Schroders

Schroder Pension Management Limited

Solvency and Financial Condition Report as at 31 December 2017

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Background and executive summary

This Solvency and Financial Condition Report (SFCR or the Report) has been prepared to enable the clients, and other stakeholders, of Schroder Pension Management Limited (SPML or the Company) to assess the financial position of the Company.

The Report contains the public disclosures required under the reporting section of the Prudential Regulation Authority (PRA) Rulebook, 'Solvency II Firms'. The PRA Rulebook incorporates the requirements set out in Article 51 (1) of Directive 2009/138/EC (the Solvency II Directive) and all directly applicable EU Regulations adopted in accordance with the Solvency II Directive (the Solvency II Regulations).

1.1 Business and performance

SPML is a limited company, incorporated and domiciled in the United Kingdom. Its ultimate parent company is Schroders plc and it operates as part of the Schroders Group (Schroders or the Group). In 2017, SPML generated profit before tax of £1.9 million (31 December 2016: £1.9 million).

The Company's principal activity is the provision of long-term life insurance services through unit-linked insurance and unit-linked reinsurance contracts. These contracts provide a tax efficient solution that enables SPML's clients to access a range of Schroders investment strategies. The Company's contracts do not include any financial options, other than surrender, or investment guarantees and the Company is not exposed to mortality or morbidity risks.

Unit-linked insurance contracts are issued solely to policyholders who are trustees of registered pension schemes. Unit-linked reinsurance is accepted from other life insurance companies wishing to expand the range of funds available to their unit-linked pension policyholders. All of SPML's business is carried out in the United Kingdom.

Revenue is earned as a percentage of assets under management (AUM), which represent assets backing unit-linked liabilities. The Company delegates the active management of these assets to another Group company, Schroder Investment Management Limited (SIM), together with the majority of its other operating activities. 96% of revenues are paid to SIM in exchange for the services received.

There were no significant changes to the Company's business operations or other events that had a material impact on the solvency and financial condition of the Company during 2017.

1.2 System of governance

SPML operates as part of the Schroders Group and is subject to the Schroders governance framework. The Schroders Group Annual Report and Accounts, which contains details of the Schroders governance framework, is available on the Schroders' corporate website at: www.schroders.com. The Board of Directors of SPML (the Board) is responsible for ensuring that an appropriate system of governance is in place for the Company.

The Board has established company specific risk management and internal control processes that align with the overall Schroders governance framework and extend this where relevant to the Company. The Board is supported by the SPML Risk Committee (the SRC), which is responsible for reviewing and monitoring the adequacy and effectiveness of the process for the identification, assessment, mitigation, monitoring and management of all risks faced by SPML.

The Company has identified a range of key functions that are important for the sound management of the Company. Individuals performing key functions are established as fit and proper through a robust framework of initial and ongoing assessment.

There were no significant changes to the Company's system of governance in 2017, although there were a number of changes to individuals in key roles. Three new directors were appointed to the Board, including a new Chairman. The Board, also, conducted a tender process during the year in respect of outsourced actuarial activities, which resulted in the appointment of a new Chief Actuary subject to supervisory approval. Further information about these changes and the Company's system of governance is provided in section B.

The Company has access to the Group's internal audit function, which provides independent and objective challenge to and assurance over the control environment through the effective evaluation of the risk management, control and governance arrangements.

The Company carries out an Own Risk and Solvency Assessment (ORSA) annually and more frequently if required. The ORSA process is intended to identify, assess, monitor, manage and report on both short and long term risks and to determine the capital required to ensure that the Company can continue to meet its solvency requirements. The ORSA enhances awareness of the risks faced by SPML and the capital needed given those risk exposures. This is used by the Company as part of its decision making process.

1.3 Risk profile

The Company's principal risk exposures relate to operational risk, market risk, surrender risk and credit risk.

- Operational risk is the risk of loss resulting from inadequate or failed processes, people and systems or from external events. The risk is mitigated under the terms of agreements between SPML and SIM whereby SPML is expected to be compensated in full for all material operational risk losses incurred
- Market risk is the risk that the value of an investment will decrease due to market factors. SPML has exposure to market risk on its linked and non-linked assets. The risk in relation to linked assets is a reduction in revenue. This risk is mitigated to a large extent as the Company's expenses are defined primarily as a percentage of revenue and therefore expenses fall as revenue falls
- Surrender risk, also referred to a lapse risk, is the risk that policyholders move their investments to another provider, thereby reducing the Company's revenue. Again, this risk is largely mitigated by the Company's expenses being defined primarily as a percentage of revenue
- Credit risk is the risk that a counterparty to a financial instrument will cause the Company financial loss by failing to discharge an obligation. SPML has exposure to credit risk from its holdings in assets, other than those allocated to unit-linked contracts, where the risk is that a counterparty will be unable to pay in full amounts when due

SPML has limited exposure to other types of risk, including underwriting risk and liquidity risk. There have been no significant changes to the risk profile of the company during 2017. Further details on the Company's risk profile are set out in section C of this Report.

1.4 Valuation for solvency purposes

The assets and liabilities of the Company are valued for solvency purposes in accordance with the Solvency II regulations. The Solvency II balance sheet is consistent with the Company's financial statements, which are prepared under International Financial Reporting Standards (IFRS), except for the items set out in the table below:

	As at 31 Dec 2017 £'000	As at 31 Dec 2016 £'000
Excess of assets over liabilities (IFRS basis)	**40,226**	**38,598**
Items not recognised in the financial statements:		
Present value of future profits (PVFP)	428	400
Risk margin	(651)	(683)
Deferred tax asset	–	54
Excess of assets over liabilities (Solvency II basis)	**40,003**	**38,369**

The PVFP is the best estimate of the excess of policy charges over expenses, which is determined using a cash-flow projection model over a period of three months. This reflects the Company's ability to terminate all contracts subject to a three month notice period.

Given all business has a three month projection period, the risk margin has been determined over a one year period (the minimum permitted under Solvency II regulations), and has been calculated on the result of the SCR at the valuation date but with the result of the market risk module and counterparty default risk module for bank counterparties set to equal zero on the assumption that these risks could be hedged if required.

1.5 Capital management

The Board of SPML reviews the Company's capital position on a regular basis and determines the appropriate capital to be maintained by the Company. It is the Board's intention that, under normal circumstances, the Company will at all times maintain own funds of no less than the higher of 200% of the Company's Pillar 1 Solvency Capital Requirement (SCR) and the capital requirement calculated under the Own Risk and Solvency Assessment (ORSA).

	As at 31 Dec 2017 £'000	As at 31 Dec 2016 £'000
Solvency Capital Requirement (SCR)	**10,138**	**9,982**
Total eligible amount of own funds to cover the SCR, of which:	40,003	38,369
– Tier 1 Unrestricted	40,003	38,315
– Tier 3	–	54
Minimum Capital Requirement (MCR)	**4,562**	**4,492**
Total eligible amount of basic own funds to cover the MCR (all Tier 1 Unrestricted)	40,003	38,315
Solvency ratio of SPML (own funds divided by the SCR)	**395%**	**384%**

The Company does not use volatility or matching adjustments, or transitional arrangements. The SCR has increased by £0.1 million to £10.1 million at 31 December 2017 (2016: £10.0 million). This increase is primarily due to an increase in the operational risk component of the SCR, which increased the impact on the SCR of £1.0 million, offset by an increase in the tax adjustment. The tax adjustment, which reflects a revised methodology, had the impact of reducing the SCR by £0.8 million.

There have been no instances of non-compliance with the Minimum Capital Requirement (MCR) or SCR during 2017. See section E.1 for further details on the Company's Own Funds.

1.6 Governance

The Directors have certified that the SFCR has been properly prepared in all material respects in accordance with the PRA rules and Solvency II regulations and that SPML has complied and will continue to comply with the PRA rules and Solvency II in the future.

