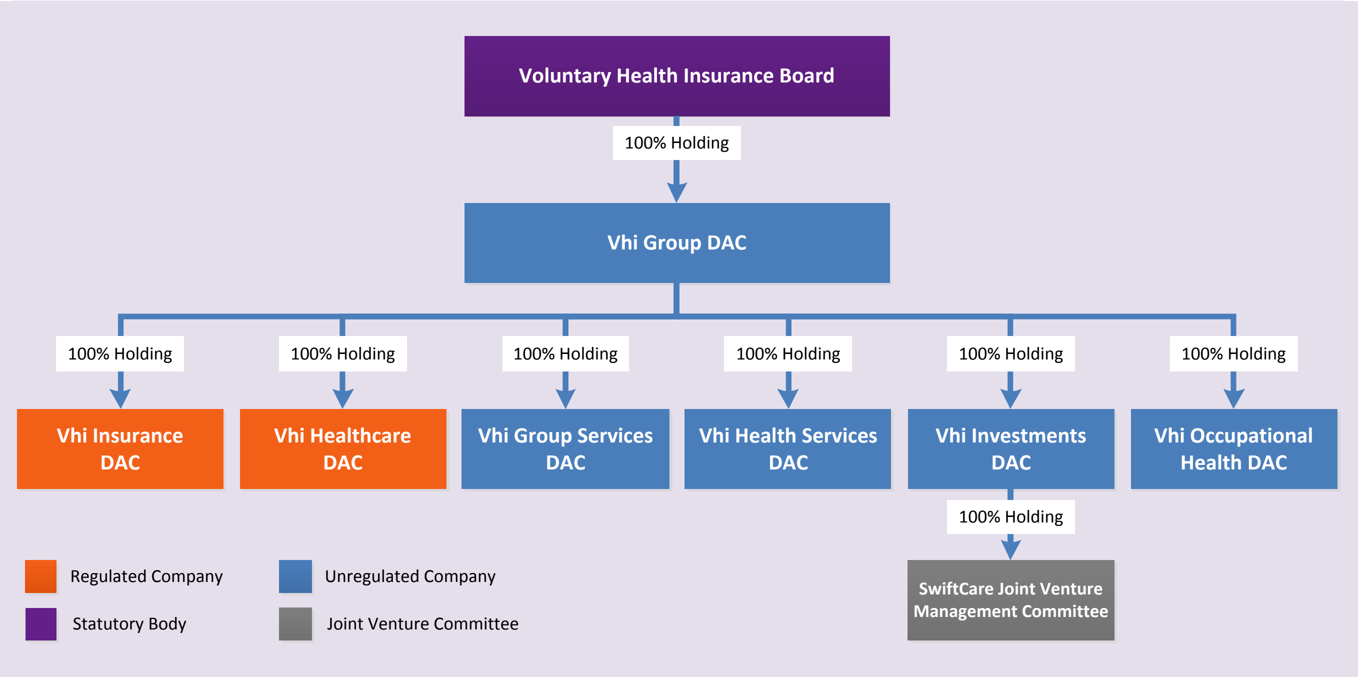
Supervisory Authority	The Central Bank of Ireland
Supervisor Contact Details	PO Box 559, New Wapping Street, North Wall Quay, Dublin 1
External Auditor	Deloitte & Touche
External Auditor Contact Details	Earlsfort Terrace, Dublin 2

This report was approved by the Board of Vhi Insurance on 25 April 2017 following recommendation from the Audit Committee. Sections D and E of this report and the related Quantitative Reporting Templates attached have been subject to external audit.

A.1.1 Vhi Insurance DAC and the Vhi group

Vhi Insurance DAC is a part of the Vhi group, which operates exclusively in the Republic of Ireland. The corporate structure of the group and details of the activities of each entity in the group is summarised below.

Vhi Insurance DAC and the Vhi group, as at 31 December 2016



The Voluntary Health Insurance Board is a statutory body established under the Voluntary Health Insurance Act 1957. The Board oversees the activities of the Vhi group.

Vhi Group DAC is a wholly owned subsidiary of the Voluntary Health Insurance Board and acts as a holding company for the wholly owned subsidiaries within the Vhi group.

The active subsidiaries are:

- **Vhi Insurance DAC** is a regulated subsidiary which trades as "Vhi Insurance". It is the Relevant Subsidiary for the purposes of the Voluntary Health Insurance (Amendment) Act 2008 and carries on the health insurance business as a regulated non-life insurance undertaking. PMI, which is classified under Solvency II as medical expense insurance, is the Company's only line of business.

  Company Number: 527606 Registered Office: Vhi House, Lower Abbey St., Dublin 1

  Vhi Group DAC is the sole shareholder of Vhi Insurance DAC. There are no other direct shareholders of Vhi Insurance DAC.

  The Voluntary Health Insurance Board, which holds shares in Vhi Group DAC, is an indirect qualifying shareholder of Vhi Insurance DAC. The shareholding of the State is held through the Voluntary Health Insurance Board. The Minister for Health is the "sponsoring" Minister of the Voluntary Health Insurance Board and is not strictly a shareholder, as no shares have ever been issued by the Voluntary Health Insurance Board. However, in the current regulatory context, in terms of ownership and control, the Minister could be considered to be the ultimate qualifying shareholder of Vhi Insurance DAC.

- **Vhi Healthcare DAC** is a regulated insurance intermediary which trades as "Vhi Healthcare". It is responsible for selling PMI products and other insurance products on behalf of the underwriter which are all provided on a tied agency basis with Vhi Insurance DAC, Collinson Insurance Services Limited, Great Lakes Insurance SE, UK branch and Astrenska Insurance Limited.

  Company Number: 527604 Registered Office: Vhi House, Lower Abbey St., Dublin 1

- **Vhi Group Services DAC** is a subsidiary which provides support services to the other subsidiaries in the Vhi group on the basis of intra-company service agreements viz., Vhi Insurance DAC, Vhi Healthcare DAC, Vhi Health Services DAC and Vhi Investments DAC.

  Company Number: 538110 Registered Office: Vhi House, Lower Abbey St., Dublin 1

- **Vhi Health Services DAC** is a subsidiary which provides occupational health services, employee assistance programmes and a range of homecare treatments for hospital-in-the-home care for a variety of conditions.

  Company Number: 474622 Registered Office: Waverly Office Pk., Old Naas Rd., Dublin 12

- **Vhi Investments DAC** is a subsidiary which has a 50% interest in Vhi SwiftCare, a joint venture operation (unincorporated) with Arás Sláinte Limited (trading as Centric Health), specialising in the management of minor injury clinics.

  Company Number: 531499 Registered Office: Vhi House, Lower Abbey St., Dublin 1

- **Vhi Occupational Health DAC** is a subsidiary which provides employed healthcare professional resources, on a secondment basis, to Vhi Health Services DAC.

  Company Number: 461202 Registered Office: Vhi House, Lower Abbey St., Dublin 1

No changes were made to the corporate structure of the Vhi group in 2016. Further information on the entities within the group is available from Vhi.ie.

A.2 Underwriting Performance

Vhi Insurance's overall underwriting performance has improved from 2015 to 2016. The table below gives a summary of the key components of the Company's underwriting performance for the respective accounting years and the factors contributing to the improvement in underwriting performance in 2016 are outlined in the subsequent notes.

Underwriting Performance	**Notes**	**2016 €'000**	**2015 €'000**
Gross premium earned	1	1,430,308	1,427,525
Other technical income gross	2	83,691	70,432
Gross claims incurred	3	(1,327,986)	(1,292,636)
Operating expenses	4	(124,801)	(123,965)
Reinsurance	5	(20,239)	(61,023)
Total underwriting result		**40,973**	**20,333**

Reconciliation of the total underwriting result to the Financial Statements		**2016 €'000**	**2015 €'000**
Total underwriting result		40,973	20,333
Net investment income	See A3	3,853	7,019
Balance on the health insurance technical account		**44,826**	**27,352**

+ Further Information Section A.3 Investment Performance

Note 1: Gross Premium Earned

The total sales (gross written premium) of Vhi Insurance was €1,447,809k for 2016, an increase of €21,240k year over year. Earned premium income (gross earned premium) increased by €2,783k over the previous year. The increase in income was driven in part by increasing membership to 1,069k customers (2015: 1,068k).

Note 2: Other Technical Income - Risk Equalisation Scheme

Other technical income includes the net impact of risk equalisation premium credits, hospital utilisation credits and levies under the RES. This increased in 2016 by €13,259k to €83,691k. One of the main drivers of this increase was the natural ageing of the customers for whom Vhi Insurance receives credits under the scheme.

During 2016, the Minister for Health announced changes to Risk Equalisation levies and credits, in particular a 10% increase in the levy on insurance policies renewed or entered into between 1 April 2017 and 31 March 2018. Vhi Insurance supports the Government policy of community rating and the enactment of the Health Insurance (Amendment Act) 2016 which represents further progress in assuring affordable health insurance for older and sicker customers and supports a sustainable community rated market.

Note 3: Gross Claims Incurred

Gross claims incurred represents the estimated cost of claims which occurred during the year together with changes in estimate for prior years. This increased by €35,350k in 2016 to €1,327,986k.

The Company has experienced volatility in claims submissions and increased claims costs from public hospitals during 2016. This is principally attributable to the implementation of the Health Amendment Act 2013 which increased the charges raised by public hospitals in respect of services rendered to patients with PMI and who elect to be charged as a holder of PMI.

Some of the other key drivers of increases in claims costs are:

- New medical innovations and treatments
- Increases in hospital capacity and utilisation
- Ageing population

Note 4: Operating Expenses

Operating expenses consist of a combination of acquisition costs and administration expenses. They have remained largely consistent year on year for Vhi Insurance. This represents a significant achievement considering the range of demands on the Company as it invests to deliver for its policyholders and implement change as the regulatory environment evolves.

Note 5: Reinsurance

Vhi Insurance has a multi-year reinsurance arrangement with National Indemnity Company, part of the Berkshire Hathaway group. During 2016, the Company has ceded 30% of its earned premium income. There has been a reduction in the cost of reinsurance between 2015 and 2016, a key driver being the impact of variations in the quota share ceded.

In Vhi Insurance's financial statements reinsurance is split out into its components to show the amount of the Company's premiums and claims that are ceded as well as showing other technical income net of reinsurance. In the underwriting summary above, the cost of reinsurance is summarised to illustrate the total cost to the Company.

The reinsurance contract is on a "funds withheld" basis whereby the Company retains premiums at least equal to the estimate of amounts receivable under the reinsurance contract at all times. This mitigates Vhi Insurance's risk of default by the reinsurer.

A.3 Investment Performance

The investment strategy of the Company prioritises capital protection over the earning of high investment returns and it is deemed that this is in the best interest of policyholders. As a result, the investment portfolio is primarily invested in debt securities and deposits in banks. There has been no material change during 2016 in the risk appetite and investment management mandate.

Vhi Insurance held €1,162,937k in investments as at 31 December 2016. The investment return net of investment expenses in 2016 was €3,853k compared to €7,019k in 2015. The year on year reduction in investment return can be attributed to a decline in yields on fixed income debt securities and reductions in interest rates on cash deposits.

Investment expenses included in the net return were €1,168k for 2016 compared with €828k for 2015. The increase in expenses resulted from the classification of negative interest, charged by banks on deposits as an investment expense in the financial statements.

The net return by asset class is shown in the table below:

Net investment return by asset class	**2016 €'000**
Equities - unlisted	443
Government Bonds	685
Corporate Bonds	1,353
Collateralised securities	(10)
Collective Investments Undertakings	(56)
Deposits other than cash equivalents	(607)
Property (other than for own use)	2,045
Total investment return by asset class	**3,853**

Income from property (other than for own use) is primarily made up of rent charged by the Company to other Vhi group companies for the use of properties that it owns.

A.3.1 Gains and/or Losses Recognised Directly in Equity

No gains or losses were recognised directly in equity in 2016.

A.3.2 Investments in Securitisation

Investments in securitised assets form a very small proportion of the total investment portfolio at 1.3% at year end 2016 (1.1% at year end 2015).

Investments in securitised assets	**2016 €'000**
At 1 January	12,551
Additions	3,500
Disposals	(761)
At end of year	**15,290**

A.4 Performance of Other Activities

Vhi Insurance had no other material income during the reporting period. The Company's other material expenses relate solely to financing costs directly attributable to subordinated debt. The table below shows the movement in interest expense year on year.

	2016 €'000	2015 €'000
Other Interest Expense	(7,860)	(3,595)

The main driver of the increase in interest expense is due to the timing in which the subordinated debt facility agreement commenced during 2015 compared with a full year during 2016.

A.4.1 Leasing Arrangements

Vhi Insurance had no financial or operating leasing arrangements in 2016.

A.5 Any Other Information

There are no additional significant events or material information regarding business and performance that have not been disclosed above.

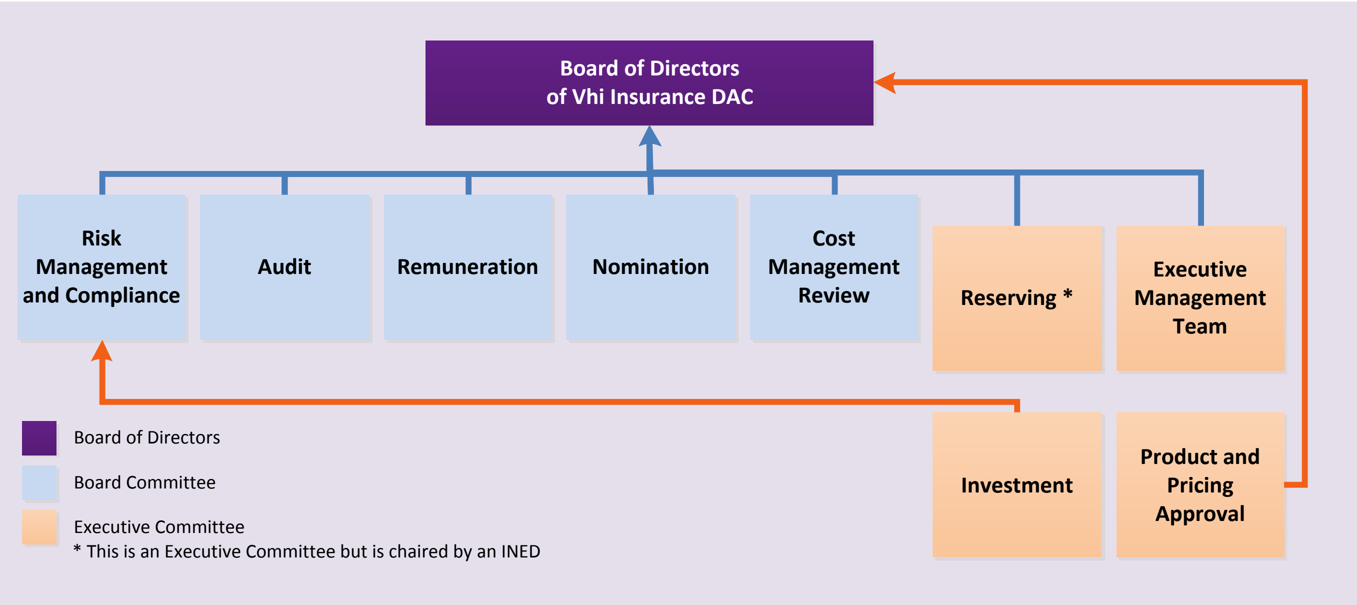
B.
SYSTEM OF GOVERNANCE

B.1 General Information on the System of Governance

The Board of Directors of Vhi Insurance (the "Board") believes an effective system of governance is essential for the appropriate management of the Company. It is committed to ensuring that the Company is well directed and managed in accordance with the high standards of governance required to deliver the sustained success of the business. The Company is subject to and complies with the relevant provisions of, the Central Bank's Corporate Governance Requirements for Insurance Undertakings, related regulations and codes. The Board attests to compliance with relevant requirements in annual Compliance Statements. Compliance, audit and risk management programmes are documented and monitored and reported upon. Accordingly, the Board considers the system of governance is adequate to the nature, scale and complexity of the risks inherent in its business.

The material components of the system of governance are described in the sections below.

The Board, Sub-Committees, Executive Management Team and Executive Committees, as at 31 December 2016



B.1.1 The Board of Directors of Vhi Insurance

The Board consists of 11 members (one vacancy), a majority (8) being independent non-executive directors ("INED") with 3 executive directors ("ED"). The Company considers the independence of a majority of its Board members to be a key feature to good corporate governance. All non-executive directors are deemed independent directors who can exercise sound judgement and decision making independent of the views of management, political interests or inappropriate outside interests.

The Board recognises that diversity is also key to its ability to function effectively by drawing on different skill sets, experiences, qualifications and other diversity factors to maximise understanding, identify different abilities, diverse perspectives and balance the decision-making process. The Board currently benefits from the broad professional and educational backgrounds of its directors, which collectively include accounting, actuarial, medical, financial, governance, risk management and regulatory experience as well as experience in both domestic and international organisations.

The Board believes it comprises an appropriate balance of executive and non-executive directors and is suitably qualified to meet its strategic objectives and any applicable regulatory requirements.

The Board of Directors of Vhi Insurance, as at 31 December 2016

Director	Type
Liam Downey (Chairman)	INED
John O'Dwyer (Chief Executive)	ED
Ruth Barrington	INED
Joyce Brennan	INED
Seamus Creedon	INED
Celine Fitzgerald	INED
Finbarr Lennon	INED
Declan Moran	ED
Paul O'Faherty	INED
Greg Sparks	INED
Brian Walsh	ED

There were no changes to the Board in 2016. Profiles for each Director are available on Vhi.ie.

The Role and Responsibilities of the Board

The Board is responsible for the effective, prudent and ethical oversight of the Company and the setting and oversight of:

- The Company's business strategy.
- The amounts, types and distribution of both internal capital and own funds adequate to cover the risks of the Company.
- The strategy for the on-going management of material risks.
- A robust and transparent organisational structure with effective communication and reporting channels.
- A remuneration framework that is in line with the risk strategies of the Company.
- An adequate and effective internal control framework.

The Board seeks to ensure it has:

- The necessary knowledge, skills, experience, expertise, competencies, professionalism, fitness, probity and integrity to carry out its duties.
- A full understanding of the nature of the Company's business, activities and related risks.
- A full understanding of members' individual direct and indirect responsibilities and collective responsibilities.
- An understanding of the Company's financial statements.

The Board gives effect to the above through receipt of management information, regular oversight of the business and an annual cycle of training and briefings, through the support of board sub-committees and executive committees and by having in place policies and structures to enable the appointment of appropriate personnel.

Reserved Powers and Delegated Authority

The Board reserves certain key matters for itself and delegates others (within specified limits) to board sub-committees and to the Chief Executive, who in turn delegates authority to executive committees and management. The Terms of Reference of the Board stipulate which decisions are reserved for the Board and which decision-making powers they have chosen to delegate.

Vhi Insurance has a delegated authority framework which includes processes and structures which are reviewed on an ongoing basis whereby it identifies those situations in which it is appropriate to use delegations of authority to ensure the effective management of the business and the procedures that should be followed when such delegations are made.

The Company recognises that the carrying out of certain roles and activities requires specific skills, knowledge and expertise, and should only be performed by suitably competent people. It is on this basis that individuals are delegated the authority to perform tasks and this delegation comes from the top down.

B.1.2 Board and Committee Structure

The Board delegates authority to a number of committees and the Executive Management Team ("EMT"), who act on behalf of the Board in respect of certain matters. Each committee has detailed Terms of Reference that articulate the role and position of the committee in the governance framework. The Terms of Reference are reviewed annually by the committees to ensure continuing appropriateness. All Terms of Reference are approved by the Board and require Board approval for material alteration.

Committee	Meeting Frequency	Responsibilities
Risk Management and Compliance Committee	Quarterly	Promote the overall effectiveness of corporate governance including a culture of compliance and risk management, and in particular monitor and review the scope, effectiveness, resources and activities of the Risk Management and Compliance functions. In addition, ensure that the Risk Appetite Statement is appropriate to the strategy and risk appetite of the Company and its business; review annually the Own Risk and Solvency Assessment ("ORSA") and review and recommend for approval of the Board the annual Compliance Plan.
Audit Committee	Quarterly	Provides an independent review of financial reporting and satisfies itself as to the effectiveness of the Company's internal controls and as to the sufficiency of external and internal audits. In addition, it monitors the activities of the Internal Audit Function and approves the annual Audit Plan.
Remuneration Committee	Twice Annually	Monitors and makes recommendations to the Board with regard to the Company's overall performance management and reward philosophy for the Chief Executive, the EMT and other senior executives i.e. those that report to the Chief Executive, those categories of staff whose professional activities have a material impact on the Company's risk profile and any such other executives the Board may determine, and ensures they are consistent and aligned with the Company's strategic objectives. The annual remuneration levels for the Chairman and each non-executive Director of the Voluntary Health Insurance Board are set by Government. The Chairman and non-executive directors of the Board of Directors of Vhi Insurance are remunerated on the same basis as the Voluntary Health Insurance Board. Executive board members do not receive remuneration for their roles on the Board. The Chairman and non-executive directors are not remunerated for each chairmanship/directorship they hold in the Vhi group. They are remunerated for one position only.
Nomination Committee	Twice Annually	Monitors and makes recommendations to the Board of Vhi Group DAC on the composition of the Board of Vhi Insurance and in accordance with the Skills Matrix and Diversity Policy, making proposals for succession planning for its membership and for identifying and recommending executive and non-executive candidates for appointment to Board positions.
Cost Management Review Committee	Twice Annually	Acts as a consultative group with the Chief Executive to review and evaluate cost management initiatives undertaken by management with particular reference to claims cost management and overhead management and supports the Chief Executive in seeking to promote effective cost management within the Company.

Committee	Meeting Frequency	Responsibilities
Reserving Committee	Quarterly	An advisory and oversight committee which has primary responsibility for the booking of reserves, considering quarterly the adequacy of the reserves, related governance, data and control considerations, making recommendations on the Board approved Reserving Policy and ensuring compliance with it. In addition, it reviews annually the Actuarial Report on Technical Provisions and the Peer Review Report.
Executive Management Team	Weekly	The EMT, in conjunction with the Chief Executive, is the decision-making unit to which is delegated day-to-day running of the Company. It is responsible for, in conjunction with the Board, the effective, prudent and ethical oversight of the Company, the development of the business strategy for consideration by the Board, the execution of the agreed strategy and ensuring that risk and compliance are properly managed.
Investment Committee	Quarterly	Advises on the management of the Company's funds to ensure they align with investment policy, solvency requirements and risk considerations. It keeps under review, monitors and makes recommendations to the Board on investment policy, the investment mandate, the investment managers and the custodian.
Product and Pricing Approval Committee	Quarterly	Ensures that overall product margins, set by the Board, are achieved either through pricing or benefit design. It reviews product profitability and the competitiveness of the product portfolio. The committee also has authority to approve material changes to the health insurance portfolio including product, price and rule changes or medical changes in accordance with certain limits set by the Board.

B.1.3 Key Functions

Vhi Insurance has four key functions, Risk Management, Internal Audit, Compliance and Actuarial.

Key Functions and Reporting Lines, as at 31 December 2016

Key Function	Main Roles and Responsibilities
Internal Audit Function	Provides an independent appraisal service to the Board and management. It provides independent assurance on the adequacy and effectiveness of the system of internal control and elements of the system of governance. Where appropriate, this role extends to the relevant controls surrounding outsourced service providers and other external parties, as well as the Company's own internal controls. **+ Further Information** Section B.5
Risk Management Function	Oversees the operation of the risk management system, is responsible for setting methodologies and standards to enable business units to identify, measure, monitor and manage their own risks and for providing advice, support and challenge to business units in relation to risk and associated controls. In addition, the function also monitors and reports on the overall risk profile of the Company, including new and emerging risks in addition to monitoring the effectiveness of adherence to the requirements of the risk management system. **+ Further Information** Section B.3
Compliance Function	Oversees and ensures that the Company is being operated in compliance with legislation and regulation, and with approved internal compliance processes and procedures. The function monitors the compliance risk of the Company and provides compliance advice, support and challenge to the business units of the Company in addition to coordinating the management, remediation and implementation of regulatory requirements. **+ Further Information** Section B.4.3
Actuarial Function	Coordinates the calculation of the technical provisions, capital management and supports the provision of pricing and management information. The function is accountable for setting actuarial methodology, reporting to the Board on the adequacy of reserves and capital requirements, and on the adequacy of underwriting and reinsurance arrangements. **+ Further Information** Section B.6

Vhi Insurance is committed to ensuring an effective structure is in place providing for cooperation and information sharing between key functions; however, each has defined responsibilities as set by the Board. The four key functions are integrated into the group organisational structure in a way that seeks to ensure no undue influence, control or constraint is exercised on the functions with respect to the performance of their duties and responsibilities by other functions, senior management or the Board. Each key function maintains operational independence by sharing no personnel with other functions and ensure no conflicts of interest arise between key function personnel and activities they undertake. Each key function is led by a senior manager, employed by Vhi Insurance, who is assessed to ensure s/he are 'fit and proper', are of good repute and who is approved for appointment by the Central Bank. Key function personnel are required to have the appropriate skills, qualifications and experience to fulfil the requirements of their roles.

Each key function reports directly to a committee chaired by an INED of the Board. Each function has the necessary authority and appropriate standing within the Company, as well as unrestricted access to all relevant information necessary to carry out its responsibilities and sufficient resources to discharge its role. Confirmation of these arrangements being in place are provided by the heads of the key functions to relevant committees. The Chief Risk Officer ("CRO") and Head of Compliance may meet privately with the Chairperson of the RMCC annually. The Head of Internal Audit meets privately with the Chairperson of the Audit Committee on a number of occasions annually and the head of each key function also has direct access to the Board Chairman, as required. Each function provides regular scheduled reports to their reporting committee and may escalate issues of concern to the committee or the Board, as deemed appropriate. The Board receives copies of the reports provided to the respective committees and are provided with updates as to the activities of the key functions from the chairpersons of the committees.

B.1.4 Material Changes in the System of Governance

The system of governance was reviewed and updated in advance of the authorisation of Vhi Insurance in 2015. No material changes were made to the system in 2016.

B.1.5 Material Transactions with Shareholders, with persons who exercise a significant influence on Vhi Insurance and/or with members of the Board

Shareholders	Vhi Insurance has one shareholder, Vhi Group DAC. The Company entered into an intercompany loan agreement with Vhi Group DAC in 2015 for €90,000k. Of this €38,900k was repaid during 2016, leaving the loan balance at €51,100k at 31 December 2016.
Persons who exercise a significant influence on Vhi Insurance	There were no material transactions with any persons who exercise a significant influence on Vhi Insurance in 2016.
Members of the Board of Directors of Vhi Insurance	There were no material transactions with members of the Board of Directors of Vhi Insurance in 2016.

B.1.6 Remuneration Policy and Practices

Vhi Insurance's remuneration policies seek to ensure that the approach to remuneration is aligned with the Company's operations, business environment, strategic objectives, effective risk management, best practice and any regulatory or legislative requirements.

Remuneration policies are designed to attract, retain and motivate personnel of the required calibre for the successful delivery of the Company's strategic and operational objectives. The remuneration framework and policy is kept under review to ensure they remain fit for purpose and are consistent with and promote sound and effective risk management. The remuneration arrangements for Board members and the EMT are set out in section B.1.2. The table below sets out the Company's remuneration framework which incorporates four components.

Fixed Pay Components	
Fixed Remuneration (Base Pay)	Vhi Insurance aims to clearly define expected performance through a structured system of performance management and uses this as the basis for remuneration decisions. Any remuneration increases made are in line with National Wage Agreements or other collective negotiation procedures, subject to the Company's ability to pay. Performance is reviewed at least annually. Fixed remuneration also includes specific role required supplements including car and travel allowances which are provided in accordance with approved expenses and company car policies.
Pensions	Pension schemes for Vhi Insurance personnel are linked to the Voluntary Health Insurance Board, the ultimate parent entity of Vhi Insurance. The general terms of the pension schemes are subject to collective bargaining agreements and oversight from the Department of Health and the Department of Public Expenditure and Reform. The Scheme Rules of the Vhi groups pension schemes do not permit supplementary pension or early retirement schemes.
Benefits	Personnel are provided with a range of benefits based on individual employment contracts and market practice.
Variable Pay Components	
Performance Based Remuneration	Performance based remuneration is subject to the achievement of individual qualitative objectives, in certain cases quantitative objectives and the business performance of Vhi Insurance and the wider Vhi group. It is carefully managed with objectives designed and balanced to ensure they foster an appropriate culture that unwanted behaviour, including excessive risk taking, are not incentivised. There are no contractual commitments to pay a minimum level of performance based remuneration.

There are no options for directors, executive management or personnel to acquire shares or share options in Vhi Insurance.

B.2 Fit and Proper Requirements

Vhi Insurance adheres to the Central Bank's fitness and probity regime which sets minimum standards aimed to ensure that all persons who effectively run the Company, or have other key functions, are at all times competent and capable, act honestly, ethically and with integrity and are financially sound. In addition to complying with these minimum standards Vhi Insurance applies its own internal business requirements and standards and is responsible for ensuring that personnel meet the required standards, both on joining the Company and throughout their career with Vhi Insurance.

The Company requires Board members and personnel to meet Vhi's ethical standards and to have the qualifications, skills and experience which are essential for them to carry out their duties and responsibilities. Vhi Insurance gives effect to the fitness and probity regime through a Fitness and Probity Standards Policy and supporting processes. The Company has identified and documented in the Fitness and Probity Standards Policy Vhi roles which are subject to the fitness and probity regime as controlled functions.

For appointments to the Board of Directors of Vhi Insurance, the Nomination Committee take full account of the Central Bank's fitness and probity requirements and Corporate Governance Requirements for Insurance Undertakings, in addition to Vhi Insurance's internal requirements, when making recommendations for Board vacancies. The Committee take into consideration factors including but not limited to; the time commitment required for the role, the challenges and opportunities facing the Company, possible conflicts of interests, the independence of any proposed non-executive director and the balance of executive and non-executive directors on the Board. In addition, the evaluation of persons for Board positions is supported by a Diversity Policy and Skills Matrix, which seek to ensure the Board consists of members with diversity of backgrounds, viewpoints, skills, knowledge and expertise to meet both current and future anticipated needs and enable sound and prudent management of the Company.