Section A Business and performance

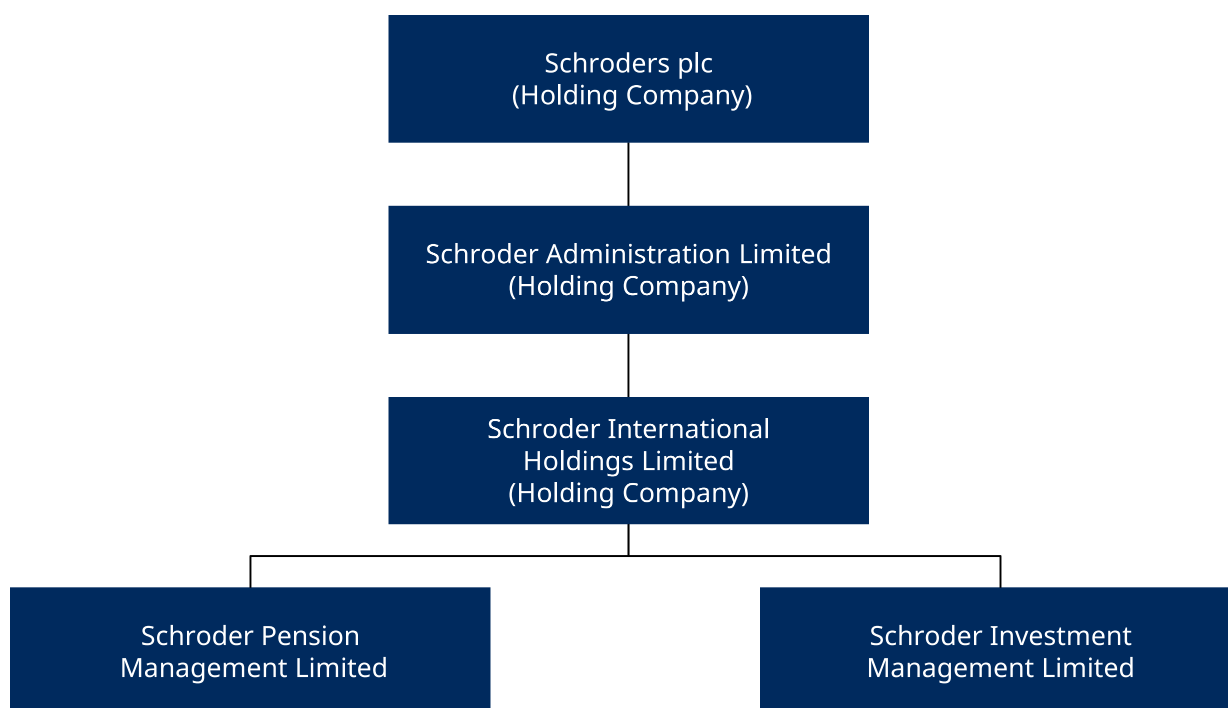
A.1 Business

SPML is a company limited by shares and is incorporated and domiciled in England and Wales. The registered address of the Company is 31 Gresham Street, London, EC2V 7QA.

SPML is a wholly owned subsidiary of Schroder International Holdings Limited (SIHL). The Company's ultimate controlling entity is Schroders plc. SIHL and Schroders plc are both incorporated and domiciled in England and Wales. Schroders plc and its subsidiaries combine to form the Schroders Group (Schroders or the Group).

The Company did not make any distributions to its shareholder during the years ended 31 December 2016 and 2017.

Simplified Group Structure as at 31 December 2017



During 2017, SIM's immediate parent company, Schroder Administration Limited (SAL), transferred its share ownership of SIM to SIHL, which is itself a wholly owned subsidiary of SAL, in a share for share exchange. The activities of SIM have not changed and there was no impact to the investment management agreement and service agreement held with SPML.

Supervision and external audit

SPML is authorised by the PRA and regulated by the PRA and the Financial Conduct Authority (FCA). Financial supervision is undertaken by the Retail Life department of the PRA. They can be contacted at:

– PRA: Bank of England, 20 Moorgate, London, EC2R 6DA

– FCA: 25 North Colonnade, London, EH14 5HS.

SPML is audited by PricewaterhouseCoopers LLP (PwC), chartered accountants and statutory auditors, 7 More London Riverside, London SE1 2RT. Following the approval of the SFCR for 2017, Ernst & Young LLP (EY) will be appointed as Independent Auditors for Schroders, including SPML, for the year ending 31 December 2018.

Lines of business

SPML writes:

– Unit-linked insurance contracts that are issued solely to policyholders who are trustees of UK registered pension schemes; and

– Unit-linked reinsurance that is accepted from other life insurance companies wishing to expand the range of funds available to their unit-linked UK pension policyholders

All business is carried out in the United Kingdom. Contracts issued by SPML contain no financial options, other than surrender, or investment guarantees.

SPML's operating model

SPML outsources almost all functions to Schroder Investment Management Limited (SIM), a wholly owned subsidiary of Schroders plc. The outsourcing arrangement is governed by an investment management agreement and a services agreement between SPML and SIM. SIM sub-contracts certain activities to third-party companies including J.P. Morgan Europe Limited (JPMorgan) for fund accounting services and DST Financial Services (DST), (previously IFDS (International Financial Data Services Limited)), following the acquisition of IFDS by DST in 2017 for transfer agency services.

SPML outsources the actuarial function role to Willis Towers Watson plc (WTW) (effective from 1 January 2018, Barnett Waddingham LLP (BW), subject to supervisory approval). The services provided are set out in an agreement between SPML and WTW (BW from 1 January 2018).

SPML also contracts directly with JPMorgan Chase Bank, N.A. (JPMorgan Chase) for custody services.

SPML has no employees. Staff involved in the management and operating activities of SPML are employed by SIM and the costs of these staff are largely met by SIM, reflecting its delegated responsibilities. Costs specifically associated with managing the business of SPML are recharged to SPML from SIM, or are borne directly by SPML. The costs borne directly by SPML are minimal, reflecting that most operating activities are performed by SIM through the outsourcing arrangements.

SIM receives 96% of the annual management fees earned by the Company for taking delegated responsibilities in respect of the SPML business in accordance with the Group's transfer pricing policy. In turn, SIM pays fees to other Group companies for services provided. These can arise through investor introductions and client relationship specific investment activities, or through investing via a mutual fund where contractual fees may arise.

Significant business and events

During 2017 PwC continued as the Company's auditors. Following an audit tender process conducted by the Schroders plc Audit and Risk Committee, PwC will resign following the approval of the 2017 SFCR and EY will be appointed as Independent Auditors for Schroders, including SPML, for the year ending 31 December 2018.

Three new directors were appointed to the Board during 2017, and a new Chairman was also appointed. Although these key individuals have changed in the year, there were no significant changes to the system of governance.

There have been no other material changes during the reporting period with respect to the Company's business and performance, system of governance or risk profile.

Events since 31 December 2017

Following a tender process, BW took over the actuarial function role from WTW effective from 1 January 2018. John Hoskin, a partner at BW, is now SPML's Chief Actuary, subject to supervisory approval.

A.2 Underwriting performance

SPML only writes unit-linked pension business and no policies include any financial options, other than surrender, or guarantees. The Company is not therefore exposed to any insurance risk.

Under the terms of the outsourcing arrangement, SIM is responsible for all activities related to the underwriting performance, which is solely dependent on the fee income earned on unit-linked assets invested by policyholders less expenses incurred in the management of the policies. The expenses associated with this agreement are correlated to the management fee income received meaning that ordinarily the Company will report a positive underwriting result. Management fees retained cover other operating expenses of the Company.

Net management fees charged reduced by £0.4 million to £54.2 million (31 December 2016: £54.7 million), driven by a 4 bps decrease in margin following the loyalty discount given to investors in the Schroder Life Diversified Growth Fund (DGF) and Schroder Life Intermediated Diversified Growth Fund (iDGF). The impact of this discount was partly offset by a £0.7 billion increase in AUM. Net fee income of £55.0 million has remained stable on 2016. The retained net revenue margin of 4%, after ceding to other Group entities, is in line with the Group's transfer pricing policy.

Description	2017			2016			Variance
	Index-linked and unit-linked insurance £'000	Accepted reinsurance £'000	Total £'000	Index-linked and unit-linked insurance £'000	Accepted reinsurance £'000	Total £'000	
Net management fees charged	36,666	17,556	54,222	39,072	15,589	54,661	(439)
Performance fees	495	237	732	199	79	278	454
Net fee income before Group charges	**37,161**	**17,793**	**54,954**	**39,271**	**15,668**	**54,939**	**15**
Fee cedes to other Group companies							
Management fees ceded to other Group companies	(35,227)	(16,866)	(52,093)	(37,564)	(14,987)	(52,551)	458
Performance fees ceded to other Group companies	(495)	(237)	(732)	(191)	(76)	(267)	(465)
Net fee income retained after fee share to other Group companies	**1,439**	**690**	**2,129**	**1,516**	**605**	**2,121**	**8**

Total operating expenses remained flat during the year at £0.5 million (year ended 31 December 2016: £0.5 million).

Description	2017 £'000	2016 £'000	Variance £'000
Professional fees	(322)	(373)	51
Non-recoverable indirect taxes	(46)	(71)	25
Other expenses	(87)	(49)	(38)
Total operating expenses	**(455)**	**(493)**	**38**

A.3 Investment performance

Financial highlights

In the year ended 31 December 2017, unit-linked liabilities increased by £332.0 million (3%) to £10,518.2 million (31 December 2016: £10,186.2 million). SPML generated a profit before tax of £1.9 million for the year ended 31 December 2017 (2016: £1.9 million). Net fee income and direct costs remained stable during the year.

Investment activity with respect to unit-linked policyholders

SPML does not bear investment risk on behalf of policyholders. Investments held on behalf of unit-linked policyholders are made in line with the published objectives of the life funds and match liabilities exactly. Accordingly, the Company has a minimal exposure to future returns through fees earned.

The table below shows the movement in the Company's unit-linked liabilities. Premiums received and claims paid reflect new investments and withdrawals by policyholders in the Company's Life funds. The increase in unit-linked assets passed on to policyholders is offset by an equivalent change in unit-linked liabilities. Management fees are charged based on the unit-linked assets, and are either deducted directly from the Life funds or are billed to and collected directly from policyholders.

In the year ended 31 December 2017, unit-linked liabilities increased by £332.0 million (3%) to £10,518.2 million (31 December 2016: £10,186.2 million) on a financial statement basis. The movement in fund assets includes premiums of £2,247.8 million less claims of £2,864.0 million with investment returns less management fees charged to the fund and other movements generating a positive return of £948.2 million.