With regard to Vhi Insurance personnel in controlled functions, required role specific competencies are set out in written job descriptions. Assessment of applicants against role specific requirements, in addition to their ethical and culture fit for Vhi, are carried out during the recruitment process, which includes both internal assessment and an external verification processes. If a candidate meets the role requirements due diligence checks are carried out. They include, but are not limited to, copies of relevant qualifications and transcripts, professional body checks, previous employer reference checks, self-certification of potential conflicts of interest, regulatory checks and judgement searches, as relevant. Compliance with minimum competency code requirements and concurrent responsibilities are also checked, as relevant.

Certain candidates for controlled functions are subject to pre-approval by the Central Bank before appointment (PCFs), including members of the Board and the heads of key functions. Before taking up a PCF position the candidate must complete and submit an Individual Questionnaire to the Central Bank for their consideration. If approval is not given the candidate is not appointed to the position.

The fitness and probity assessment processes are carried out in advance of position offers and appointments. The assessment process for Board members is facilitated by the Nomination Committee, Head of Compliance and the Department of Health. The assessment process for other key function holders is carried out by the Head of Compliance and HR Function.

Vhi Insurance does not allow a person to perform a controlled function unless it is satisfied that the person complies with the fitness and probity requirements of the Central Bank and has agreed to abide by them on an ongoing basis. This includes a commitment to continuing their professional development and continuing in their roles is contingent on their retention of required qualifications. Annually, persons in controlled functions attest to their continuing to meet the fitness and probity requirements of the Central Bank. Personnel, including Board members or another key function holders, who no longer meet fitness and probity requirements can be removed from their position.

B.3 Risk Management System including the Own Risk and Solvency Assessment

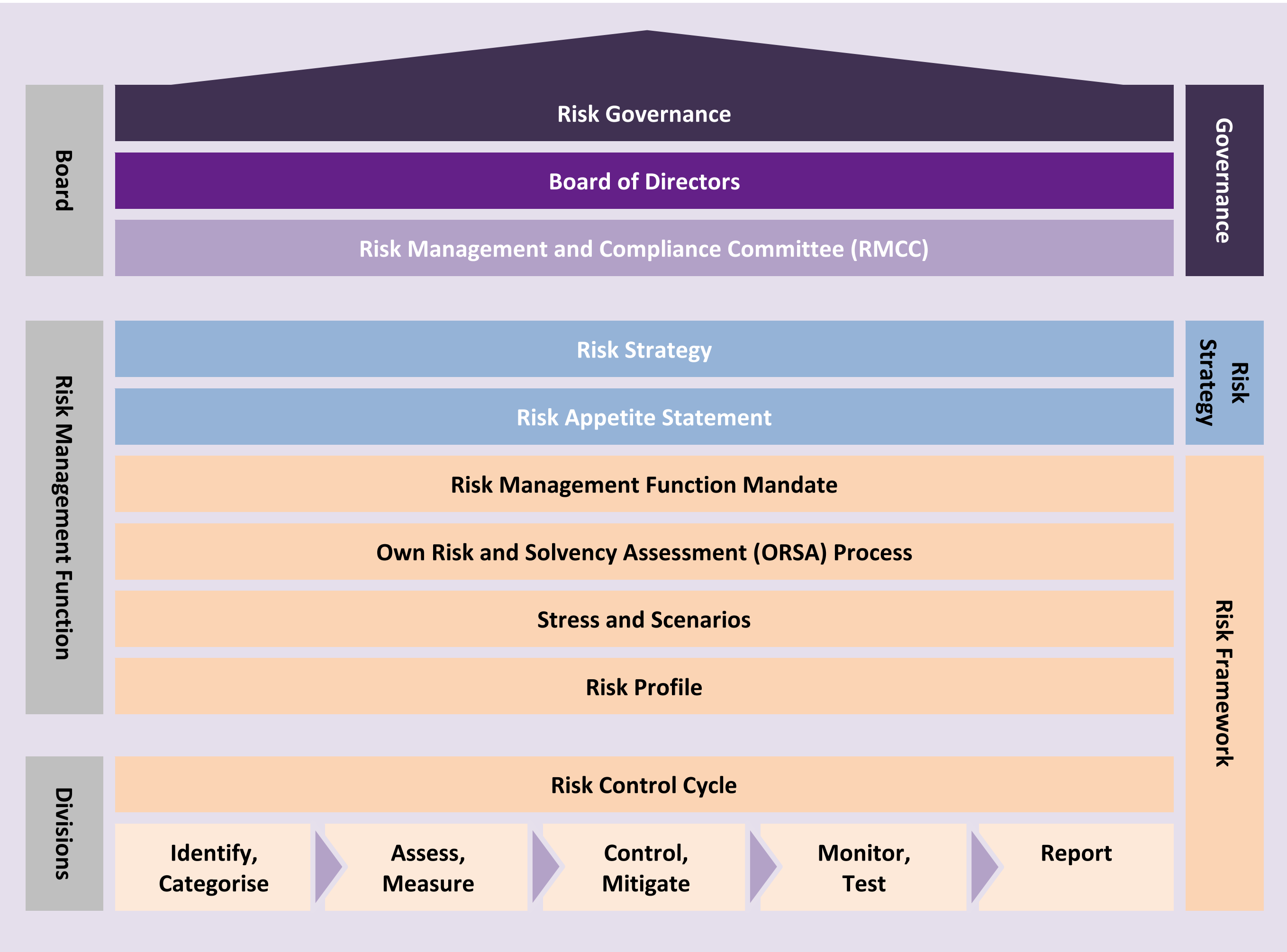
B.3.1 The Risk Management System

Vhi Insurance is subject to internal risks arising from its business operations and external risks arising from economic conditions in Ireland and global financial markets in general, as they affect the PMI sector.

Delivering on the strategic intent of the Company requires an understanding of the nature and significance of the risks to which it is exposed. This enables Vhi Insurance make the best decisions for the Company, customers and providers and enables it to sustainably deliver on its purpose into the future.

Vhi Insurance operates a Risk Management System which ensures an integrated and consistent approach to managing risk with processes to identify, measure, control, monitor and report on risks to enable the achievement of the Company's goals and objectives. This is implemented through a 'three lines of defence' approach, described in section B.4.1, to manage risk; incorporating roles, responsibilities and accountabilities including governance and risk based decision-making.

Vhi Insurance Risk Management System



The Risk Management System is underpinned by:	
Risk Governance	The practice, procedures, attitudes and approaches to enable the consistent and effective operation and oversight of the management of risk. It includes rules, oversight, control and assurance in the management of risk principally through the setting of risk appetite, policies, roles and responsibilities with a 'three lines of defence' model and oversight provided through reporting processes.
Risk Strategy	The Risk Management Strategy aims to: • Protect the Company's assets and prospects and take the right risks. • Take calculated financial risks to address competitive exposures in the Company's business model. • Take appropriate risks to support the achievement of higher returns. • Avoid risks that could fundamentally damage the Company's capital base. • Accept operational risk where it is appropriately managed and reduce it where it is cost effective to do so. • Minimise any significant clinical, reputation and compliance risks. These objectives seek to ensure that risks stay within risk appetite tolerances over the medium to long term planning horizon with risks managed to enhance risk weighted value.
Risk Appetite Statement	The level and type of risk the Company is prepared to accept to achieve its goals with limits and tolerances set for the main business risks. Risk appetite informs the strategy, business planning and operational processes and seeks to ensure their execution is in line with the risk appetite parameters set by the Board.
Risk Framework	Components of the framework include: • Risk Management Function Mandate. • Own Risk and Solvency Assessment ("ORSA") process including stress and scenario testing. • Risk profile. • Processes through which risk is managed as a continuous cycle of activity and enables understanding of the nature and significance of the risks (at an individual and aggregated level) to which the Company is exposed, including the sensitivity to those risks and its ability to mitigate them.

Enterprise Risk Management ("ERM") is the methodology and process, which seeks to understand and manage risk, to support the achievement of the Company's objectives and minimise the effects of risk on capital requirements, by addressing the full spectrum of risks the Company is exposed to and managing the combined impact of those risks. The processes supporting ERM are described below.

Enterprise Risk Management (ERM) Life Cycle/ Risk Control Cycle

Risk Framework	
1. Identify and Categorise	Risks, including emerging risks, are identified at business unit (bottom-up) and organisational (top-down) level.
2. Assess and Measure	Risks are assessed in terms of likelihood of occurrence and impact, with key risk indicators and underlying drivers considered, to determine how they interact. Where risk appetite tolerance breaches or risk events are identified, a mitigation plan is put in place with controls assessed to determine adequacy and effectiveness. Business change proposals are subject to a risk assessment to seek to ensure proposals are in line with risk appetite before the change is implemented.
3. Control and Mitigate	Controls are implemented to mitigate risk. Control effectiveness is assessed on a regular basis, with shortcomings reported to the Risk Management Function. Risk assessments of business change proposals consider control adequacy and effectiveness. The regular review and aggregation of risks identifies the amount of capital the Company requires and any requirement for additional controls.
4. Monitor and Test	The business units monitor key risk indicators and underlying risk factors regularly to inform risk self-assessments, which includes an assessment of control adequacy and effectiveness. The Risk Management Function review and challenge these risk self-assessments. The internal and external auditors test key controls and processes. The EMT and Board review the material risks, controls, mitigation plans and capital adequacy on a regular scheduled basis.
5. Report	Risk reporting is a key component of the ERM Life Cycle including regular (e.g. risk assessments) and ad-hoc (e.g. risk appetite tolerance breaches, risk events) reporting by business units to the Risk Management Function. The Risk Management Function provides the Board with a regular update on the effectiveness of the Risk Management System including details of the material risks facing the Company and managements implementation of mitigating actions. This is provided through the risk appetite, risk profile, control framework and incident reporting.

B.3.2 How the risk management system including the risk management function are implemented and integrated into the organisational structure and decision-making

The Board is ultimately responsible for ensuring an appropriate Risk Management System is in place, implemented on a consistent basis and embedded across the Company. Oversight on the appropriateness and effectiveness of the Risk Management System is underpinned by a governance framework which includes:

- An organisational structure with responsibilities delegated from the Board to management.
- Clear Terms of Reference for the Board, its sub- committees and executive committees.
- Right of access for the CRO to the Board and reporting on specific areas of risks initiated at the request of the Board or on the initiative of the Risk Management Function.
- Ownership of policies, to oversee adherence and compliance.

The four key functions, as detailed in section B.1.3, play a significant role in ensuring the effectiveness of the Risk Management System. These functions retain responsibility for taking the decisions necessary for the proper performance of their duties without interference from other functions, senior management or the Board.

Risk Appetite	Risk appetite makes explicit the Board's risk management requirements. The Risk Appetite Statement focuses on the following areas: • Managing financial strength. • Engaging in sustainable business activity. • Operating in an effective and efficient manner. • Treating customers in a responsible, fair and compliant manner. The Risk Appetite Statement is reviewed at least annually and in the event of material changes to the Company's activities or operating environment. Decision making in running the business is necessitated by change, including strategic change and changes in the business environment, with a risk assessment performed on business change proposals.
Risk Policies	Risk policies define the high level rules, standards and underlying principles for the management of risk. These policies are reviewed at least annually or where there is a material change to risk appetite.
Risk Framework	The 'bottom-up' approach to identifying, measuring, monitoring, controlling and reporting on risks the Company is, or could be, exposed to, occurs on an ongoing basis with reporting at least quarterly to the EMT and the Board. This includes a focus on emerging risks, control adequacy and effectiveness, business change and mitigation plans. The 'top-down' approach considers the nature and significance of the risks (at an individual and aggregated level) to which the Company is exposed, including the sensitivity of the Company to those risks and its ability to mitigate them.
Own Risk and Solvency Assessment ("ORSA") Process	The ORSA process is a continuous process comprising annual and recurring activities, undertaken at various times throughout the year, that consider risk and capital impacts on decision making and in particular business and financial planning. **+ Further Information** Section B.3.3

B.3.3 The ORSA

The ORSA process assesses the main risks to Vhi Insurance, including relevant considerations from the wider Vhi group, and determines appropriate capital requirements by projecting the potential impact of these risks over the medium term.

The 3 year period under which solvency cover is projected and assessed aligns with the strategic planning processes for 2016. The planning process considers the key financial and capital metrics over the period. To aid this assessment the plan is stressed for risks that Vhi Insurance is or could be exposed to. A number of stresses and scenarios are developed to test the planning process and to determine the potential impacts on capital requirements and solvency cover. The stresses and scenarios selected cover the material risks (insurance, market, credit, liquidity, operational risks) which the Company is or could be exposed to and are designed to be plausible and sufficiently challenging in order to provide a sound basis upon which to assess the overall solvency needs of the Company.

The ORSA process comprises annual and recurring activities undertaken over the year which informs decisions on strategy, growth, risk control and capital. The activities are:

Annual Activities	Recurring Activities
• Business planning • Risk appetite review • Stress and scenario testing • Risk policies review	• Financial reporting • Capital projections • Risk assessment

The key components of the ORSA process are:

Risk Identification	Material risks are identified and informed by risk assessments conducted by business units and risks assessed as part of the strategic planning processes. This includes the consideration of emerging risks and trends.
Risk Assessment and Aggregation	Risk is considered on a forward looking basis to determine the capital requirements and solvency, informed by stress and scenario testing.
Results	The results highlight the appropriateness of solvency cover, resilience of capital to stress tests and adequacy of capital to meet risk appetite requirements. They provide insights to focus mitigation and contingency planning.
Report	The final output, the ORSA Report, documents the risk and solvency assessment and includes a prospective assessment of the solvency position.

The outcome of the process determines the adequacy of capital to continue to meet regulatory capital requirements and the Company's capital and risk appetite requirements over the period. It assists the Board and management in making decisions relating to strategy and planning, risk appetite changes, capital management and funding plans. Additionally, it informs management actions on growth, product development and pricing.

The ORSA process requires the engagement and participation of a wide group of stakeholders including the Board, management and, in particular, the Finance, Actuarial and Risk Management functions. Risk, capital and planning activities, performed by these functions, link the strategic management process with the decision making processes. In particular, the Board take an active part in directing the ORSA process including how the assessment is performed, challenging the results and recommending capital, contingency and de-risking plans based on the results and conclusions from the ORSA process. The Board review and challenge of the ORSA aims to ensure that a robust assessment of material risks facing the Company has been performed. This review also seeks to ensure risks that would threaten the Company's business model, financial performance and solvency have been appropriately accounted for and the Company can meet its obligations and liabilities over the period of the assessment.

An ORSA report is produced, at least annually, or more frequently where there is a significant change in the risk profile of the Company or for significant strategic decisions requiring Board approval. The CRO is responsible for the oversight and implementation of the ORSA process and for making a presentation on the report to the EMT and Board. Following Board approval of the annual ORSA Report it is submitted to the Central Bank.

B.4 Internal Control System

The Internal Control System within Vhi Insurance is designed to provide reasonable assurance regarding the achievement of business objectives. An effective internal control system increases the effectiveness and efficiency of operations, the reliability, completeness and accuracy of financial and non-financial data for reporting and aims to ensure compliance with legal and regulatory obligations. It can provide only reasonable, not absolute, assurance.