Description	2017 £'000	2016 £'000	Variance £'000
Premiums received	2,247,807	1,500,837	746,970
Claims	(2,863,999)	(2,257,134)	(606,865)
Investment return	987,377	1,305,263	(317,886)
Management fees charged directly to the life funds	(39,172)	(40,524)	1,352
Increase in unit-linked assets	**332,013**	**508,442**	**(176,429)**
Increase in unit-linked liabilities	(332,013)	(508,442)	176,429
Net impact on underwriting performance of the Company	**0**	**0**	**0**

Investment activity with respect to the Company's non-linked investments

Non-linked investments are mostly invested in cash and the Schroder Special Situations Fund – Sterling Liquidity Plus (SSSF SLP). Interest income is also earned on the loan to Schroders plc. SPML holds no direct investment in securitisations.

The SSSF SLP investment held by SPML is designated as an available-for-sale (AFS) asset meaning all fair value movements from date of purchase until disposal date are taken through other comprehensive income (OCI). Upon disposal, fair value gains or losses are recycled through the income statement in line with International Financial Reporting Standards (IFRS). The Company made a gain of £0.1 million on this investment in 2017 (net of tax), leaving a year end market value of £15.4 million (31 December 2016: £15.3 million).

Description	2017 £'000	2016 £'000	Variance £'000
Net fair value movement arising from AFS financial assets	75	103	(28)
Tax charge on items taken directly to OCI	(8)	–	(8)
Other comprehensive income for the year, net of tax	**67**	**103**	**(36)**

The Company also earned net interest income predominantly on the loan to Schroders plc and other non-linked cash holdings of £260,000 in 2017 (2016: £288,000).

A.4 Performance of other activities

SPML does not hold any financial leases or operating leases. There are no other activities.

A.5 Any other information

Service agreements

The service agreements in place between SPML and SIM make provision for those Group companies to meet any costs resulting from operational failure of the services performed. The service agreements were enforced over the reporting period such that SPML did not meet any significant operational risk event losses.

Section B System of governance

B.1 General information on the system of governance

The strategy for the Group is set by the Board of Schroders plc. SPML operates within the overall strategy of the Group. The Schroders plc Board ensures that SPML's strategy is appropriate for the Group, and that it promotes the success of the Company within the Group's overall business plan.

The Board of Directors of SPML (the Board) is the Company's governance and management body for regulatory purposes. The Board meets at least four times per year. The Board is responsible for ensuring sound governance, that the operational effectiveness of the risk management and control environment is maintained and that effective risk management policies are adhered to within the Schroders Group Risk Management Framework. The Board has responsibility for providing effective oversight of those who exercise executive functions.

The Board primarily consists of employees of SIM, as well as two independent (non-executive) directors. It is supported by the SPML Risk Committee which reports to the Company's Chief Executive Officer (CEO).

Other than changes in the directors of the business, set out in the table below, there have been no material changes to the governance structure of SPML in the year to 31 December 2017.

The composition of the SPML Board as at the date of approval of this SFCR is detailed in the below table:

Director	Approved function
Guy Henriques[1]	SIMF 9 Chairman
David Heathcock	SIMF 1 Chief Executive Officer
Wayne Mepham	SIMF 2 Chief Finance Function
Julian Walker-Hazell[2]	CF 1 Director
Graham Aslet	SIMF 14 Senior Independent Director
Calum Thomson[3]	Non-Executive Director

[1]Appointed as Chairman on 27 April 2017. Replaced John Troiano who resigned from the Board on 12 May 2017.
[2]Appointed 1 February 2017.
[3]Appointed 1 April 2017.

The CEO of SPML has overall responsibility for the implementation of SPML's strategy and the executive management and operation of the business. His key responsibilities include:

Implementing SPML's strategy and initiatives

- Communication and implementation of the Company's strategy; and
- Development and maintenance of the Company's business model by the governing body.

Managing the day to day activities of the Company

- Executive management of SPML's business;
- Management of the day to day business of SPML, with the exception of the matters reserved for the decision of the Board; and
- Regular reporting to the Board.

Maintaining an appropriate culture

- Overseeing the adoption of the Company's culture in its day-to-day management;
- Overseeing the efficient and effective operation of SPML within regulatory and best practice parameters and in accordance with SPML specific and Group policies;
- Ensuring the operation of the Company with a framework of prudent and effective risk management;

- Ensuring the production of reporting material to support the Company's governance framework;
- Ensuring that delegated responsibilities are clearly identified within job descriptions and agreements with third parties;
- Ensuring that the relationship with internal and external suppliers is proactively managed to ensure issue resolution;
- Ensuring that the Company has complied with the obligation to ensure that every person who performs a key function is fit and proper; and
- Policies and procedures for the induction, training and professional development.

SPML Risk Committee

The purpose of the SRC is to assist the SPML Board and the SPML CEO in discharging their responsibilities. The SRC is responsible for reviewing and monitoring the adequacy and effectiveness of the process for the identification, assessment, mitigation, monitoring and management of all risks faced by SPML in achieving its business objectives. Specifically the SRC aims to:

- Support effective risk management in SPML in line with the Group approach;
- Provide greater transparency on risk trends and highlight key issues;
- Support the annual ORSA review;
- Bring together key SPML stakeholders to discuss risk matters of relevance to SPML; and
- Look for continuous improvements in the SPML risk framework.

Key roles and responsibilities

The table below details the key functions applicable to the Company. SPML's Chief Actuary until 31 December 2017, Trevor Fannin, is an employee of WTW. John Hoskin, a partner of BW, was appointed as SPML's Chief Actuary on 1 January 2018, subject to supervisory approval.

Key function	Outsourced counterparty	Senior Insurance Managers Regime approved function	Responsibilities
Finance	SIM	SIMF 2 – Chief Finance Officer (CFO)	Responsible for all finance activity, including financial controls, financial reporting and regulatory reporting
Risk Management	SIM	SIMF 4 – Chief Risk Officer	Responsible for the risk management framework, policies and controls in addition to identifying and monitoring SPML's key risks
Internal audit	SIM	SIMF 5 – Internal Audit	Assesses the adequacy and effectiveness of the internal control environment. Determines annual internal audit plan. Reports the results of audits which are relevant to SPML to the Board
Actuarial Function Holder	WTW/BW[1]	SIMF 20 – Chief Actuary	Coordinates the calculation of the Company's technical provisions, ensuring the appropriateness of the methodologies and underlying models used. Contributes to the effectiveness of the risk management system
Compliance	SIM	CF 10 – Compliance	Responsibility for ensuring that the Company is managing its regulatory risks appropriately
Financial Crime	SIM	CF 11 – Money laundering reporting	Responsibility for ensuring the effectiveness of controls around fraud risks, bribery and money laundering

[1] Willis Towers Watson plc (until 31 December 2017), Barnett Waddingham LLP (from 1 January 2018 subject to supervisory approval).

SPML's remuneration policy

SPML has no employees and does not therefore incur any direct salary costs. The emoluments of the non-executive directors are borne directly by the Company.

The remuneration strategy is set by the Group Remuneration Committee. The Group Remuneration Committee is responsible for reviewing and approving the remuneration and policies of the Group, as recommended by the Group Chief Executive. The remuneration policy is aligned to the long-term business strategy, business objectives, risk appetite, values and long-term interests of the Group and will recognise the interests of relevant stakeholders.

In reviewing the remuneration strategy and policies the Group Remuneration Committee considers the following factors:

- That the remuneration practices in place are consistent with effective risk management and do not encourage excessive or inappropriate risk taking;
- That any performance related compensation arrangements maintain an appropriate balance between managed risk, both current and future, and reward, and that they do not encourage behaviour which is detrimental to the interests of stakeholders;
- That relevant provisions and recommendations of Remuneration Codes and other relevant regulations as these apply to the Group are properly incorporated; and
- That provisions of the UK Corporate Governance Code and the other relevant legal or regulatory requirements, together with associated guidance are fully considered.

Transactions with related parties

During the year ended 31 December 2017, the Company had the following transactions (as reported in the Company's Annual Report and Accounts) with related parties within the Schroders Group:

	Income £'000	Expenses £'000	Amounts owed by related parties £'000	Amounts owed to related parties £'000
Ultimate parent	266	–	21,630	–
Other related companies within the Schroders Group	952	(52,926)	767	(5,075)

During the year ended 31 December 2016, the Company had the following transactions (as reported in the Company's Annual Report and Accounts) with related parties within the Schroders Group:

	Income £'000	Expenses £'000	Amounts owed by related parties £'000	Amounts owed to related parties £'000
Ultimate parent	280	–	21,649	–
Other related companies within the Schroders Group	1,535	(54,489)	992	(5,897)

Amounts owed by related parties include a loan of £21.5 million to Schroders plc (2016: £21.5 million).

All transactions with related parties are made at an arm's length basis on normal commercial terms.

B.2 Fit and proper requirements

Schroders operates in an environment where maintaining the highest possible professional standards is essential in order to minimise exposure to financial and regulatory risks and to promote the Group's reputation as a market leader.

Whilst additional focus is given to employees exercising governance or oversight roles, Schroders requires all employees to demonstrate integrity and professional competence at all times.

SPML Directors are required to adhere to the following regulatory standards:

PRA Individual Conduct Standards (required of all key function holders)

1. Act with integrity;
2. Act with due skill, care and diligence; and
3. Be open and cooperative with the FCA, the PRA and other regulatory bodies.