The Board is ultimately responsible for ensuring that adequate and effective internal controls exist within the Company. However, operational responsibility for management of this is devolved to board sub-committees and executive management which is responsible for establishing and maintaining adequate internal control.

For consistency internal control principles are set at a group level and apply group-wide in line with the Board Internal Control Policy. The recommendations of the following have been taken into account in establishing the systems of internal control:

- The Central Bank's Corporate Governance Requirements for Insurance Undertakings
- The Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)
- Solvency II
- The relevant provisions of the Code of Practice for the Governance of State Bodies

B.4.1 The Three Lines of Defence

Vhi Insurance operates a 'Three Lines of Defence' model which is used to structure roles and responsibilities for risk and control activity, including risk governance and risk based decisions-making within the business.

The Three Lines of Defence	
1st Line of Defence	The 1st line of defence incorporates all of the business functions which carry out the day-to-day operations of the Company. 1st line activities require personnel to operate in accordance with and adhere to policies and frameworks, to identify, manage and own risks and controls.
2nd Line of Defence	The 2nd line of defence develops, maintains and implements control policies and frameworks across the Company, undertakes monitoring of front line business operations along with advising, supporting and challenging the 1st line of defence. The Risk Management and Compliance functions are part of the 2nd Line of Defence.
3rd Line of Defence	The 3rd line of defence undertakes independent monitoring and assurance activities. The Internal Audit Function and external auditors provide the Board and management with independent objective assurance that the policies, various frameworks and controls in place are appropriate, proportionate and adequately adhered to across the group in the 1st and 2nd lines of defence.
Oversight	Although the Board, board sub-committees and the executive committees are not considered to be among the three "lines" in this model, they are the primary stakeholders served by the "lines," and they are the parties best positioned to help ensure that the three lines of defence model is reflected in the Company's risk management and control processes. They do this by overseeing the management of risk, the internal control system, setting policy and monitoring the performance of the key control functions, internal audit and any external assurance providers.

B.4.2 The Internal Control Framework

The Internal Control Policy sets out the principles, expectations, philosophy and framework of internal control within the Vhi group for all personnel. The policy is intended to support the implementation and maintenance of a transparent and effective internal control system, underscored by accountability, sufficient in terms of the group's business scale and complexity and facilitating the accomplishment of the group's business goals. The Internal Control Framework of Vhi Insurance has five key elements, in line with the COSO internal control principles.

Components of the Internal Control Framework	
1. The Control Environment	The control environment is organisational culture. It provides the foundation for all other components of internal control and has a pervasive influence on all decisions and activities throughout the Company. It is the general attitude and behaviour towards internal control as set by the Board and executive management which influences the consciousness of Vhi personnel.
2. Risk Assessment	Risk assessment is the identification and analysis of the risks that the Company is exposed to in pursuit of its business objectives. It forms a basis for determining how the identified risks should be managed. Once risks have been assessed a determination can be made on the scale and nature of the internal controls that are required to prevent, detect or mitigate these risks. The aim is not necessarily to try and avoid risk but to be risk aware and to make risk-conscious decisions, understanding where risks are being taken and how much risk is regarded as acceptable in the pursuit of business objectives.
3. Control Activities	Control activities are the actions or process steps that help to ensure that management objectives are carried out in a risk-conscious manner. They are tools, both manual and automated which can prevent or reduce risk and encompass many activities such as approval and authorisation, reconciliations and segregation of duties, supervision, business continuity, back up and disaster recovery. Management and personnel develop and implement control activities that contribute to the mitigation of risks to acceptable levels, in line with the risk appetite of the Company. All levels of the Company and all functions have responsibility to undertake control activities as part of the internal control system.
4. Monitoring	Monitoring of internal control is an essential process that assesses the quality of internal control performance over time, to ensure they remain fit for purpose and are functioning as expected. Regular monitoring allows performance expectations to be established and any variances from these can be identified and investigated, potentially providing an early indicator of potential incidents. Monitoring and reporting are also used to provide the Board and executive management with the relevant information required for informed decision-making. Independent monitoring is undertaken by the 2nd and 3rd line functions on an ongoing basis throughout the year. This includes compliance monitoring, risk assessments, internal audits and reviews by external assurance providers such as the external auditors. This monitoring supplements self-assessment monitoring and testing conducted by functions.
5. Information and Communication	Vhi Insurance recognises that a good system of communication is essential for the Company to maintain an effective system of internal control. The communication of relevant information supports decision making and the co-ordination of activities. Relevant information must be identified, captured and communicated within a timeframe, in a manner that enables personnel to carry out their duties and responsibilities. The upward dissemination of data from all three lines of defence ensures that the highest levels of the group are provided with a holistic view of the operations of the entire group and companies within it.

Through its internal control system, Vhi Insurance ensures all personnel are aware of their role in the system, thereby promoting the importance of performing appropriate internal controls for the sound operation of the business.

B.4.3. How the Compliance Function is Implemented

The role of the Compliance Function is to manage the overall compliance risk of Vhi Insurance and to support the Company to achieve its strategic objectives and:

- To conduct its business prudently and in accordance with both the letter and the spirit of relevant laws and regulation,
- To ensure compliance with those internal policies and standards, designed to achieve the Company's compliance objectives and
- To act ethically, professionally and with integrity, honestly and fairly in dealing with customers.

The Compliance Function is an independent 2nd line of defence assurance provider which reports to the RMCC, and administratively to the Chief Financial Officer. The planned activities of the function are detailed in an annual Compliance Plan which sets out the focus of the function for the coming year. The plan is presented annually to the Board, for approval on recommendation of the RMCC. A review and analysis of Vhi Insurance's compliance profile, along with a status update on progress against the Compliance Plan, are provided to the RMCC quarterly.

The Compliance Function maintains the standards and frameworks for compliance within which the Company operates and is responsible for management of overall compliance implementation and the compliance governance framework in the Company. The key activities of the function include, but are not limited to:

- Management of the compliance universe, including identification and assessment of the impact of any changes in legislation/regulation on Vhi Insurance and coordination of the implementation of business changes required.
- Overseeing, investigating and managing the reporting / escalation with the business of any potential or actual breaches of regulation.
- Guiding/overseeing compliance remediation programmes.
- Conducting compliance risk-based monitoring and themed reviews including sales monitoring of Vhi Insurance underwritten products, error and complaint activities and monitoring and reporting on actual or potential compliance breaches.
- Co-ordinating the delivery of responsibilities arising under the Company's relationship with regulators and guiding the business and management in this regard.
- Approval of various processes and documentation across product, advertising, sales and customer terms and conditions, information and literature.
- The provision of a Compliance helpline/ advice to business units.
- Development and maintenance of compliance documentation, including compliance policies, the Compliance Manual and procedural documentation related to compliance activities and structures.
- Managing the provision of induction and regulatory/compliance training, education and briefings and supporting management in the promotion of a compliant and ethical culture.
- Interacting with the other key functions, including in particular Risk Management and Internal Audit.

Vhi Insurance believes the Compliance Function has appropriate standing in the Company and has the authority and capability to undertake its role.

Compliance Function personnel are active members of the Association of Compliance Officers of Ireland.

B.5 Internal Audit Function

B.5.1 How the Internal Audit Function is Implemented

The role of the Internal Audit Function is to support the achievement of the Company's business objectives, by providing independent assurance on the adequacy and effectiveness of the system of internal control and identify areas where improvements in efficiency can be made. This role extends to the relevant controls surrounding outsourced service providers and other external parties.

The Internal Audit Function is an independent 3rd line of defence assurance provider which reports to the Audit Committee, and administratively to the Chief Executive. The planned activities of the function are detailed in an annual Audit Plan which sets out the focus of the function for the coming year. The plan is presented annually to the Audit Committee for its approval.

It is the policy of the Board that the function operates to the best national and international professional standards. The Internal Audit Function is given the multi-disciplinary resources necessary to effectively discharge its responsibilities. Audit personnel must comply with the integrity, objectivity, confidentiality and competency principles contained in the ethical guidelines from the Chartered Institute of Internal Auditors and where appropriate their own various professional associations.

The Internal Audit Function discharges its responsibilities by critically reviewing, on a risk focussed basis:

- The effectiveness and efficiency of the system of internal control.
- The reliability, timeliness and integrity of financial and operating information, and the processes used to identify, measure and report such information.
- Compliance with policies, plans, procedures, laws and regulations.
- The means for safeguarding assets and information, including information stored on computer systems and databases.
- The adequacy and effectiveness of management actions to address issues identified by both Internal Audit and the external auditors.

In carrying out its responsibilities the Internal Audit Function has unrestricted access to all information, explanations, records, assets and personnel necessary for audit purposes and is facilitated by management and personnel in this regard.

The Internal Audit Function is also responsible for ensuring that audit work takes due account of the potential for fraud and for investigating fraud, either suspected or uncovered, but it should be noted that internal audit personnel are not expected to have the expertise of any person(s) whose primary responsibility is detecting and investigating fraud.

Additionally, the Internal Audit Function evaluates and contributes to the improvement of governance and risk management processes.

In meeting its objectives, the Internal Audit Function liaises with the statutory auditors, external advisors, and the other key functions to ensure that assurance from all internal and external sources is, insofar as possible, managed in an integrated, complementary and cost-effective manner.

B.5.2 The Independence of the Internal Audit Function

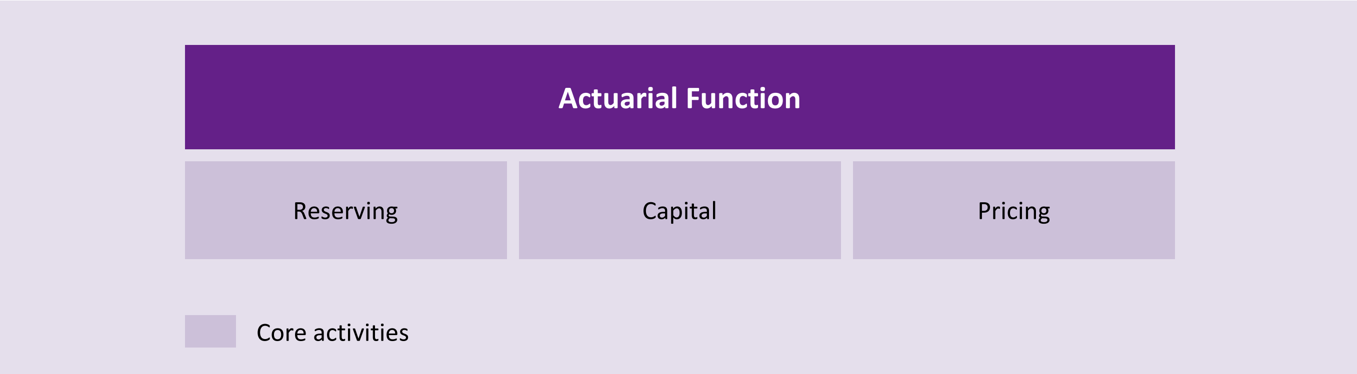
The independence of the Internal Audit Function is achieved:

- Through the objectivity of internal audit personnel.
- Through the absence of executive responsibility or authority over the activities or operations it reviews and audits.
- Through the avoidance of conflicts of interest and compliance with the Vhi Conflict of Interest Policy.
- By ensuring that internally recruited auditors do not audit activities or functions they previously performed during the timeframe covered by the audit.
- Through the functional reporting line to the Audit Committee and the administrative reporting line to the Chief Executive.
- Through attendance at meetings of the Audit Committee, including time alone with the Audit Committee on a yearly basis and otherwise as required.
- Through regular private meetings with the Chairperson of the Audit Committee.
- Through attendance at meetings of the RMCC.
- Through regular private meetings with the Chief Executive.
- Through right of access to the Board Chairman at any time.

B.6 Actuarial Function

B.6.1 How the Actuarial Function is Implemented

The Actuarial Function



The Actuarial Function supports the business primarily in three broad areas; reserving, capital and pricing. The function is overseen by the Head of Actuarial Function ("HoAF") who reports administratively to the Chief Financial Officer and is responsible for the management and reporting of actuarial matters to the Board.

The Actuarial Functions responsibilities include, but are not limited to:

- Coordination of the calculation of the Technical Provisions, both on an accounting and Solvency II basis. A key component of this process is the determination of the best estimate Outstanding Claims Reserves ("OSCR"), which is calculated using a number of standard actuarial reserving methodologies such as Basic Chain Ladder and Bornhuetter-Ferguson methods, using both paid and incurred data.
- Provision of a formal opinion on the adequacy of the Solvency II Technical Provisions. The Actuarial Opinion on Technical Provisions ("AOTP") and Actuarial Report on Technical Provisions ("ARTP"), which supports the AOTP, are provided to the Board annually by the HoAF.
- Management of the Board approved Reserving Policy for Vhi Insurance. The function prepares and presents an information pack to the Reserving Committee. The Reserving Committee meets quarterly to review the Technical Provisions for appropriateness and compliance with the Reserving Policy.
- Management of the Board approved Capital Management Policy for Vhi Insurance. The capital requirements of the Company are monitored continuously over the year through a number of processes either owned by the Actuarial Function or with input from the Actuarial Function.
- Annual preparation of a Medium Term Capital Plan which makes recommendations regarding capital management. The plan is submitted to the Board for approval.
- Calculation of the Solvency Capital Requirement ("SCR") on a quarterly basis and also on an ad-hoc basis as may be required.

The HoAF also provides the following to the Board annually:

- Actuarial opinion on the ORSA and the overall contribution to risk management.
- Actuarial opinion on the underwriting policy.
- Actuarial opinion on the reinsurance arrangements.

In addition to the provision of an actuarial opinion on the underwriting policy, the Actuarial Function is also responsible for monitoring the experience of the portfolio and making pricing recommendations.

The Actuarial Function activities undertaken throughout the year are presented in the Actuarial Function Report which is submitted to the Board annually.

B.7 Outsourcing

B.7.1 Outsourcing Policy

The Vhi group's Outsourcing Policy, which applies to Vhi Insurance, sets out the principles used to manage internal and external outsourcing within the Vhi group. The policy is intended to support the implementation and maintenance of an effective and ethical outsourcing regime which is sufficient and proportionate in terms of the Vhi group's business scale and complexity. It recognises that to conduct operations as effectively and efficiently as possible, it may be advantageous to outsource certain function or activities.

The policy addresses outsourcing responsibilities, due diligence to be performed, contractual requirements, risk management requirements and supervision and monitoring arrangements to be implemented regarding outsourcing. The policy requires the Board to approve the outsourcing of any critical or important operational functions or activities in advance of any contract being signed and for the Board to receive annual reports on the approved arrangements.

B.7.2 Outsourced Functions/Activities

Vhi Insurance outsources some critical or important operational functions or activities to outsourcing providers external of the Vhi group. Such external outsourced arrangements include:

- Investment management arrangements which are outsourced to professional investment managers located in Ireland.
- Claims data entry and claims third party recoveries which are outsourced to providers in Ireland.
- Claims coding which is outsourced to a provider in the Republic of Mauritius.
- Software testing which is outsourced to a provider in South Africa.

In addition to external outsourcing Vhi Insurance also engages in intra group outsourcing within the Vhi group. Services outsourced to other Vhi group companies include personnel for the key functions, Internal Audit, Risk Management, Compliance and Actuarial. Other internally outsourced critical or important operational functions include but are not limited to; Finance, Human Resources, IT, Legal and Secretarial, Marketing and Corporate Communications. All intra group services are carried out in Ireland.