Senior Insurance Manager Conduct Standards

1. Take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively;
2. Take reasonable steps to ensure that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system;
3. Take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person;
4. Disclose appropriately any information of which the FCA or PRA would reasonably expect notice; and
5. Exercising responsibilities, due regard to the interests of current and potential future policyholders in ensuring the provision by the firm of an appropriate degree of protection for their insured benefits.

The section below outlines the Schroders processes and practices to ensure that relevant employees meet the fit and proper test:

Initial assessment

In order to ensure that employees recruited by Schroders have the required skills and behaviours, a clearly defined process of pre-employment screening is followed. A risk-based approach is used to assess the level of screening required, with three levels identified:

- **Tier One**: FCA Controlled Functions and Significant Influence Functions which require the most extensive screening
- **Tier Two**: Approved Persons and others in roles that might have a higher level of risk (such as finance or payroll)
- **Tier Three**: Other new hires

The recruitment process includes an assessment of education, professional qualifications and employment history, and uses competency based interview techniques to ascertain whether or not the candidates have the technical competence to fulfil the role for which they are applying. All hires undergo thorough reference, criminal record and regulatory sanctions checks.

For Tier One candidates, the line manager is required to provide the Group's compliance department with a competence statement. This statement outlines how the appointment complements Schroders' business strategy, how the appointment was agreed, information on the employee's background and experience and their expected impact on the role together with how the decision was made to employ them.

On-going assessment

The assessment of staff members' on-going competence for the role that they are performing is primarily the responsibility of the individual's immediate manager and is facilitated through the formal appraisal process which is documented in Human Resources policies.

All Schroder employees are required to complete an annual declaration which assesses fitness and propriety. The individual is responsible for informing Human Resources of any subsequent changes to the responses provided in the questionnaire.

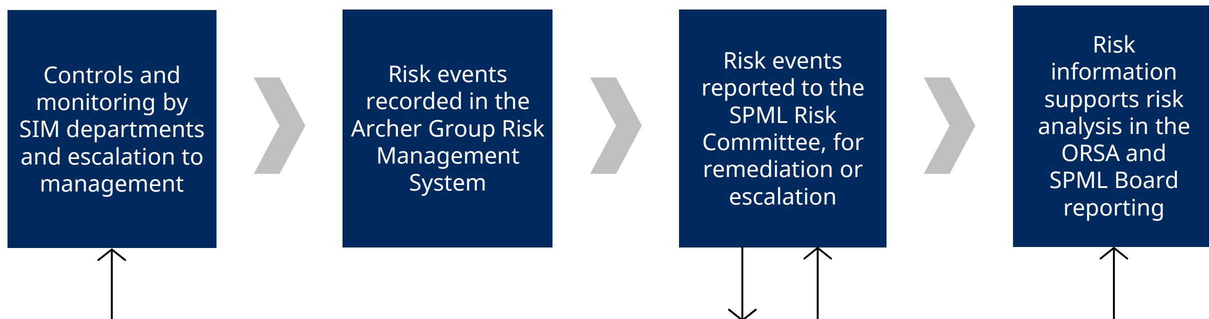
Should an individual's manager or the relevant board become aware of any information that may be relevant to an assessment of fitness and propriety that was either not previously known, or which casts doubt on the individual's ability to perform their function, a full assessment is expected to be promptly undertaken at the earliest opportunity, with input from Human Resources if required.

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

Risk management approach

The Group's approach to risk management is outlined in its 'Pillar 3 Disclosures' document and the Group Annual Report and Accounts which are available on the Schroders' corporate website: www.schroders.com.

SPML operates within the Group's Risk Framework, supplemented by SPML's own Risk Management Framework which is overseen by the SPML Board. SPML considers risks from both a bottom-up and a top down perspective to mitigate their impact and minimise financial and reputational losses. A high level description of the process is shown below, with a feedback loop to support the ongoing risk management process.



SPML's Risk Management Framework is supported by the Group Risk function. Group policies apply to SPML and these are used by staff involved in the management of SPML activities, to help maintain effectiveness of governance and controls. SPML's Board of Directors is also responsible for ensuring sound governance and controls are maintained and that SPML has an effective risk management process.

Risk appetite and solvency cover

SPML faces a range of risks that the Board accepts are a consequence of the company's business model and strategy, and which require management and mitigation. SPML's risk appetite is primarily set by its target solvency cover, which impacts the level of capital required and corresponding capital management approach.

Target solvency cover

Under Solvency II, SPML must hold capital at least equal to the SCR. Insurance policyholders that use the standard formula to calculate their SCR and place reinsurance with SPML are also required to hold capital for the risk of SPML default on the reinsurance arrangement. In order to limit the Solvency II capital requirements for such policyholders, SPML has decided to maintain SCR coverage of at least 200%, plus a buffer to allow for risk events.

Risk appetite for key risks

SPML operates within the Group's overall risk appetite framework but also faces specific risks due to the nature of insurance business. The SPML Board is required to set and approve risk appetite which is done at least annually through the ORSA process.

The Group has in place a risk appetite framework which:

– Assesses risk position against risk appetite for key risks; and
– Supports risk appetite statements and metrics to ensure risk appetite is quantified, where possible, and is aligned to our key risks.

The Schroders Group Internal Capital Adequacy Assessment Process (ICAAP) takes account of the risks accepted by the Group including those in respect of the SPML business delegated to SIM. The ICAAP is determined at the same confidence level as SPML's own risk capital assessment and provides support that relevant Group companies will be able to fulfil their contractual obligations to SPML.

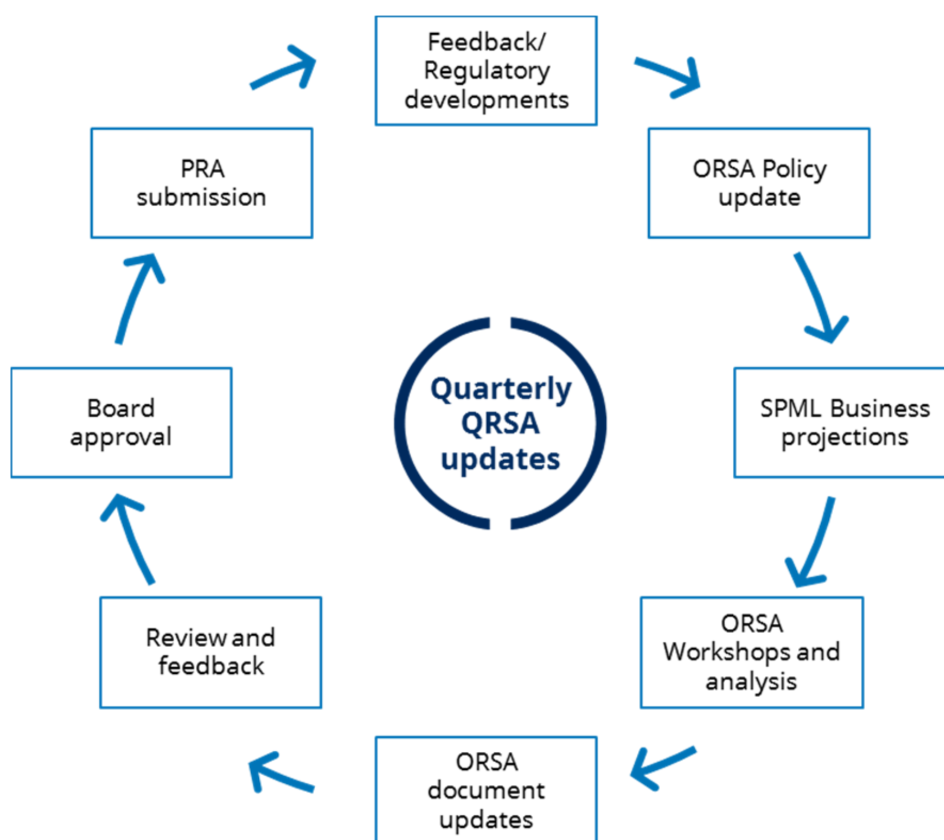
The process for establishing and updating a risk appetite for SPML's key risks is incorporated in the ORSA risk workshops. Stakeholders are required to review risk appetite statements and metrics in order to ensure they accurately reflect the risk profile. This information is then used to assess how individual risks may contribute to the overall risk appetite for SPML and impact the risk profile of the business. Stakeholders are also required to review risk appetite on an ongoing basis.

Own risk and solvency assessment (ORSA)

The ORSA sets out SPML's own assessment of its capital requirements under Solvency II. The ORSA is a continuous process which includes involvement from the Board, Compliance, the Chief Actuary, Finance and Risk. It is reviewed by the Board on a quarterly basis and is formally approved by the Board annually.

The annual ORSA review process involves a number of key stages. The quarterly ORSA updates provide a more frequent review of SPML's risk profile and solvency.

ORSA process



The ORSA is prepared by considering the risks to which SPML is exposed and the mitigating circumstances which might limit the impact of those risks. The assessment is made for SPML as a stand-alone entity.

The ORSA process is carried out with the full involvement and approval of the Board. During the process, a number of key staff within the Group are interviewed and their views sought on the possible risk scenarios and the mitigating circumstances. In addition, SPML's Chief Actuary provides comments and input into the process.

Particular points of note on the ORSA process are as follows:

- The report is subject to review and challenge by members of the Board and other senior Schroders staff;
- The scenarios, which reflect possible business outcomes under different circumstances, identified as being of potentially material risk to SPML are discussed and verified with members of Schroders staff having day-to-day responsibility for the areas in question;
- Other members of Schroders staff from the risk management, finance, product development and legal areas are consulted throughout the process, their views being sought particularly on the availability of Group capital and insurance, on the ability of SPML to rely on its third-party service providers (e.g. SIM

directly, and indirectly through SIM to DST and JPMorgan) and on the controls in place to prevent additional risk being introduced through changes to the business model, such as through new product developments;

- The Board are kept informed of progress throughout the ORSA process;
- SPML's Chief Actuary provides independent external advice on the process, and confirms that the conclusions reached are considered reasonable taking into account the information provided and on the assumption that the agreements between SPML and its service providers provide SPML with protection against losses incurred as a result of the service provider's actions; and
- The Board considers and approves the ORSA and it is taken into consideration when making decisions on behalf of the Company.
- The ORSA captures all material risks in calculating its own solvency needs

The ORSA capital requirement is intended to be calculated at a confidence interval of 99.5% over a one-year period, extended throughout the Company's business planning period. This confidence interval represents SPML's own risk budget and is consistent with the risk budget of the Group. Given the relatively simple nature of the risks faced by SPML, a pragmatic approach is taken such that some elements of the calculations are considered to be stronger than 99.5% confidence. Consideration is given as to whether the capital calculated at the balance sheet date needs to be increased to allow for possible increases in capital requirements over SPML's five-year business planning period.

For risks identified as being both plausible and material, an assessment of the possible cost to SPML of those risks occurring is made through scenario analysis. In making these assessments, account is taken of the operating model of SPML and the ability of service providers to compensate for any operational losses. The analysis has been performed over the business planning period where possible.

ORSA frequency

The full ORSA report is produced on an annual basis, or more frequently in response to major business changes. The SRC and SPML Board also receive a quarterly ORSA update, in the form of a shortened report, to provide:

- A summary of the estimated capital requirements on a SCR and ORSA basis;
- Information on capital resources;
- Updates on the key risks and risk events; and
- Other business changes during the period.

Significant changes to the SPML business model, operating model or risk profile may prompt an ad-hoc ORSA review. This is subject to agreement between the SPML Board and Group Head of Risk. In performing an ad-hoc ORSA, any deviations or change from the usual ORSA process, including availability/use of data and information are to be noted in the report. Changes that may require an ad-hoc ORSA for SPML include:

- Entering a new class of business;
- Significant changes to business strategy;
- Significant change to the risk appetite; and
- Material risk changes.

Any significant changes or updates to the ORSA approach, process or result are to be communicated to all key stakeholders, as soon as practicable. The SPML Board may decide to change aspects of the ORSA approach or process, in response to internal or external factors impacting the business. Changes to SPML's risk, solvency profile or regulatory requirements may affect the ORSA results – which may also require a review of the ORSA process.

The ORSA and SPML business strategy

As stated, SPML's business strategy is set by the Schroders plc Board and Senior Management within the Group. SPML is a distribution channel of the UK Institutional business and, therefore its business strategy is led by strategy for the UK Institutional business. SPML's final business strategy is usually presented to the SPML Board in Q2 of the year.

This approach allows the SPML Board to review the ORSA output alongside development of SPML's business strategy. It is important to note that the ORSA process involves an ongoing review of SPML's risk profile and key risks, together with impact from any changes in SPML's business strategy or products. This is reported to the SPML Board via quarterly ORSA updates (further details below), which are an integral part of the SPML risk framework. Given the nature of SPML's business, the SPML Board feel that this approach is a pragmatic way to incorporate business strategy within the ORSA process.

Key risk identification and assessment

The ORSA capital requirement has been estimated using a risk identification, quantification and stress testing based approach. Balance sheet date stresses have been used, intended to be at least as strong as a 99.5% confidence interval stress, applied to value at risk over a one-year time period. Consideration is then given to whether the capital determined by the balance sheet date stresses should be increased, to allow for potential increases in required capital over the business planning period.

SPML does not allow for diversification effects between different types of risk in its ORSA calculations (although it does allow for diversification within different market risks) and does not allow for the possible tax impacts that might otherwise reduce required capital on an ORSA basis. This approach is considered to be prudent and proportional to the overall methodology employed.

The key management action considered in the ORSA assessment is that the SPML Board may, if necessary, give notice of termination of the policy contracts, subject to a notice period of three months. In this event, the business would be expected to be closed and have no liabilities to customers within three months.

The Board would consider possible and/or necessary actions if the results of the ORSA indicate required capital is, or may become, unacceptably high taking into account the risk, required capital and the specific circumstances. Such actions include amendment to the risk management system to better control or mitigate those risks contributing to the capital requirement. Conversely, any proposed changes to the risk management system are considered as part of the ORSA process to determine the likely impact on the Company's capital position.

B.4 Internal control

The Company's internal control is governed by the Board – refer to section B.1 of this report for an outline of the Company's system of governance.

SPML outsources its operations to SIM and accordingly the internal controls in place at SIM indirectly impact the Company. Details of these controls are outlined in the Internal Controls Report (ISAE 3402/AAF 01/06) which is audited annually.

Group compliance supports the SPML Board in respect of relevant regulatory developments that may impact SPML. The quarterly compliance report to the SPML Board covers: regulatory relationships and key interactions, significant compliance issues and activities, compliance monitoring and key regulatory developments. This is provided and presented by the Head of Distribution Compliance.

Responsibilities and competences of the Group compliance function are detailed in the Group compliance charter, including measures for monitoring, advising and reporting. The majority of policies in the UK Compliance Manual that address essential compliance requirements are established, implemented and maintained by Compliance. Links to relevant Group policies are also included in the manual. The manual is periodically reviewed by Compliance. Updates are made where necessary – for example to accommodate a significant regulatory development or change to internal compliance arrangements. Individual policies are reviewed by the respective owner at least annually.

B.5 Internal audit function

Overview

The operating model employed by SPML means that is does not have its own internal audit function. The Group's internal audit function does however perform work over areas relevant to the Company.

Role and reporting of Group Internal Audit

The role of Group Internal Audit (GIA) is to provide independent and objective challenge to and assurance over the Group's control environment through the effective evaluation of the risk management, control and governance arrangements implemented by management.

GIA is fully independent of line management with the primary reporting line to the Chairman of Schroders' Board Audit and Risk Committee (BARC). All members of the BARC are non-executive directors of Schroders plc. There is a secondary reporting line to the Group Chief Executive.

The work of GIA is reported to the:

- BARC;
- Group Risk Committee;
- Group Management Committee; and
- Subsidiary entities Board of Directors.

GIA is a stand-alone function within the Group and personnel within GIA do not perform any other functions on behalf of SPML (or any other Group entities).

B.6 Actuarial function

SPML outsources the Chief Actuary role to BW. The Chief Actuary, John Hoskin (subject to regulatory approval), is a partner of BW and is responsible for the organisation and delivery of the SPML actuarial function activities. The performance of the Chief Actuary and actuarial function is monitored by the Chief Executive Officer of SPML. Prior to 1 January 2018, SPML outsourced the Chief Actuary role to Trevor Fannin of WTW on a similar basis.

The services provided by the Chief Actuary are detailed in a statement of work and are performed in line with the requirements of the actuarial function as set out in Rule 6.1 of the PRA Rulebook: *Solvency II firms: Conditions Governing Business* and the provisions of the PRA Rulebook: *Solvency II Firms: Actuaries*. The Chief Actuary carries out the role of the "external actuary" referred to in paragraph 2.1 of PRA 2015/29 (*Solvency II Firms: Actuaries Instrument 2015*).

The activities of the actuarial function follow the requirements set out under Article 48 of the Solvency II Directive.

B.7 Outsourcing

SPML outsources its key activities for the following reasons:

- SPML's primary purpose is to act as a vehicle to 'wrap' Schroders investment solutions;
- The Company has no employees; and
- Efficiency – activities are outsourced to take advantage of Group and external expertise.

The Company, either directly or indirectly, utilises various outsourced parties to conduct these key activities. These arrangements include a direct outsourcing arrangement with SIM for various services including investment management, operations, sales, marketing and distribution. SIM, in accordance with the terms of the services agreement, has outsourced transfer agency services and fund accounting services to IFDS (now DST, following the acquisition of IFDS) and JPMorgan respectively. SPML also has direct outsourced relationships with WTW for Actuarial services (now BW, following a tender process leading to a change in provider from 2018) and with JPMorgan Chase for custodian services. All of SPML's outsourced service providers are located in the United Kingdom.

SPML is bound by the Group policy with respect to outsourcing arrangements which sets out guidelines with respect to the following areas:

- **Guidelines on making the decision to outsource** – Prior to making the decision to outsource a service, a cost benefit analysis is undertaken which includes consideration of the associated risks of delivering the services in-house versus through an outsourced service provider (including analysis of long-term operational dependencies)
- **Selection of provider and key governing principles** – Once the outsource service provision has been approved a sponsor must be appointed. The sponsor has primary responsibility for the selection and approval process. Depending on the nature of the service required the sponsor should consider the involvement of the following departments; Group Risk, Compliance, Group Finance and Information Assurance. In most cases, it will be appropriate to involve the procurement team, based in London, who will offer guidance and support
- **Due diligence** – Prior to any appointment being made due diligence must be performed to confirm that the service provider can deliver the services required and will comply with its obligations

B.8 Any other information

The Group has established a permanent and effective Compliance function which operates independently and which monitors and assesses the adequacy and effectiveness of the measures, policies and procedures put in place by the Group and the Company in relation to its regulatory requirements and advises the Board in relation to those matters. The Company has assessed the adequacy of the system of governance and feel it is adequate to respond to the risks inherent to SPML due to the nature and simple structure of the business.