Although not considered outsourcing, Vhi Insurance also has a tied agency agreement in place with Vhi Healthcare DAC, which acts as an insurance intermediary. The agreement allows Vhi Healthcare DAC to sell the insurance company's products to customers on its behalf.

B.8 Any Other Information

There is no additional material information regarding the system of governance that has not been disclosed above.

C.
RISK PROFILE

The risk profile of Vhi Insurance includes risks which could impact on the achievement of the Company's strategy and objectives, in particular those relating to strategic and value growth and conduct, reputation and compliance objectives. The main risks are underwriting risk, market risk, counterparty default risk and operational risk.

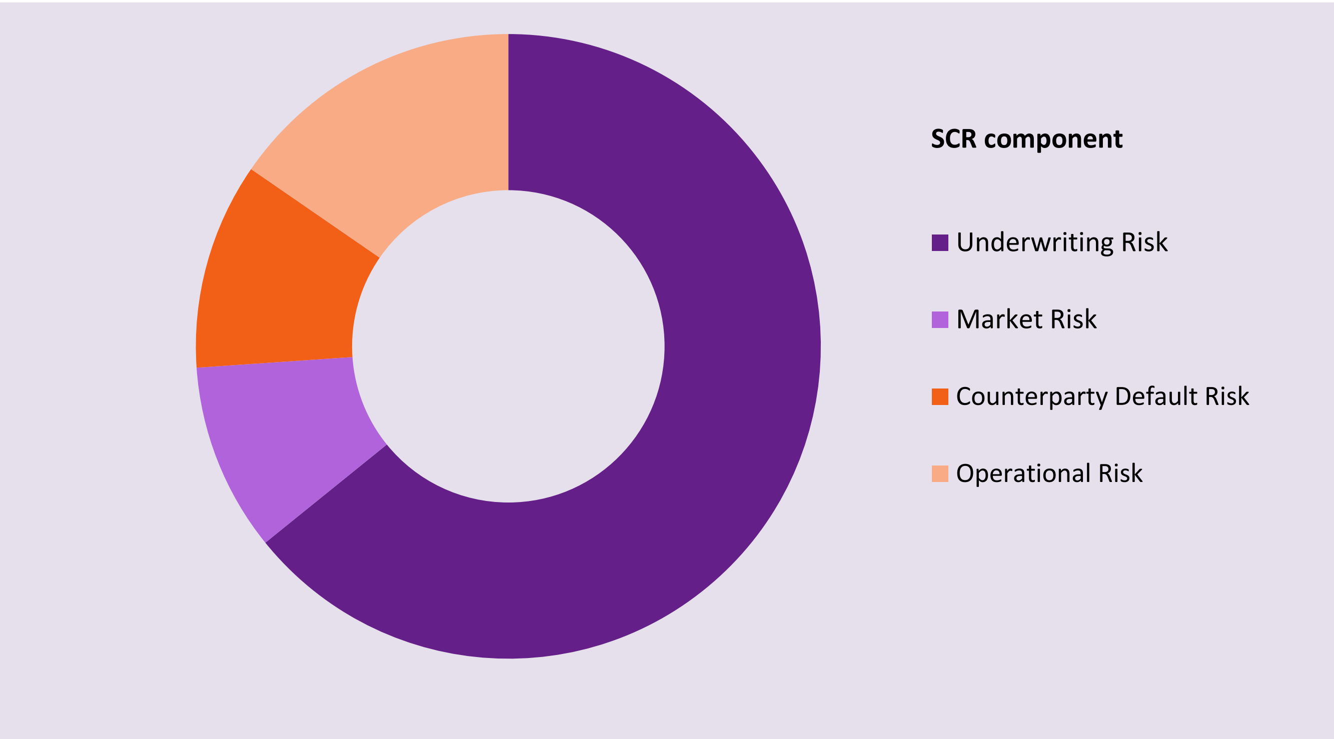
Vhi Insurance considers the RES in Ireland partially effective and requires further enhancement to ensure the industry is focused on healthcare quality and efficiency for customers. Additionally, it should ensure the RES does not place insurers covering a disproportionate share of higher risk older and less healthy policyholders at a competitive disadvantage.

Vhi Insurance actively seeks to be risk aware, understanding where risks are being taken and how much risk is regarded as acceptable in the pursuit of business objectives that provide a reasonable opportunity to earn a financial return. Risks are regularly reviewed through the ERM Life Cycle, incorporating the identification, measurement, assessment and reporting of risk to determine whether the Company is prepared to accept the risk and to consider the adequacy of planned mitigating actions.

A description of the main risks together with the strategies to mitigate risk is set out in this section.

Risk Exposure

The SCR capital calculation demonstrates the relative exposure to the different components of capital risk. Underwriting and operational risk are the main drivers of the SCR. Other components of the SCR include market risk and counterparty default risk.



+ Further Information The risk exposure by risk category is detailed in Section E.2 SCR and MCR

There are no off-balance sheet positions and no element of risk transferred to special purpose vehicles.

C.1 Underwriting Risk

Underwriting Risk

The risk that unexpected variations in frequency, size or timing of claims lead to reductions in financial returns

The main underwriting risks are:

Premium and Reserve Risk	Utilisation and Capacity Risk	Provider Agreement Risk	Competition and Regulation Risk

Risk Exposure	
Factors affecting risk exposure	Factors affecting risk exposure include; macroeconomic trends, medical costs, lapse rates, longevity, morbidity risk, demographics and technology developments. Vhi Insurance had gross written premium of €1,447,809k in 2016. The health underwriting risk component of the SCR was €178,891k as at 31 December 2016.
Methods of risk assessment	• Analysis of business mix and product profitability. • Pricing analysis to determine premium adequacy. • Reserving analysis to understand claims exposure. • Risk mitigation through reinsurance. • Stress and scenario testing.
Changes to the risk during the reporting period	The risk has increased during the reporting period, primarily due to uncertainty with regard to competitor activity, in particular the differentiation in product offerings with continued pressures on price and benefits.
Risk Mitigation	
Mitigation methods	• Risk selection and pricing appropriate to the level of risk underwritten and in line with community rating requirements. • Reserving control, with effective claims management to reduce exposure to large claims. • Reinsurance, to reduce the severity or occurrence of underwriting risk, with reinsurance placed with providers who have a Standard & Poor's A+ rating and a limit framework aligned to Vhi Insurance's risk appetite.
The effectiveness of risk mitigation methods	The Board has responsibility for monitoring the effectiveness of these risk mitigation techniques and in doing so relies on reasonable assurance provided by: • The Risk Management Function, which provides support and independent challenge to business units on the completeness, accuracy and consistency of risk self-assessments, reporting on adherence and compliance with risk appetite together with the outcome of the risk assessment process, which considers risk selection, pricing, claims management, reserving and related risks (credit risk, liquidity risk) quarterly. • The Actuarial Function, which proposes the optimum reinsurance solution for the Company and the adequacy of its reinsurance arrangements given the current and future business plans.

C.2 Market Risk

Market Risk

The risk of loss due to adverse movements in costs or returns from a change in the market price or rate

The main market risks are:

Equity Risk	Concentration Risk	Spread Risk	Interest Rate Risk	Property Risk

Risk Exposure	
Factors affecting risk exposure	Factors affecting risk exposure include; volatility of asset prices and value of assets held and liabilities. In pursuit of its growth objectives Vhi Insurance seeks some level of market risk as part of its investment strategy, however it does so on the basis that it does not introduce any unnecessary balance sheet risk. Vhi Insurance had total Solvency II investment assets of €1,127,154k as at 31 December 2016. The market risk component of the SCR was €27,122k as at 31 December 2016.
Methods of risk assessment	• Compliance with investment mandate. • Reviews of investment manager performance. • Stress and scenario testing.
Changes to the risk during the reporting period	There has been no material change to the Company's market risk exposure due to favourable economic conditions, low inflation expectations and no significant change in interest rates.

Risk Mitigation	
Mitigation methods	• An investment mandate which incorporates limits and restrictions. • Asset and liability matching. • Quarterly and periodic stress testing of key risk indicators.
The effectiveness of risk mitigation methods	The Board has responsibility for monitoring the effectiveness of these risk mitigation techniques and in doing so relies on reasonable assurance provided by: • The Investment Committee, which oversees that the investment portfolio is being managed in accordance with the investment mandate, solvency requirements and risk considerations. This includes reviewing the performance of the investment manager. • The investment manager, who presents to the Board on performance, market and economic issues. • The Finance Function, which monitors the investment mandate and investment manager. • The Risk Management Function, which provides support and independent challenge to business units on the completeness, accuracy and consistency of risk self-assessments, reporting on adherence and compliance with its risk appetite and policy management frameworks together with the outcome of the risk assessment process, which considers market risk quarterly.

Application of the Prudent Person Principle

Vhi Insurance invests in assets in accordance with the prudent person principle as set out in Regulation 141 of the *European Union (Insurance and Reinsurance) Regulations 2015*. The investment strategy aims to ensure that assets are invested in a manner appropriate to the nature and duration of the insurance liabilities and to ensure the security, quality, liquidity and profitability of the investment portfolio as a whole and the invested assets are held in locations which ensure their availability. All assets are invested in the best interests of policyholders.

The portfolio consists of assets managed by outsourced asset managers and short term bank deposits managed within the Vhi group. The outsourced asset managers must manage assets within parameters as set out in Vhi Insurance's investment mandate. Similarly, the internally managed short term deposits are managed within parameters set out by the Board.

The mandate has specific restrictions to ensure that Vhi Insurance only invests in assets which it can properly identify, measure, monitor, manage, control and report on and take into account in the calculation of the SCR. The parameters in the mandate ensure that the portfolio is appropriately diversified in such a way which avoids excessive reliance on any particular asset, issuer, geographical area or accumulation of risk in the portfolio as a whole. The parameters are aligned with the Board's Risk Appetite Statement and business strategy and are set independently of third parties; such as financial institutions, asset managers and rating agencies.

Derivatives are only invested in where they reduce the risks to which Vhi Insurance is exposed or to facilitate efficient portfolio management. Investment in assets which are not admitted to trading on a regulated financial market are kept to prudent levels.

C.3 Credit Risk

Credit Risk

The risk of a change in the value of assets and liabilities caused by an unexpected default or deterioration in the credit rating of counterparties and debtors. Debtors include policyholders, corporate policyholders, reinsurers and other third parties

The main credit risk is:

Counterparty default risk (Reinsurer, Banks)

Risk Exposure	
Factors affecting risk exposure	Factors affecting risk exposure include; volatility of asset prices, volatility of liabilities and economic contraction where default rates are elevated. Vhi Insurance had gross written premium of €1,447,809k in 2016. Reinsurance is on a funds withheld basis. The counterparty default risk component of the SCR was €29,812k as at 31 December 2016.
Methods of risk assessment	• Assessing the limits framework aligned to risk appetite. • Monitoring debtor days and debtor values. • Measuring and monitoring credit risk exposure and the credit ratings of counterparties. • Undertaking stress and scenario testing.
Changes to the risk during the reporting period	There has been no material change to the Company's credit risk exposure due to favourable economic conditions and the availability of credit. There is a control framework in place to mitigate this risk.
Risk Mitigation	
Mitigation methods	• Implementing a limits framework aligned to risk appetite. • An investment mandate enforced by limits and restrictions. • Monitoring the appropriateness of credit ratings applied to portfolio assets. • Cessation of cover if premium is not paid within specific timelines. • Active monitoring of arrears. • Managing the terms on which payments for outsourced services are arranged (i.e. reinsurance cover).
The effectiveness of risk mitigation methods	The Board has responsibility for monitoring the effectiveness of these risk mitigation techniques and in doing so relies on reasonable assurance provided by: • The Investment Committee, which engages with the investment manager to oversee the credit quality of the investment portfolio and challenge the appropriateness of credit ratings applied to portfolio assets as a measure of their credit risk. This includes reviewing the performance of the investment manager. • The Finance Function, which monitors the investment mandate and investment managers,seeks to ensure investments are being managed in accordance with the investment mandate, solvency requirements and risk considerations. • The Risk Management Function, which provides support and independent challenge to business units on the completeness, accuracy and consistency of risk self-assessments, reporting on adherence and compliance with its risk appetite and policy management frameworks together with the outcome of the risk assessment process, which considers credit risk quarterly.

C.4 Liquidity Risk

Liquidity Risk

The risk that forced early realisation of assets due to the need to meet payment obligations incurs a financial cost

The main liquidity risk:

Not having sufficient liquid or realisable assets to meet liabilities as they fall due over the short and medium term

Risk Exposure	
Factors affecting risk exposure	Factors affecting risk exposure include; net cash flows, investment strategy, credit cycles, external effects on the level of interest rates and other penalties charged on early realisation of assets. Vhi Insurance held 25% of total assets in cash and short term deposits as at 31 December 2016. The total amount of the expected profit included in future premiums is €22,383k.
Methods of risk assessment	• Assessing the limits framework aligned to risk appetite. • Monitoring short and medium term liquidity. • Monitoring forecast and actual cash flows. • Undertaking stress and scenario testing.
Changes to the risk during the reporting period	There has been no material change to the Company's liquidity risk exposure with diversification limits on banks, exposure limits to non-EU banks together with credit rating restrictions.
Risk Mitigation	
Mitigation methods	• Restrictions on asset allocations, holding substantial amounts in short term deposits. • Monitoring and projecting cash flows, including those provided by the investment manager. • Provider hospital contracts to ensure no exposure to penalties for late payment. • Liquidity buffers.
The effectiveness of risk mitigation methods	The Board has responsibility for monitoring the effectiveness of these risk mitigation techniques and in doing so relies on reasonable assurance provided by: • The Investment Committee, which engages with the investment manager to oversee management of the Company's funds, including liquidity buffers. This includes reviewing the performance of the investment manager. • The Finance Function, which provides cash flow projections to the investment manager, monitors the investment mandate and investment manager and seeks to ensure investments are being managed in accordance with the investment mandate, solvency requirements and risk considerations. • The Risk Management Function, which provides support and independent challenge to business on the completeness, accuracy and consistency of risk self-assessments, reporting on adherence and compliance with its risk appetite and policy management frameworks together with the outcome of the risk assessment process, which considers liquidity risk quarterly.

C.5 Operational Risk

Operational Risk

The risk of loss resulting from inadequate or failed internal processes, people or systems or from external events

The main operational risks are:

Business Interruption Risk	Clinical Risk	Data Protection & Cyber Attack Risk	Litigation Risk	Compliance Risk	Fraud Risk

Risk Exposure	
Factors affecting risk exposure	Operational risk is inherent in all business units and can have many impacts, including but not limited to, unexpected losses, reputational damage due to negative publicity, legal, regulatory and compliance risks. The operational risk component of the SCR was €42,909k as at 31 December 2016.
Methods of risk assessment	• Assessing the limits framework aligned to risk appetite. • Monitoring incidents and near misses. • Assessing the adequacy and effectiveness of controls, the operating environment and business continuity plans. • Undertaking stress and scenario testing.
Changes to the risk during the reporting period	There has been no material change to the Company's' operational risk exposure. Vhi Insurance anticipates that the development of the Abbey Street, Dublin premises will result in an increase in operational risk, however, measures are in place to monitor, control and report on risks and controls as the development progresses.

Risk Mitigation	
Mitigation methods	• Implementing a limits framework aligned to risk appetite. • An effective control environment. • Controls for IT security and data protection. • Controls over third party supplier contracts.
The effectiveness of risk mitigation methods	The Board has responsibility for monitoring the effectiveness of these risk mitigation techniques and in doing so relies on reasonable assurance provided by: • The EMT, which seeks to ensure material operational risks are identified, including incidents and near misses, across all business units with ownership assigned at executive level. • The Risk Management Function, which co-ordinates operational risk management activities, providing support and independent challenge to business units on the completeness, accuracy and consistency of risk self-assessments, reporting on adherence and compliance with its risk appetite and policy management frameworks together with the outcome of the risk assessment process, which considers operational risk quarterly.

C.6 Other Material Risks

Strategic & Value Growth Risk	Specific Regulation Risk	Reputation, Compliance, Conduct Risk
This risk relates to the Company's ability to grow financially and commercially	This risk relates to the community rating system and Vhi Insurance's disproportionate share of older customers in the PMI market	This risk relates to the risk of damage to the Vhi brand and loss of customers, the risk of detriment to customers and impairment to the Company's business model, reputation and financial condition and the risk that the Company's actions adversely affect its customers

Risk Exposure	
Factors affecting risk exposure	Failure to appropriately manage these risks can result in insolvency, reduced operating flexibility, increased costs, reputational harm, regulatory action and loss of customers. Total PMI membership in 2016 was 1,069k.
Methods of risk assessment	• Assessing the limits framework aligned to risk appetite. • Projecting forward capital requirements. • Monitoring the brand, complaints and media messages. • Conducting reviews of strategy, business plans and the performance of the underwriting portfolio. • Undertaking stress and scenario testing.
Changes to the risk during the reporting period	Vhi Insurance considers the RES in Ireland remains only partially effective and places insurers covering a disproportionate share of higher risk older and less healthy policyholders at a competitive disadvantage with attendant risk to capital, value and sustainability. Efforts to improve the RES are likely to require EU Commission approval which will take time. Competitor activity brings increased risk to the competitive advantage of insurers in the market. The risk to Vhi Insurance's competitive advantage increases given the trends in ageing, the prevalence of chronic disease and competitor activity in the market.
Risk Mitigation	
Mitigation methods	• Implementing a limits framework aligned to risk appetite. • Market intelligence. • Product relevance, differentiated propositions, segmentation, business mix and pricing. • Sales and relationship management. • Managing capital with appropriate reinsurance cover and holding excess capital to absorb shocks. • Restricting increases in medical inflation and ageing of the insured book. • An effective control environment with contingency plans to deal with incidents. • Compliance monitoring programme. • Influencing regulation. • Monitoring complaints. • Focus on conduct and compliance when dealing with customers, providers and the public sector. • Proactively managing the brand and media messages. • Monitoring complaints about treatments covered and access restrictions.

The effectiveness of risk mitigation methods	The Board has responsibility for monitoring the effectiveness of these risk mitigation techniques and in doing so relies on reasonable assurance provided by: • The EMT, which seeks to ensure these risks are identified and managed across all business units with ownership assigned at executive level. • The Risk Management Function/CRO, who has oversight responsibility in ensuring that adequate capital is held for the risk profile of the Company. • The Risk Management Function, which provides support and independent challenge to business units on the completeness, accuracy and consistency of risk self-assessments, reporting on adherence and compliance with its risk appetite and policy management frameworks together with the outcome of the risk assessment process quarterly. • Business units, through Compliance Coordinators, in each unit who identify, measure and report on compliance, escalating material changes and breaches to the Risk Management and Compliance functions.

Concentration Risk

Vhi Insurance's operations are based in Ireland, therefore, the Company is exposed to macroeconomic conditions in Ireland and turbulence in the wider Eurozone and global economy.

Underwriting Risk	• Concentration of risk is monitored through the limits framework aligned to risk appetite which seeks to ensure an appropriate balance of risk across Vhi Insurance's product suite. Product concentration is monitored and reported regularly with mitigating actions taken on product design, as appropriate. • There is no concentration in any specific area.
Market Risk	• Interest rate risk arises primarily from Vhi Insurance's investment in quoted debt securities and deposits. There is no significant concentration of interest rate risk. • Price risk arises from fluctuations in the value of financial instruments as a result of changes in market prices and the risks inherent in investments. There is no significant concentration of price risk.
Credit Risk	• There is no concentration of credit risk, with the Company exposure managed through limits and tolerances aligned to risk appetite on credit control and asset credit ratings.
Liquidity Risk	• The risk of default is an important factor in concentration risk and is measured by the credit ratings issued by agencies such as Moody's and Standard & Poors. • There is no concentration of liquidity risk as Vhi Insurance operates a closely matched and low risk mandate with strict adherence to limits and restrictions.
Operational Risk	• There is no risk concentration in operational risk as Vhi Insurance operates with a control framework that is monitored on an ongoing basis. That is not to say that operational risks are not correlated but many of them are not heavily so.
Other Material Risks	• **Strategic and Value Growth Risk:** Components of this risk include underwriting, market, credit and operational risk, where concentration risk is described in the sections above. • **Specific Regulation Risk:** A deterioration in the effectiveness of the RES impacts value and profit concentrations, increasing the Company's exposure to business mix risk. • **Reputation, Compliance and Conduct Risk:** There is no particular concentration of the risks themselves but correlation may exist between these and operational risks.

Risk Sensitivity

Assessments utilising business expertise is used to agree relevant stresses for the components of the material risks, to assess impact and controls and agree management actions. This enables Vhi Insurance to quantify the solvency impact by selecting the stresses with material impact to develop suitable scenarios that are plausible, sufficiently challenging and provide a sound basis upon which to assess solvency for the material risks.

The main assumptions underlying the stress tests and scenario analysis are consistent with those used in the business and financial planning processes.

	Stress / Scenario	
Underwriting Risk	• Economic downturn • Removal of income tax relief • Adverse change to risk equalisation	• Claims surge • Provider risks • Increase in competition
Market Risk	• Equity risk • Spread risk • Interest rate risk	• Property risk • Concentration risk
Credit Risk	• Counterparty default risk	
Liquidity Risk	• Equity risk • Spread risk	• Interest rate risk
Operational Risk	• Information security breach from a cyber attack	
Other Material Risks	• **Strategic & Value Growth Risk**: The main components of this risk are market, operational, insurance and credit risk, details of stresses and scenarios are provided above. Stress tests are performed to understand the value impacts, (membership, business mix, margin) on the material risks. • **Specific Regulation Risks, Reputation, Compliance and Conduct Risk:** Vhi Insurance uses stress and scenario analyses in a similar way for these risks as the Company does for Strategic and Value Growth Risk as described above.	

C.7 Any Other Information

There is no additional material information regarding the risk profile of Vhi insurance that has not been disclosed above.

D.
VALUATION FOR SOLVENCY PURPOSES

D.1 Assets

This section has been completed in the order of how the assets appear on QRT S.02.01.02 Balance Sheet.

Vhi Insurance DAC Solvency II Balance Sheet Extract	Notes	Solvency II Value €'000	Statutory Accounts €'000
Assets			
Deferred acquisition costs	1	0	29,301
Property, plant & equipment held for own use	2	4,899	4,984
Investments			
Property (other than for own use)		20,038	20,038
Equities		4,557	4,557
Government Bonds		396,876	396,876
Corporate Bonds		430,660	430,660
Collateralised securities		15,290	15,290
Collective Investments Undertakings		10,880	10,880
Deposits other than cash equivalents		248,853	284,636
Total Investments	3	**1,127,154**	**1,162,937**
Reinsurance recoverable from non-life and health similar to non-life	4	168,960	306,910
Insurance and intermediaries receivables	5	318,941	588,138
Reinsurance receivables	4	0	13,989
Cash and cash equivalents	3	36,898	1,115
Any other assets, not elsewhere shown	6	38	116,261
Total Assets		**1,656,890**	**2,223,635**

Note 1: Deferred Acquisition Costs

The costs incurred during the financial year that are directly attributable to the acquisition of new business are expensed in the same accounting period as the premiums to which they relate are earned.

Under Solvency II, deferred acquisition costs are included in the calculation of the premium provision.

Asset	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Deferred acquisition costs	0	29,301	(29,301)

Note 2: Property Plant and Equipment Held For Own Use

Property, plant and equipment held for own use is a combination of 'Tangible assets' and 'Land and buildings' in the statutory accounts.

Asset	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Tangible Assets	0	85	(85)
Property - held for own use	4,899	4,899	0
Property, plant & equipment held for own use	4,899	4,984	(85)

Tangible Assets

For the statutory accounts, tangible assets are stated at cost less accumulated depreciation and impairment. Depreciation is calculated so as to write off the cost of the assets over their estimated useful lives on a straight line basis.

The Company may not use this valuation technique to value tangible assets under Solvency II and is required to consider alternative valuation techniques but given the low GAAP value and the difficulty in converting these assets to a cash inflow, no value has been placed on them for the purposes of Solvency II.

Property

Property is valued annually on an open market value basis. Valuations are made by independent professionally qualified valuers with recent experience in the location and class of the properties held. These valuations are based on recent market prices adjusted to reflect the condition and location of the specific properties. Valuations are carried out as close as possible to each year end.

Most property held is shared by Vhi Insurance with other Vhi group companies. The property value is split between *Property - held for own use* and *Property - other than for own use* based on the occupation ratio of the buildings by the personnel of Vhi Insurance and the personnel of other Vhi group companies.

Asset	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Property - held for own use	4,899	4,899	0
Property - other than for own use	20,038	20,038	0
Total Property	24,937	24,937	0

Note 3: Investments and Cash

In line with the statutory accounts, investment assets under Solvency II are held at fair value. Fair value is determined as the market value which represents the bid price inclusive of any accrued interest at the balance sheet date.

Where available, market prices are determined by reference to publically available prices of identical assets in active markets. The Company considers a market active in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information to market participants on an ongoing basis. Where actual market prices are not publically available, valuations are calculated by valuation services with access to private market information. Where prices for identical assets are not available, valuations are calculated by reference to prices for similar assets trading on active markets with appropriate adjustments for differences between the assets.

At 31 December 2016, all assets included in the categories of Government Bonds, Corporate Bonds and Collateralised Securities:

- were considered to be trading in active markets as prices were available to market participants,
- were valued by valuation services using quoted prices for identical or similar assets and
- were subject to minimal valuation uncertainty.

Collective investments undertakings are composed of money market funds with constant or variable net asset values whose value is derived from the market value of the underlying assets held. Such funds are valued by the fund manager and considered to be at risk of minimal valuation uncertainty.

+ Further Information Section D.4. Alternative Methods for Valuation discusses the valuation of unlisted equities

Bank deposits are carried at face value plus or minus any accrued interest at the balance sheet date. The directors believe that this value does not need to be further adjusted under Solvency II as all accounts mature within one year.

In the balance sheet, €35,783k which was held on call as part of the cash element of the total investment portfolio and classified in 'Deposits in banks' in the Company's financial statements is reclassified to 'Cash and cash equivalents' as it is immediately available for use in making payments.

Asset	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Equities - unlisted	4,557	4,557	0
Government bonds	396,876	396,876	0
Corporate bonds	430,660	430,660	0
Collateralised securities	15,290	15,290	0
Collective investments undertakings	10,880	10,880	0
Investment portfolio assets at fair value	**858,263**	**858,263**	**0**
Deposits other than cash equivalents	248,853	284,636	(35,783)
Property (other than for own use)	20,038	20,038	0
Total investment assets	**1,127,154**	**1,162,937**	**0**
Cash and cash equivalents	36,898	1,115	35,783
Total	**1,164,052**	**1,164,052**	**0**

Note 4: Reinsurance Recoverable and Reinsurance Receivables

Reinsurance recoverable and Deposits from reinsurers:

A reinsurance recoverable is recognised where the Company has purchased reinsurance and expects to be able to recover claims amounts which are outstanding or yet to be incurred under insurance contracts issued. The valuation of the recoverable is consistent with the valuation of the underlying technical provisions made for claims outstanding or unearned premiums.

Premiums retained from the reinsurer until settlement of the underlying claims are recognised as a liability – *deposits from reinsurers*. Vhi Insurance currently retains premiums equal to the recoverable at all times.

Under Solvency II, these amounts are reduced as underlying provision for claims outstanding is lower due to the elimination of prudence.

	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Asset Reinsurance recoverable from non-life and health similar to non-life	168,960	306,910	(137,950)
Liability Deposits from reinsurers	(168,960)	(306,910)	137,950

Reinsurance receivables and Reinsurance payables:

Reinsurance receivables or payables are valued at the expected immediate cash inflow or outflow under reinsurance contracts entered into.

Under Solvency II, reinsurance is recalculated, and as a result of the elimination of prudence from the technical provisions, the expected reinsurance receivable is replaced with an estimate for the eventual payable.

	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Asset Reinsurance receivables	0	13,989	(13,989)
Liability Reinsurance payables	(2,641)	0	(2,641)

Note 5: Insurance and Intermediaries Receivables

Insurance and intermediaries receivables include amounts receivable from policyholders via intermediaries and related tax relief-at-source and risk equalisation credits for insurance policies incepted. The receivable for risk equalisation credits is shown under ‘other debtors’ in the statutory accounts but is classified here as an insurance receivable.

In the statutory accounts, receivables are valued at face value net of an allowance for potential doubtful debts estimated using historical data and regularly tested against experience.

Under Solvency II, cash flows in respect of unexpired insurance coverage are removed and included in the calculation of the premium provision. No other valuation adjustment is made as all receivables are receivable within one year.

Asset	Solvency II Value €’000	Statutory Accounts €’000	Difference €’000
Insurance & intermediaries receivables	318,941	588,138	(269,197)

Note 6: Any Other Assets, Not Elsewhere Shown

Other assets consist of deferred expenses under the Risk Equalisation Scheme and prepayments. Deferred risk equalisation expenses are included in the calculation of the premium provision under Solvency II. Prepayments are considered to be valued consistently for Solvency II purposes.

Asset	Solvency II Value €’000	Statutory Accounts €’000	Difference €’000
Any other assets, not elsewhere shown	38	116,261	(116,223)

D.2 Technical Provisions

D.2.1 Technical Provisions Methodology and Bases

The following standard actuarial techniques are applied to estimate the claims for the Provision for Claims Outstanding ("PCO"): Development Factor Method, Estimated Loss Ratio Method and the Bornhuetter-Ferguson Method. The Estimated Loss Ratio is also used to calculate the Premium Provision ("PP").

- **Development Factor Method ("DFM")** A DFM (or otherwise known as basic chain ladder method) assumes that for any particular Accident Period ("AccPeriod"), the proportion of the total ultimate claim costs, which has developed by each period, follows past trends. This method is applied using both paid and incurred claims data.

- **Estimated Loss Ratio ("ELR") Method** For this method, a projected LR is estimated independently of the claims experience to date for that AccPeriod. The ELR method is used for recent AccPeriods which are relatively less developed as DFM's may not be appropriate given they have relatively less data at these early stages.

- **Bornhuetter-Ferguson ("BF") Method** This method combines features of the DFM and ELR methods, and assigns weights for the percentage of losses paid and losses incurred. Unlike the Chain Ladder Method, which builds a model based on past experience, the Bornhuetter-Ferguson technique builds a model based on the insurer's exposure to loss. This is most useful for more recent periods, reducing the reliance on less developed claims experience.