Section C Risk profile

SPML offers a life insurance 'wrapper' for Schroders' investment strategies, providing tax and administratively efficient investment solutions for pension schemes. SPML is capitalised as a stand-alone entity but is inextricably linked to the Group; agreements between SPML and other Group companies are structured in such a way as to minimise the risks retained by SPML.

The regulatory and legislative regime surrounding unit-linked life funds offers an environment in which SPML can build fund solutions quickly, and in compliance with the Permitted Links Rules and the Prudent Person Principle under Solvency II. SPML's structure allows the use of existing Schroder funds as building blocks for the launch of new fund propositions, usually without the need for large amounts of seed capital.

The policy contracts (linked policies) written by SPML do not include investment guarantees or insurance benefits. Therefore SPML is not exposed to mortality or morbidity risks. The contracts written include no charge guarantees[1]. While SPML does have permission to provide for the payment of an annuity there is no intention to supply such services, on guaranteed terms or otherwise, nor have there been any historical occurrences.

SPML is indirectly impacted by market risk and lapse risk on linked policies because lower assets under management (AUM) ultimately lead to reduced fee income. However, this impact is limited for SPML as it only retains a small proportion of fee income received, with the majority paid to SIM for the provision of services.

SPML outsources the majority of its functions to SIM, which is also a wholly owned subsidiary of Schroders plc. The outsourcing arrangement is governed by an Investment Management Agreement and a Service Agreement between SPML and SIM. SIM sub-contracts certain activities to third-party companies: JPMorgan for Fund Accounting services and DST for Transfer Agency services. SPML outsources custody and safekeeping services directly to JPMorgan. SPML's Chief Actuary services are provided since 1 January 2018 by BW (formerly WTW). The outsourced operating model significantly reduces SPML's operational risk exposure.

The primary measurement used by SPML for assessing financial risk is the loss or reduction in future profit which would be seen in the financial statements either immediately or over time. In addition, SPML considers the impact of risks on capital requirements and on the continued viability of the business.

Given the simplicity of the business and the risks accepted, SPML does not, in general, set quantifiable tolerances other than maintaining its target level of capital.

SPML products

Any proposals to write new business types or launch products which generate material additional risk or introduce new risks are assessed prior to implementation. This also involves assessing the potential impact on capital resources and capital requirements.

SPML offers a range of unit-linked life funds, covering the main asset classes: Multi-Asset; Equities; and Fixed Income. SPML offers a Defined Benefit (DB) pension scheme liability management product called Flight Path Swift (FPS), which uses a dedicated range of liability-driven investment (LDI) based funds. Derivatives use within the unit-linked life funds is relatively low. However, greater flexibility under Solvency II rules provides opportunities for SPML to explore increased use of derivatives for product development.

SCR risks

SPML's principal sources of risk, on an SCR basis, are: operational risk; market risk; and credit risk. SPML does not have any typical insurance risk, such as mortality risk.

C.1 Underwriting risk

Underwriting risk relates to the adequacy of product pricing for the policyholder benefits provided. SPML's business is purely related to policyholder investment in unit-linked funds. SPML does not underwrite insurance benefits of any kind or give any guarantees to policyholders on investment performance or levels of charges.

[1] Payments or other benefits to which a particular policyholder or investor has an unconditional right that is not subject to the contractual discretion of the issuer.

Therefore, underwriting risk is limited to lapse risk and expense risk, within the Pillar 1 SCR, which is relatively small. The risk of a fall in revenue resulting from lapse risk is managed to a large extent by the terms of the outsourcing arrangements with SIM which have SPML's costs defined as a percentage of fee income.

Other expenses (i.e. those not paid under the outsourcing arrangements) are modest. Such expenses are closely monitored and periodically reviewed.

SPML's solvency position is not particularly sensitive to changes in lapse or expense assumptions. If the best-estimate lapse assumption is doubled or if the best-estimate assumption of expenses not defined as a percentage of fee income is increased by 25%, the reduction in Own Funds is approximately £0.02m and the impact on the SCR is less than £0.01m.

The impact of adverse lapse and expense experience are considered in the ORSA under a number of scenarios. These demonstrate that the Company is able to withstand extreme adverse lapse and/or expense experience whilst continuing to meet regulatory capital requirements and without impacting on its ability to meet policyholder obligations in full.

There have been no material changes to underwriting risk or how it is measured over the reporting period.

C.2 Market risk

Market risk arises from market movements, which can cause a fall in the value of investments.

Linked assets and shareholder assets are considered separately.

Market risk on linked assets results in a reduction in fee income. The impact on SPML of market risk on linked assets is similar to that for lapse risk discussed under section C.1 and is similarly managed by the fee structure of the outsourcing arrangements between SPML and SIM.

The linked assets are managed in accordance with the investment mandate for the particular fund taking into account the prudent person principle requirements under the PRA Investments Rulebook and the permitted links rules included in the FCA Conduct of Business Sourcebook (COBS) 21. In particular, policyholder liabilities are fully matched with units established within the relevant internal linked funds and with assets of the same value. Adherence to the permitted links/prudent person principle requirements involves a combination of pre-trade and post-trade monitoring of investment decisions made by portfolio managers, and compliance with risk parameters established in relation to life funds in accordance with these regulations.

The shareholder assets are used to cover the SCR, the MCR and any technical provisions in excess of the linked assets, and are invested, taking into account the prudent person principle, to preserve capital.

Market risk on shareholder assets is limited to investments held within the Schroder Special Situations Fund – Sterling Liquidity Plus Fund (£15.4 million investment at 31 December 2017). This fund invests in a range of cash instruments, short term credit and government bonds and, as such, market risk is limited.

Any fall in the value of shareholder assets due to market risk will directly impact the level of Own Funds and consequently is expected to lead to a reduction in the market risk SCR (as the SCR stresses are applied to lower values).

All other shareholder assets are considered under credit risk below.

The Company investigates the potential impact of market risks on its income and solvency position by way of stress and scenario tests that are carried out as part of the ORSA process. These demonstrate that the Company is able to withstand extreme market falls whilst continuing to meet regulatory capital requirements and without impacting on its ability to meet policyholder obligations in full, but recognising that policyholder obligations will reflect the impact of market risks on linked assets.

There have been no material changes to market risk or how it is measured over the reporting period.

C.3 Credit risk

Credit risk means the risk of loss or of adverse change in the financial situation, resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors to which SPML is exposed, in the form of counterparty default risk, spread risk, or market risk concentrations.

Linked-assets, and non-linked shareholder assets and debtors are considered separately.

Credit risk accepted on linked assets depends upon the investment objectives and mandate of each unit-linked fund and is managed under the Group Agency Credit Risk Framework. Credit risk/asset defaults on linked assets results in a reduction in fee income. The impact on SPML of credit risk on linked assets is similar to that for lapse risk discussed under section C.1 and the impact of the risk on SPML is similarly managed by the fee structure of the outsourcing arrangements between SPML and SIM.

SPML has a low tolerance to credit risk in relation to shareholder assets. The risk is managed by limiting direct exposure to cash (bank) counterparties and investing other assets in a diversified portfolio of high quality short-term assets through the Schroder Special Situations Fund – Sterling Liquidity Plus Fund.

SPML aims to hold cash with creditworthy counterparties, in line with the SPML Capital Policy and Group Counterparty and Credit Risk Framework. Bank accounts are reconciled daily and transfers of funds are subject to approval and monitoring controls employed by the Group Treasury team. The Group Credit Risk team monitors credit limits with counterparties at Group level and these are reviewed in response to changes in business requirements, credit ratings and market events.

At 31 December 2017, SPML held non-linked cash (or cash equivalent) assets at Citibank NA, JPMorgan Chase Bank NA and National Westminster bank plc (NatWest). SPML also has a loan to Schroders plc, the terms of which are considered cash equivalent. SPML is therefore exposed to the risk of these counterparties defaulting.

The loan to Schroders plc (£21.5m) is considered a material risk concentration and can be recalled immediately at any time. Exposures to other bank counterparties may be material from time to time.

Any credit default on shareholder assets will directly impact the level of Own Funds and consequently is expected to lead to a reduction in the market risk and/or counterparty default risk SCR (as the SCR stresses are applied to lower values). SPML's capital position is also affected by changes to the credit rating of counterparties. If the Solvency II credit quality step for Schroders plc is reduced by 1, SPML's SCR will increase by £1.4m.

SPML's debtors are primarily service providers and policyholders. SPML currently has no reinsurance ceding agreements (outward reinsurance) in place.

The risk of a service provider defaulting on its obligations is primarily managed by initial and on-going due diligence of the service provider together with protections included in service contract terms. The terms of the agreements between SPML and SIM are such that SIM will make good any loss if a sub-contractor is unable or unwilling to meet its financial obligations towards the Company.

The terms of SPML policies allow SPML to recover losses from policyholders in the event of the policyholder failing to meet its obligations.