In calculating the technical provisions the probability weighted discounted average of all possible future outcomes is considered, this includes an allowance for events not in historic claims data.

The technical provisions considers all cashflows arising from claims and associated expenses that will be incurred servicing policies during their lifetime. Vhi Insurance holds a provision to cover future expense cashflows. This includes expenses associated with the future payment of claims for expired risk and expenses associated with the ongoing maintenance of policies for unexpired periods of risk.

The payoff profile for the cashflows projected within the technical provisions is constructed using the historic payment development trends that the portfolio has experienced previously. These cashflows are discounted using the year end 2016 risk free term structure of interest rates published by the European Insurance and Occupational Pension Authority ("EIOPA").

+ Further Information Section D.2.7 outlines the calculation of the Risk Margin.

A Quota Share contract is in place and when calculating the net technical provisions the reinsurer's proportionate share of future cashflows are allowed for in the technical provisions.

Medical Expense Insurance	Gross €'000	Net €'000
Provision for Claims Outstanding ("PCO")	313,264	202,015
Premium Provision ("PP")	192,389	134,679
Risk Margin	16,523	16,523
Total Technical Provisions	**522,176**	**353,217**

D.2.2 Level of uncertainty associated with the value of technical provisions

Vhi Insurance underwrites medical expense insurance which is short tailed in nature and under a normal course of business experiences a relatively low degree of volatility. This is recognised in the volatility assumption applied under the Solvency II standard formula guidelines, which is lower compared to other non-life business lines.

In recent periods there has been a higher level of volatility in public hospital claims than was previously the case, so the current level of uncertainty is considered to be higher than normal.

D.2.3 Explanation of any material differences between the bases, methods and main assumptions

The technical provisions in the financial statements total €1,022,399k at 31 December 2016. This compares to Solvency II technical provisions of €522,176k.

The reasons for the difference are due to different valuation bases for the respective calculations.

The Solvency II Technical Provisions are on a discounted, best estimate basis, allowing for all future cashflows associated with claims and expenses associated with business to which Vhi Insurance is obligated as at 31 December 2016.

The Financial Statements Technical Provisions have been prepared in accordance with FRS 102 and FRS 103. These allow for reasonably foreseeable events and need not be on a best estimate basis.

The largest reason for difference between the two bases is the allowance for future premium receivable in the Solvency II Technical Provisions, which gives rise to a reduction of €269,197k.

The remaining differences are mainly explained by the removal of any margins for prudence and recognition of surplus within unexpired risk.

D.2.4 Matching adjustment, volatility adjustment or transitional measures applied to the technical provisions

Vhi Insurance does not apply:

- a matching adjustment
- a volatility adjustment
- transitional measures

D.2.5 Description of recoverables from reinsurance contracts

Vhi Insurance have a multi-year quota share reinsurance agreement in place. The current amount ceded is 30%.

The National Indemnity Company, part of the Berkshire Hathaway group (the “Reinsurer”), has a strong credit rating, AA+ with Standard & Poor’s at the 31 December 2016. Under Solvency II this corresponds to a credit quality step of 1. Any reinsurance recoverable is adjusted for expected default of the Reinsurer in line with Article 61 of Delegated Regulation 2015/35/EU.

Vhi Insurance has calculated the reinsurer’s share of cashflows underpinning the Gross Technical Provisions. The Net Technical Provisions have been calculated by deducting the reinsurer’s share of Gross Technical Provisions, from the Gross Technical Provisions.

D.2.6 Material changes in the relevant assumptions made in the calculation of technical provisions compared to the previous reporting period

This is the first reporting period under Solvency II. Therefore, there is no previous period technical provisions yet available for comparison.

D.2.7 Risk Margin

The Solvency II Risk Margin shall be such as to ensure that the value of the technical provisions is equivalent to the amount an insurance and reinsurance undertaking would be expected to require in order to take over and meet the insurance obligations of the Company.

This component should be calculated using a cost of capital approach. The cost of capital approach requires the Solvency II Risk Margin to be calculated by determining the cost of providing an amount of eligible own funds equal to the SCR necessary to support the obligations over their lifetime.

In EIOPA's "Guidelines on the Valuation of Technical Provisions" a hierarchy of methods is specified for the estimation of future SCR. Vhi Insurance adopts the top method in this hierarchy, "Method 1".

The cost of capital applied in calculating the Solvency II Risk Margin is 6%. The Solvency II Risk Margin calculated at the 31 December 2016 was €16,523k.

D.3 Other Liabilities

This section has been completed in the order of how the liabilities appear on QRT S.02.01.02 Balance Sheet.

Vhi Insurance DAC Solvency II Balance Sheet Extract	Notes	Solvency II Value €'000	Statutory Accounts €'000
Other Liabilities			
Deposits from reinsurers	4	168,960	306,910
Deferred tax liabilities	7	27,026	143
Insurance & intermediaries payables	8	133,324	162,625
Reinsurance payables	4	2,641	0
Payables (trade, not insurance)	9	1,963	1,963
Any other liabilities, not elsewhere shown	10	9,583	126,559
Total Other liabilities		**343,497**	**598,200**

Note 7: Deferred Tax Liabilities

Vhi Insurance recognises a deferred tax liability as a result of the transition to FRS102 and values this under GAAP at its undiscounted face value.

Under Solvency II, this deferred tax liability is increased for the taxable value of the unrealised gain which results from recalculation of the technical provisions without prudence.

Liability	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Deferred tax liabilities	27,026	143	26,883

Note 8: Insurance and Intermediaries Payables

Insurance and intermediaries payables include amounts due to hospitals and doctors for policyholder claims assessed at the balance sheet date and not yet paid, along with amounts due for the Health Insurance Levy to fund the Risk Equalisation Scheme, and commission payable to intermediaries for policies sold. Under GAAP, these are valued at the undiscounted face value.

Under Solvency II, commission payable which relates to the unexpired portion of in force contracts are included in the calculation of the premium provision. No further adjustment is made to these values as all amounts are expected to settle within one year.

Liability	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Insurance & intermediaries payables	133,324	162,625	(29,301)

Note 9: Payables (Trade, Not Insurance)

Trade payables include amounts due to other Vhi group companies for shared services received and corporation tax payable. Under GAAP, they are valued at the undiscounted face value as they are expected to settle within one year.

Under Solvency II, no adjustment is made to these values as all amounts are expected to settle within one year.

Liability	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Trade payables	1,227	1,227	0
Corporation tax payable	736	736	0
Payables (trade, not insurance)	**1,963**	**1,963**	**0**

Note 10: Any Other Liabilities, Not Elsewhere Shown

Deferred Risk Equalisation Scheme income is included in the calculation of the premium provision under Solvency II. Payables to Vhi group companies include payables for interest accrued on subordinated debt issued. Accruals and other payables are valued at the undiscounted face value under GAAP and are considered to be valued consistently under Solvency II.

Liability	Solvency II Value €'000	Statutory Accounts €'000	Difference €'000
Deferred Risk Equalisation Scheme income	0	116,976	(116,976)
Payables to Vhi group companies	2,101	2,101	0
Accruals	7,482	7,482	0
Any other Liabilities, not elsewhere shown	**9,583**	**126,559**	(116,976)

D.4 Alternative Methods for Valuation

Vhi Insurance uses alternative valuation methods to value assets and liabilities where markets are not active or quoted prices are not available. Maximum possible use has been made of relevant market inputs where available.

Unlisted equities are valued by reference to observable market prices using a discounted cash flow method. The value of cash inflows are calculated by reference to publically available prices for similar assets. Investments in unlisted equities are kept to prudent levels (less than 1% of assets) such that valuation uncertainty is not material for the Company.

D.5 Any Other Information

There is no additional material information regarding the valuation of assets and liabilities for solvency purposes for Vhi Insurance that has not been disclosed above.

E.
CAPITAL MANAGEMENT

E.1. Own Funds

Vhi Insurance manages its own funds with the main objective of satisfying solvency requirements in line with the Company's Risk Appetite Statement. The Company prepares a Medium Term Capital Plan which is updated annually in line with the Board's Capital Management Policy. This includes the projection of own funds over a four year time horizon and aims to ensure that the Company continues to hold own funds within the preferred risk appetite range throughout this horizon.

E.1.1 The Structure, Amount and Quality of Own Funds

The below table sets out, separately for each tier, information on the structure, amount and quality of own funds at 31 December 2016 including the eligible amount of own funds to cover the SCR, classified by tiers and the eligible amount of basic own funds to cover the MCR, classified by tiers.

	2016 €'000
Basic Own Funds for SCR	
Tier 1	740,118
Tier 2	-
Tier 3	51,100
Total Basic Own Funds	**791,218**
Eligible Own Funds for SCR	
Tier 1	740,118
Tier 2	-
Tier 3	32,052
Total Eligible Own Funds for SCR	**772,170**
Eligible Own Funds for MCR	
Tier 1	740,118
Tier 2	-
Tier 3	-
Total Eligible Own Funds for MCR	**740,118**

A capital contribution of €26,000k from Vhi Group DAC was made in December 2016 and €38,900k of Tier 3 basic own funds (subordinated debt) was repaid in December 2016. The remaining increase in Tier 1 own funds is due to positive underwriting performance in 2016.

E.1.2 Differences between equity as shown in the financial statements and the excess of assets over liabilities

The financial statements of Vhi Insurance show equity of €5,000k and retained earnings of €546,936k. The breakdown of the movement between the financial statements and Solvency II are outlined in the table below.

Excess of assets over liabilities – Attribution of valuation difference	€'000
Difference in the valuation of assets	(566,745)
Difference in the valuation of technical provisions	(500,223)
Difference in the valuation of other liabilities	(254,703)
Total of reserves and retained earnings from financial statements	546,936
Reserves from financial statements adjusted for Solvency II valuation differences	735,118
Excess of assets over liabilities attributable to basic own fund items (excluding the reconciliation reserve)	5,000
Excess of assets over liabilities	**740,118**

The own funds presented in the above tables are fully available for the absorption of policyholder losses.

E.1.3 Information on Own Fund Items

Tier 1	The Tier 1 own funds of Vhi Insurance comprise retained earnings and €5,000k equity. These funds can be called on demand and are fully available to absorb losses on a going concern basis and in the case of winding up.
Tier 3	Vhi Insurance issued a subordinated debt instrument in July 2015 of which €51,100k is outstanding at year end 2016. This had an original tenor of 7 years and is subordinated to policyholders and all other Vhi Insurance creditors therefore, it is fully available to absorb losses.

The Tier 3 basic own fund items for Vhi Insurance have decreased over the year. A repayment of €38,900k was made on the Tier 3 subordinated debt over 2016. The Tier 1 own funds increased due to positive underwriting performance in 2016 and a capital contribution from Vhi Group DAC of €26,000k was made to Vhi Insurance. No distributions have been made to shareholders throughout the year and all profits have been retained as reconciliation reserve.

The reconciliation reserve represents the net asset value under Solvency II for Vhi Insurance less equity and subordinated debt own fund items.

There are no restrictions or adjustments applied to own fund items other than restricting Tier 3 to the 15% of SCR eligibility criteria according to Solvency II regulation.

E.2 Solvency Capital Requirement and Minimum Capital Requirement

Vhi Insurance calculates the SCR using the standard formula. The table below sets out the SCR and MCR for Vhi Insurance as at year end 31 December 2016.

Capital Requirements	**2016 €'000**
Solvency Capital Requirement (SCR)	213,679
Minimum Capital Requirement (MCR)	63,458

Capital Requirements by sub-module	**2016 €'000**
Market Risk	27,122
Counterparty Default Risk	29,812
Health Underwriting Risk	178,891
Operational Risk	42,909
Adjustments and Diversification	(65,055)
Solvency Capital Requirement (SCR)	**213,679**

No simplified calculations or undertaking specific parameters are applied in the calculation of the standard formula SCR for Vhi Insurance.

The MCR is bound by a maximum of 45% and a minimum of 25% of the SCR. Its calculation is based on a straight line formula including net technical provisions and premium written for the previous 12 months.

There has been no material change to the SCR or the MCR over the reporting period.

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

This section is not applicable to Vhi Insurance.

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

This section is not applicable to Vhi Insurance.

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

This section is not applicable to Vhi Insurance.

E.6 Any Other Information

There is no additional material information regarding the capital management of Vhi Insurance that has not been disclosed above.

Appendix. Quantitative Reporting Templates

This appendix includes the annual Quantitative Reporting Templates (QRTs) for Vhi Insurance DAC in respect of year end 31 December 2016. All figures are shown in thousands (€'000). Please note there may be minor differences in totals due to rounding.

Reference	Template Name	Audited
S.02.01.02	Balance Sheet	✓
S.05.01.02	Premiums, Claims and Expenses by line of business	n/a
S.17.01.02	Non-Life Technical Provisions	✓
S.19.01.21	Non-Life Insurance Claims Information	✓
S.23.01.01	Own Funds	✓
S.25.01.21	Solvency Capital Requirement – for undertakings on Standard Formula	✓
S.28.01.01	Minimum Capital Requirement – Only Life or only non-life insurance or reinsurance activity	✓

S.02.01.02 Balance Sheet

		Solvency II Value
	Assets	C0010
R0030	Intangible assets	0
R0040	Deferred tax assets	0
R0050	Pension benefit surplus	0
R0060	Property, plant & equipment held for own use	4,899
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	1,127,154
R0080	*Property (other than for own use)*	20,038
R0090	*Holdings in related undertakings, including participations*	0
R0100	*Equities*	4,557
R0110	*Equities - listed*	0
R0120	*Equities - unlisted*	4,557
R0130	*Bonds*	842,827
R0140	*Government Bonds*	396,876
R0150	*Corporate Bonds*	430,660
R0160	*Structured notes*	0
R0170	*Collateralised securities*	15,290
R0180	*Collective Investments Undertakings*	10,880
R0190	*Derivatives*	0
R0200	*Deposits other than cash equivalents*	248,853
R0210	*Other investments*	0
R0220	Assets held for index-linked and unit-linked contracts	0
R0230	Loans and mortgages	0
R0240	*Loans on policies*	0
R0250	*Loans and mortgages to individuals*	0
R0260	*Other loans and mortgages*	0
R0270	Reinsurance recoverables from:	168,960
R0280	*Non-life and health similar to non-life*	168,960
R0290	*Non-life excluding health*	0
R0300	*Health similar to non-life*	168,960
R0310	*Life and health similar to life, excluding health and index-linked and unit-linked*	0
R0320	*Health similar to life*	0
R0330	*Life excluding health and index-linked and unit-linked*	0
R0340	*Life index-linked and unit-linked*	0
R0350	Deposits to cedants	0
R0360	Insurance and intermediaries receivables	318,941
R0370	Reinsurance receivables	0
R0380	Receivables (trade, not insurance)	0
R0390	Own shares (held directly)	0
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	0
R0410	Cash and cash equivalents	36,898
R0420	Any other assets, not elsewhere shown	38
R0500	**Total assets**	1,656,890

		Solvency II Value
	Liabilities	C0010
R0510	Technical provisions – non-life	522,176
R0520	*Technical provisions – non-life (excluding health)*	0
R0530	*TP calculated as a whole*	0
R0540	*Best Estimate*	0
R0550	*Risk margin*	0
R0560	*Technical provisions - health (similar to non-life)*	522,176
R0570	*TP calculated as a whole*	0
R0580	*Best Estimate*	505,653
R0590	*Risk margin*	16,523
R0600	Technical provisions - life (excluding index-linked and unit-linked)	0
R0610	*Technical provisions - health (similar to life)*	0
R0620	*TP calculated as a whole*	0
R0630	*Best Estimate*	0
R0640	*Risk margin*	0
R0650	*Technical provisions – life (excluding health and index-linked and unit-linked)*	0
R0660	*TP calculated as a whole*	0
R0670	*Best Estimate*	0
R0680	*Risk margin*	0
R0690	Technical provisions – index-linked and unit-linked	0
R0700	*TP calculated as a whole*	0
R0710	*Best Estimate*	0
R0720	*Risk margin*	0
R0740	Contingent liabilities	0
R0750	Provisions other than technical provisions	0
R0760	Pension benefit obligations	0
R0770	Deposits from reinsurers	168,960
R0780	Deferred tax liabilities	27,026
R0790	Derivatives	0
R0800	Debts owed to credit institutions	0
R0810	Financial liabilities other than debts owed to credit institutions	0
R0820	Insurance & intermediaries payables	133,324
R0830	Reinsurance payables	2,641
R0840	Payables (trade, not insurance)	1,963
R0850	Subordinated liabilities	51,100
R0860	*Subordinated liabilities not in Basic Own Funds*	0
R0870	*Subordinated liabilities in Basic Own Funds*	51,100
R0880	Any other liabilities, not elsewhere shown	9,583
R0900	**Total liabilities**	916,771
R1000	**Excess of assets over liabilities**	**740,118**

S.05.01.02.01 Premiums, Claims and Expenses by line of business

		Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance) Medical expense insurance	Total
		C0010	C0200
	Premiums written		
R0110	Gross - Direct Business	1,447,809	1,447,809
R0120	Gross - Proportional reinsurance accepted	0	0
R0130	Gross - Non-proportional reinsurance accepted		0
R0140	Reinsurers' share	435,689	435,689
R0200	Net	1,012,121	1,012,121
	Premiums earned		
R0210	Gross - Direct Business	1,430,308	1,430,308
R0220	Gross - Proportional reinsurance accepted	0	0
R0230	Gross - Non-proportional reinsurance accepted		0
R0240	Reinsurers' share	430,438	430,438
R0300	Net	999,870	999,870
	Claims incurred		
R0310	Gross - Direct Business	1,309,853	1,309,853
R0320	Gross - Proportional reinsurance accepted	0	0
R0330	Gross - Non-proportional reinsurance accepted		0
R0340	Reinsurers' share	393,645	393,645
R0400	Net	916,208	916,208
	Changes in other technical provisions		
R0410	Gross - Direct Business	0	0
R0420	Gross - Proportional reinsurance accepted	0	0
R0430	Gross - Non- proportional reinsurance accepted		0
R0440	Reinsurers' share	0	0
R0500	Net	0	0
R0550	**Expenses incurred**	**122,248**	**122,248**
R1200	**Other expenses**		0
R1300	**Total expenses**		**122,248**

S.17.01.02 Non-Life Technical Provisions

		Direct business and accepted proportional reinsurance Medical expense insurance	Total Non-Life obligation
		C0020	C0180
R0010	**Technical provisions calculated as a whole**	0	0
R0050	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	0	0
	Technical provisions calculated as a sum of BE and RM		
	Best estimate		
	Premium provisions		
R0060	Gross	192,389	192,389
R0140	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	57,710	57,710
R0150	Net Best Estimate of Premium Provisions	134,679	134,679
	Claims provisions		
R0160	Gross	313,264	313,264
R0240	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	111,250	111,250
R0250	Net Best Estimate of Claims Provisions	202,015	202,015
R0260	**Total Best estimate - gross**	**505,653**	**505,653**
R0270	**Total Best estimate - net**	**336,693**	**336,693**
R0280	**Risk margin**	**16,523**	**16,523**
	Amount of the transitional on Technical Provisions		
R0290	Technical Provisions calculated as a whole	0	0
R0300	Best estimate	0	0
R0310	Risk margin	0	0
	Technical provisions - total		
R0320	Technical provisions - total	522,176	522,176
R0330	Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total	168,960	168,960
R0340	Technical provisions minus recoverables from reinsurance/SPV and Finite Re - total	353,217	353,217

S.19.01.21 Non-Life Insurance Claims Information

Total Non-Life Business

Z0010	Accident year / Underwriting year	**Z0010**	Accident year [AY]

Gross Claims Paid (non-cumulative)

(absolute amount)

Development year

	Year	0	1	2	3	4	5	6	7	8	9	10 & +	In Current year	Sum of years (cumulative)
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0170	C0180
R0100	**Prior**											1	1	1
R0160	**N-9**	752,067	227,562	24,328	6,607	1,654	976	346	71	258	23		23	1,013,891
R0170	**N-8**	823,513	298,724	22,182	4,669	2,004	721	634	200	-14			-14	1,152,633
R0180	**N-7**	975,052	256,711	18,558	5,538	1,094	-1,071	-413	-566				-566	1,254,903
R0190	**N-6**	985,701	243,633	18,063	3,757	-236	-152	-334					-334	1,250,431
R0200	**N-5**	964,413	286,873	20,794	3,244	1,211	576						576	1,277,111
R0210	**N-4**	997,768	259,357	17,986	3,036	1,297							1,297	1,279,443
R0220	**N-3**	942,521	285,755	23,151	6,262								6,262	1,257,688
R0230	**N-2**	936,632	304,716	29,322									29,322	1,270,670
R0240	**N-1**	983,274	279,749										279,749	1,263,023
R0250	**N**	1,022,868											1,022,868	1,022,868
R0260												**Total**	1,339,184	12,042,661

Gross undiscounted Best Estimate Claims Provisions
(absolute amount)

Development year

	Year	0	1	2	3	4	5	6	7	8	9	10 & +	Year end (discounted data)
		C0200	C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0290	C0300	C0360
R0100	Prior											124	125
R0160	N-9	0	0	0	0	0	0	0	0	0	121		121
R0170	N-8	0	0	0	0	0	0	0	0	91			92
R0180	N-7	0	0	0	0	0	0	0	218				219
R0190	N-6	0	0	0	0	0	0	333					335
R0200	N-5	0	0	0	0	0	671						674
R0210	N-4	0	0	0	0	1,137							1,141
R0220	N-3	0	0	0	2,565								2,574
R0230	N-2	0	0	8,038									8,064
R0240	N-1	0	29,580										29,678
R0250	N	269,346											270,243
R0260												Total	313,264

S.23.01.01 Own Funds

		Total	Tier 1 - unrestricted	Tier 1 - restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35					
R0010	Ordinary share capital (gross of own shares)	5,000	5,000		0	
R0030	Share premium account related to ordinary share capital	0	0		0	
R0040	Initial funds, members' contributions or the equivalent basic own - fund item for mutual and mutual-type undertakings	0	0		0	
R0050	Subordinated mutual member accounts	0		0	0	0
R0070	Surplus funds	0	0			
R0090	Preference shares	0		0	0	0
R0110	Share premium account related to preference shares	0		0	0	0
R0130	Reconciliation reserve	735,118	735,118			
R0140	Subordinated liabilities	51,100		0	0	51,100
R0160	An amount equal to the value of net deferred tax assets	0				0
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	0	0	0	0	0
	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					
R0220	Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds	0				
	Deductions					
R0230	Deductions for participations in financial and credit institutions	0	0	0	0	
R0290	**Total basic own funds after deductions**	**791,218**	**740,118**	**0**	**0**	**51,100**
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	0			0	
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand	0			0	
R0320	Unpaid and uncalled preference shares callable on demand	0			0	0

R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	0			0	0
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	0			0	
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	0			0	0
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0			0	
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	0			0	0
R0390	Other ancillary own funds	0			0	0
R0400	**Total ancillary own funds**	**0**			**0**	**0**
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	791,218	740,118	0	0	51,100
R0510	Total available own funds to meet the MCR	740,118	740,118	0	0	
R0540	Total eligible own funds to meet the SCR	772,170	740,118	0	0	32,052
R0550	Total eligible own funds to meet the MCR	740,118	740,118	0	0	
R0580	**SCR**	**213,679**				
R0600	**MCR**	**63,458**				
R0620	**Ratio of Eligible own funds to SCR**	**3.6137**				
R0640	**Ratio of Eligible own funds to MCR**	**11.6632**				
	Reconciliation reserve	C0060				
R0700	Excess of assets over liabilities	740,118				
R0710	Own shares (held directly and indirectly)	0				
R0720	Foreseeable dividends, distributions and charges	0				
R0730	Other basic own fund items	5,000				
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	0				
R0760	**Reconciliation reserve**	**735,118**				
	Expected profits					
R0770	Expected profits included in future premiums (EPIFP) - Life business	0				
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	22,383				
R0790	**Total Expected profits included in future premiums (EPIFP)**	**22,383**				

S.25.01.21 Solvency Capital Requirement – for undertakings on Standard Formula

		Gross solvency capital requirement
		C0110
R0010	Market risk	27,122
R0020	Counterparty default risk	29,812
R0030	Life underwriting risk	0
R0040	Health underwriting risk	178,891
R0050	Non-life underwriting risk	0
R0060	Diversification	-38,029
R0070	Intangible asset risk	0
R0100	**Basic Solvency Capital Requirement**	**197,795**
	Calculation of Solvency Capital Requirement	C0100
R0130	Operational risk	42,909
R0140	Loss-absorbing capacity of technical provisions	0
R0150	Loss-absorbing capacity of deferred taxes	-27,026
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	0
R0200	**Solvency capital requirement excluding capital add-on**	**213,679**
R0210	Capital add-on already set	0
R0220	**Solvency capital requirement**	**213,679**
	Other information on SCR	
R0400	Capital requirement for duration-based equity risk sub-module	0
R0410	Total amount of Notional Solvency Capital Requirement for remaining part	0
R0420	Total amount of Notional Solvency Capital Requirements for ring fenced funds	0
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	0
R0440	Diversification effects due to RFF nSCR aggregation for article 304	0

S.28.01.01 Minimum Capital Requirement – Only Life or only non-life insurance or reinsurance activity

Linear formula component for non-life insurance and reinsurance obligations

		C0010
R0010	MCRNL Result	63,458

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0020	C0030
R0020	Medical expenses insurance and proportional reinsurance	336,693	1,013,466
R0030	Income protection insurance and proportional reinsurance	0	0
R0040	Workers' compensation insurance and proportional reinsurance	0	0
R0050	Motor vehicle liability insurance and proportional reinsurance	0	0
R0060	Other motor insurance and proportional reinsurance	0	0
R0070	Marine, aviation and transport insurance and proportional reinsurance	0	0
R0080	Fire and other damage to property insurance and proportional reinsurance	0	0
R0090	General liability insurance and proportional reinsurance	0	0
R0100	Credit and suretyship insurance and proportional reinsurance	0	0
R0110	Legal expenses insurance and proportional reinsurance	0	0
R0120	Assistance and proportional reinsurance	0	0
R0130	Miscellaneous financial loss insurance and proportional reinsurance	0	0
R0140	Non-proportional health reinsurance	0	0
R0150	Non-proportional casualty reinsurance	0	0
R0160	Non-proportional marine, aviation and transport reinsurance	0	0
R0170	Non-proportional property reinsurance	0	0

Linear formula component for life insurance and reinsurance obligations

		C0040
R0200	MCRL Result	0

		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
		C0050	C0060
R0210	Obligations with profit participation - guaranteed benefits	0	
R0220	Obligations with profit participation - future discretionary benefits	0	
R0230	Index-linked and unit-linked insurance obligations	0	
R0240	Other life (re)insurance and health (re)insurance obligations	0	
R0250	Total capital at risk for all life (re)insurance obligations		0

	Overall MCR calculation	C0070
R0300	Linear MCR	63,458
R0310	SCR	213,679
R0320	MCR cap	96,155
R0330	MCR floor	53,420
R0340	Combined MCR	63,458
R0350	Absolute floor of the MCR	2,500

		C0070
R0400	**Minimum Capital Requirement**	**63,458**

Glossary

Community rating	PMI policyholders are charged the same premium for a particular PMI contract irrespective of age, gender or state of health, subject to certain prescribed exceptions.
Lifetime cover	PMI policyholders are entitled to renew their PMI contracts irrespective of factors such as age, health status or claims history.
Minimum benefits	PMI policyholders must be provided with certain minimum in-patient hospital cover.
Minimum Capital Requirement (MCR)	The level of capital below which an insurer is not permitted to go. It represents the final threshold that triggers supervisory action in the event that it is breached.
Generally Accepted Accounting Principles (GAAP) / Financial Reporting Standard (FRS)	These are accounting standards used for the preparation of financial statements.
Open enrolment	PMI insurers must accept all applicants for cover regardless of current age, sex or state of health, subject to certain waiting periods before claims may be made.
Own Funds	Own Funds are comprised of basic and ancillary own funds. Basic own funds refer to the excess of assets over liabilities, valued in accordance with Solvency II requirements. Ancillary own funds consist of items other than basic own funds which can be called up to absorb losses. They are categorised, i.e. tiered, based on set criteria.
Own Risk and Solvency Assessment (ORSA)	A set of processes used to provide insight, over the business planning time horizon, into the risk profile, capital requirements and strategy of an insurer. The information produced by these processes is used to support decision making.
Private medical insurance (PMI)	Insurance providing cover for costs incurred by private medical treatment or care due to illness, accident, infirmity or disability. Under Solvency II this is classified as Medical Expense Insurance.
Quantitative Reporting Templates (QRTs)	A set of standardised templates detailing financial and monetary information about an insurer.
Reinsurance	Insurance purchased by an insurer, used to transfer risk.
Risk Appetite Statement	The document which sets out the level and type of risk that an insurer is willing to take in order to achieve its business objectives.
Risk Profile	The specific risks to which an insurer is exposed. The risk profile of every insurer is different.
Risk-mitigation techniques	The methods used by an insurer to reduce risk exposure.

Solvency Capital Requirement (SCR)	The amount of capital that an insurer must hold that will enable them to absorb significant losses and gives reasonable assurance to policyholders and stakeholders that claims will be paid as they fall due. This amount is set at the worst 1 year loss that would be expected to occur in 200 years. The SCR can be calculated using the Standard Formula, an internal model or a partial internal model.
Solvency II	A harmonising risk based prudential regulatory regime that applies to all insurance and reinsurance undertakings in the European Union, which came into force on 1 January 2016.
Solvency II Risk Margin	The value above the technical provisions equivalent to a theoretical amount of money needed for a third party to take over and meet all of the insurance obligations.
Solvency II Technical Provisions	A liability on the Solvency II Balance Sheet. Technical provisions are a 'probability weighted best estimate' of the future cashflows associated with insurance obligations, which have been recognised at the valuation date.
Standard Formula	A formula set out within the Solvency II regime which details the calculations for generating the Solvency Capital Requirement (SCR). An insurer which chooses not to use the standard formula to calculate the SCR may use an internal model or partial internal model, subject to supervisory approval.
System of Governance	The system through which an insurer is organised and controlled.