The Company investigates the potential impact of credit risks on its income and solvency position by way of stress and scenario tests that are carried out as part of the ORSA process. These demonstrate that the Company is able to withstand extreme credit events whilst continuing to meet regulatory capital requirements and without impacting on its ability to meet policyholder obligations in full, but recognising that policyholder obligations will reflect the impact of credit risks on linked assets.

There have been no material changes to credit risk or how it is measured over the reporting period.

C.4 Liquidity risk

Liquidity risk is the risk that the SPML cannot meet its contractual or payment obligations in a timely manner.

Linked-assets and non-linked shareholder assets are considered separately.

SPML's linked-assets are managed in accordance with the permitted links rules/prudent person principle for insurance companies under Solvency II.

Liquidity management is delegated to SIM as part of the investment process. SIM manages liquidity risk within appetite through the liquidity risk monitoring framework for its funds. The framework ensures that liquidity risk of funds (including the SPML funds) is identified, assessed and monitored on an on-going basis. This includes liquidity stress test scenarios which consist of a combination of unfavourable market liquidity conditions and large capital outflows. This helps ensure fund liquidity remains in line with the respective investment policy and overall risk profile. In contingency situations, the SPML Policy Rules allow the use of the following techniques:

- Market conditions or external factors allow SPML to delay surrender of units or payment of proceeds by 30 days (180 days for real estate funds);
- The scale of fund redemption that may have an adverse impact on policyholders, whereby SPML can cancel orders and transfer assets to a new fund for orderly realisation;
- Large deals (£5 million or 10% of the fund NAV, whichever is the lower) can be rejected or if accepted, deferred to the next business day; and
- Deferral of cancellation proceeds up to 30 business days in the event of exchange control, regulations or similar constraints or in exceptional circumstances where the liquidity of a fund is not sufficient to meet the cancellation requests.

SPML only invests shareholder assets in instruments which have been approved by the Group Capital Committee under the Group's Liquidity Management Policy. Where the Group Capital Committee makes changes to the instruments approved under the Group's Liquidity Management Policy, the Board of SPML considers the changes.

SPML has minimum target liquidity positions for shareholder assets which are monitored by Group Treasury. Under periods of stress SPML would also have access to the Group's liquidity resources. SPML is also covered by the Group's Liquidity Management Policy (LMP) and Liquidity Contingency Plan (LCP). The LMP policy sets out the minimum standards which must be followed when managing the Group's liquidity resources. The LCP sets out the plan for the management of liquidity, either where a potential event is expected or an actual event has occurred and which could cause a strain on the Group's liquidity resources.

Shareholder assets are largely held in cash or in investments, including a loan to Schroders plc, that can be recalled within one day without adversely affecting values. The investments take into account the prudent person principle.

Under the SPML and SIM Investment Management Agreement, SIM is liable for any operational losses to SPML as a result of negligence, wilful default or fraud. Scenarios which could give rise to an SPML/SIM operational loss liquidity requirement are included in the Consolidated Group Internal Liquidity Adequacy Assessment Process (ILAAP) and therefore SPML's potential liquidity requirement for operational risk events is provided for within the Consolidated Group ILAAP.

There have been no material changes to liquidity risk or how it is measured over the reporting period.

Given the nature of the business written by SPML, the expected profit in future premiums calculated in accordance with Article 260(2) of the Delegated Regulation is zero.

C.5 Operational risk

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

SPML's outsourced operating model significantly reduces its exposure to operational risk which, subject to any specific terms and conditions, is transferred to its suppliers through contractual arrangements.

Although operational risk is successfully transferred to the Company's outsourced service providers, this mitigation is not allowed for in the operational risk SCR for companies such as SPML using the standard formula. The operational risk SCR for the business written by SPML is calculated as 25% of non-acquisition expenses incurred over the last 12 months.

Operational risk from external events, including significant events arising from SPML's third party service providers, is primarily managed by ensuring compliance with current regulation and legislation, and by maintaining the ability to react appropriately to external risks and issues. As part of its ORSA process, the Company considers the impact of external influences on its business model and considers the management actions that might be taken to address any issues.

There have been no material changes to operational risk or how it is measured over the reporting period.

C.6 Other material risks

Strategic risk

The risk of Schroders' strategy failing to deliver the expected outcomes, earnings and profitability can be influenced by internal and external factors.

SPML's risk profile is based on its business strategy to pursue one single line of business, which is the provision of unit-linked funds to UK registered pension schemes and authorised insurance companies. Threats to this business strategy may come from changes in tax or pension legislation, downward pricing pressure on Defined Contribution (DC) funds and poor fund performance.

Future risks with uncertain impact, probability and timeframe could have an impact on SPML. The estimated likelihood and timing of future risks may also change over time.

SPML may mitigate these threats by:

- Using membership of industry bodies to influence regulation;
- Leveraging the Group's product innovation in its DC offering to take advantage of the switch of assets out of DB schemes; and
- Apply more rigorous oversight of its funds if there are concerns with performance.

The Schroders group operates a diversified business by geography, asset class and distribution channel. Schroders has a preference for a diversified product set which reduces its dependence on the performance of any one fund or asset class.

Reputational risk

The reputation of SPML and Schroders can be impacted by any of the key risks. Reputational risk may impact Schroders' brands, reliability, and relationships with clients, regulators and shareholders. This may arise from poor conduct or judgments or risk events due to weaknesses in systems/controls.

In addition, ineffective branding and marketing may impact Schroders' ability to grow the business. Reputational risk may also arise from inappropriate client relationships or mandates which have adverse implications for the Group.

Risk events arising from SPML's third party service providers can damage confidence in SPML, leading to falls in AUM via unexpected net outflows from policyholders which may eventually result in operating losses. Being inextricably linked to the Schroders Group, SPML is exposed to reputational risk arising from the Group's other entities. This could arise through a major risk event, operational loss or regulatory fine.

Schroders actively monitors and manages outcomes of other risks that could drive reputational risk. Management information covering errors, omissions and risk events is reported to the SRC and SPML Board to help consider reputational impact to SPML and the Group.

Risk mitigation techniques

SPML has not purchased or entered into any risk mitigation contracts or arrangements during the reporting period.

Reinsurance

SPML has no recoverables from reinsurance contracts and has transferred no risks to special purpose vehicles.

Off balance sheet positions

SPML does not hold any off-balance sheet positions.

Future management actions

SPML assumes no future management actions in calculating its Solvency Capital Requirement.

C.7 Any other information

There is no other material information regarding the risk profile of the Company.

Section D Valuation for solvency purposes

The below sets out the Company's approach to valuing its assets and liabilities for solvency purposes.

In general, the valuation method is aligned with IFRS and so the basis of preparation aligns with the accounting policies outlined in the notes to Company's financial statements. A brief description of the valuation basis and any differences to these methods are outlined in the relevant sections below.

SPML has two lines of business, unit-linked insurance business written as direct contracts and unit-linked reinsurance accepted on similar terms. All business is pensions business. A summarised balance sheet as at 31 December 2017 is provided below.

As at 31 December 2017 (£'000)	Reference to QRT S.02.01.02	Financial Statements £'000	Solvency II value £'000	SFCR Reference
Assets				
Deferred tax assets	R0040	–	–	D1.1
Collective Investments Undertakings	R0180	15,368	15,368	D1.2
Assets held for index-linked and unit-linked contracts	R0220	10,318,337	10,318,337	D1.3
Insurance and intermediaries receivable	R0360	30,901	1,050	D1.4
Receivables (trade, not insurance)	R0380	56,069	56,069	D1.5
Cash and cash equivalents	R0410	198,151	198,151	D1.6
Any other assets, not shown elsewhere	R0420	–	29,851	D1.4
Total assets	**R0500**	**10,618,826**	**10,618,826**	
Liabilities				
Technical provisions calculated as a whole	R0700	10,518,245	10,518,245	D2.1
Best estimate	R0710	–	(428)	D2.2
Risk margin	R0720	–	651	D2.3
Technical provisions – unit-linked	**R0690**	**10,518,245**	**10,518,468**	
Deferred tax liabilities	R0780	20	20	D3.4
Derivatives	R0790	2,643	2,643	D3.3
Insurance and intermediaries payables	R0820	44,153	–	D3.1
Payables (trade, not insurance)	R0840	13,539	13,539	D3.2
Any other liabilities, not shown elsewhere	R0880	–	44,153	D3.1
Total Liabilities	**R0900**	**10,578,600**	**10,578,823**	
Excess of assets over liabilities	**R1000**	**40,226**	**40,003**	

D.1 Assets

The valuation methodology of each type of asset within the regulatory balance sheet shown above has been provided below. There has been no change to the recognition and valuation bases used or to estimate during the reporting period. All assumptions and judgements are detailed within the relevant sections below.

D1.1 Deferred tax

The deferred tax balances are measured on the same basis as those used for IFRS (IAS 12 'Income Taxes') as set out in the notes to the Company's financial statements. Differences in the deferred tax balances can arise where balance sheet items are recognised on a different basis for Solvency II. At 31 December 2016 a deferred tax asset was recognised on the difference between the Solvency II technical provisions and the financial liabilities for investment contracts reported in the financial statements. At 31 December 2017, no similar deferred tax asset was recognised.

D1.2 Collective Investment Undertakings (CIU's)

Investments in CIU's are measured at fair value.

D1.3 Assets held for index-linked and unit-linked contracts

SPML issues unit-linked investment contracts without fixed terms whose fair value is dependent on the fair value of the underlying financial assets and derivatives.

Each instrument has been categorised using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. These levels are based on the degree to which the fair value is observable and are defined as follows:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities and principally comprise investments in quoted equities, daily priced funds, gilts and exchange-traded derivatives; and
- Level 2 fair value measurements are those derived from prices that are not traded in an active market but are determined using valuation techniques, which make maximum use of observable market data included within Level 1 for the asset or liability and principally comprise corporate bonds and foreign exchange contracts. Valuation techniques may include using a broker quote in an inactive market, an evaluated price based on a compilation of primarily observable market information or industry standard calculations, utilising vendor fed data and information readily available via external sources. For funds not priced on a daily basis, e.g. real estate funds, the net asset value which is issued monthly or quarterly is used
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data and principally comprise investments in private equity funds. These are measured by applying appropriate valuation techniques in accordance with International Private Equity and Venture Capital Guidelines. The valuation review is a continual process throughout the year

Further information on valuation is set out in note 8 of the Company's financial statements.

D1.4 Insurance receivables and any other assets, not shown elsewhere

There is no observable market for receivables or similar assets that can be used to fair value the assets. It is considered that the present value of the expected cash-flows, allowing for anticipated bad debts, is materially the same as measuring the receivables at amortised cost using the effective interest rate method, less any impairment. As a result, there is no difference between IFRS and Solvency II measurement. However, on a Solvency II basis only amounts past-due are presented as insurance and intermediaries receivable. Current amounts of insurance receivables are presented in any other assets, not shown elsewhere.

D1.5 Trade receivables

As with Insurance receivables above, Trade receivables are measured at amortised cost using the effective interest rate method, less any impairment.

D1.6 Cash and cash equivalents

These are cash at bank and are held at amortised cost. The book value of such assets approximates their fair value.

D.2 Technical provisions

Technical provisions have been determined as the sum of the value of units (shown as technical provisions as a whole in the above table), best estimate liabilities and risk margin.

D2.1 Technical provisions as a whole

This is the value of units allocated to in-force investment contracts at the valuation date, as disclosed in the financial statements as investment contracts.

D2.2 Best estimate

A deterministic cash-flow projection method is used to calculate the best estimate of the excess of policy charges over expenses, hereafter referred to as the present value of future profits (PVFP).

The PVFP is determined over a projection period of three months, reflecting the Company's ability to terminate all contracts subject to a notice period of three months. This approach is proportionate and compliant with Article 56 of Commission Delegated Regulation (EU) 2015/35 (the 'Delegated Regulation') and appropriately estimates the risks associated with the business, resulting in technical provisions that are higher than would be determined under a long-term projection.

The projection estimates the policy charges and expense cash-flows that the Company expects to receive and incur respectively in each month of the three month projection period, based on the business in force at the valuation date and using a single set of best estimate projection assumptions. The net cash-flow in each month is then discounted to the valuation date to give a present value.

The policy charges cash-flows are annual management charges which are either deducted directly from unit-linked funds, or otherwise invoiced directly to policyholders.

The expense cash-flows fall into two categories:

- Expenses that are contractually defined as a percentage of annual management charges received (and which can never exceed annual management charges received); and
- Other expenses, or "direct expenses", that are fixed or variable monetary amounts.

Economic assumptions are based on market data at the valuation date. The rate of withdrawal of AUM is based on actual experience over a five year period up to the valuation date. Expenses, other than those which are contractually defined, are based on the Company's budgeted expenses from its business plan. The average rate of fee income received is in line with the assumption in the SPML business plan.

There is no obligation for policyholders to pay additional premiums other than, for some policies, where charges are invoiced and paid by way of premiums. The technical provisions therefore include no allowance for additional premiums other than such charges.

The contracts written by the Company contain no financial options, other than surrender, or guarantees, other than charge guarantees, for a period of not more than three months. The surrender option means that the PFVP is reported under "Contracts with options and guarantees" on quantitative reporting template S.12.01.02 in accordance with a question and answer issued by the European Insurance and Occupational Pensions Authority (EIOPA).

An aggregate approach across all business is used to calculate the PVFP to the end of the three month period, that is, cash-flows are projected for the business as a whole, not at an individual policy level. This approach implicitly assumes that the direct expenses are apportioned over individual policies on a pro rata basis based

on the monetary amount of annual management charge each policy is expected to generate net of the expenses that are contractually defined as a percentage of the annual management charge. The aggregate approach is considered appropriate given the homogeneous nature of the contracts written and the low materiality of the PVFP. The aggregate calculation involves a number of simplifications, none of which are considered material over the projection term due to the short projection period and the dynamics of the calculation. The simplifications are:

– Unit growth on all linked-assets (both UK and overseas) is taken as the UK basic risk-free yield curve. The use of currency or country specific growth rates would not lead to a materially different result;

– Unit funds are projected net of the average rate of annual management charge. In practice, a proportion of policyholders are invested in zero annual management charge funds and pay annual management charges on an invoiced basis. The projection will therefore slightly understate the value of units and hence understate charges deducted from funds. The extent of the understatement is not material; and

– The use of an average annual management charge rate and an aggregate withdrawal rate implicitly assumes that the mix of unit-linked investments remains constant over the projection period. Calculations at a more granular level would not lead to a materially different result.

D2.3 Risk margin

Given all business has a three month projection period, the risk margin has been determined over a one year period (the minimum permitted under Solvency II regulations), and has been calculated on the result of the SCR at the valuation date but with the result of the market risk module and counterparty default risk module for bank counterparties set to equal zero on the assumption that these risks could be hedged if required.

The risk margin has been apportioned across the two lines of business in proportion to the respective unit liabilities. This is considered a proportionate and appropriate approach as the amount of unit liabilities is a reasonable proxy for the risk associated with each line of business and the impact of using a different apportionment method would not be material to the overall technical provisions by line of business.

D2.4 Summary of technical provisions

Technical provisions – Direct unit-linked insurance business

Technical Provision Item	31 December 2017 £'000s	31 December 2016 £'000s
Technical provisions as a whole	7,112,719	7,273,062
PVFP	(289)	(286)
Risk margin	440	487
Total technical provisions	**7,112,870**	**7,273,263**

Technical provisions – Unit-linked reinsurance accepted business

Technical Provision Item	31 December 2017 £'000s	31 December 2016 £'000s
Technical provision as a whole	3,405,526	2,913,170
PVFP	(139)	(115)
Risk margin	211	196
Total technical provisions	**3,405,598**	**2,913,251**

D2.5 Assumptions

Given the similarities between the two lines of business written, the same assumptions are used for both lines. The assumptions used at the valuation date, (and at the previous valuation date if different) are:

- Starting unit prices: 100% of the unit prices at the valuation date;
- Unit growth before management charges and investment expenses: UK basic risk-free yield curve as provided by EIOPA;
- Annual management charges: Average rate, net of rebates, at the valuation date;
- Withdrawals: 20% per annum (2016: 18% per annum);
- Amounts payable under transfer pricing arrangements in force at the valuation date, expressed as an average percentage of fee income based on the AUM at the valuation date, 96% of fee income;
- Direct expenses of £34k per month (2016: £48k);
- Projection period: three months;
- Expense inflation: 3% per annum;
- Discount rate: UK basic risk-free yield curve as provided by EIOPA;
- The reduction in the direct expense assumption primarily reflects an expectation of reduced regulatory compliance costs now that Solvency II requirements are embedded in the business.

D2.6 Policyholder behaviour

The contracts written by the Company contain no financial options, other than surrenders, or guarantees, other than charge guarantees, for a period of not more than three months and relevant policyholder behaviour is limited to:

- The payment of additional premiums for investment;
- Switching investments between the different internal unit-linked funds maintained by the Company; and
- Partial and full withdrawals.

Given that there is no obligation to pay additional premiums for investment, the calculation of technical provisions assumes that no further premiums are payable. In reality, additional premiums are expected to be received on some policies, particularly those written as inward reinsurance. In the year to the valuation date of 31 December 2017, £2,248 million of additional investment premiums was received.

Switching investments between the different internal unit-linked funds maintained by the Company is permitted. Such switching activity is usually associated with policyholders' periodic review of investments and will take into account information that is unknown to the Company. Switching activity is therefore difficult to predict.

D2.7 Management actions

The technical provisions assume no future management actions.

D2.8 Judgements associated with the value of technical provisions

All business written by the Company is unit-linked pensions business and the contracts contain no financial options, other than surrender, or financial guarantees. The policyholder unit liabilities are matched by holding the assets upon which the unit liabilities are determined.

The Company has the unilateral right to terminate contracts subject to three months' notice. This is a typical policy clause for the type of business written by the Company which is sold only to institutional investors.

The expense agreements in place between SPML and other companies within the Group are such that SPML retains a modest percentage of fee income. The fee income retained is sufficient to cover expenses incurred directly by the Company in the normal course of business.

The technical provisions for solvency purposes have been calculated on a simplified basis under which a three month projection period is applied. Cash-flows relating to the insurance contracts written by the Company are included in the calculation of the best estimate liabilities and associated risk margin, up until the point at which the Company has the unilateral right to terminate the contract.

If a simplified method had not been applied, cash-flows in respect of the in-force business would be assumed to continue over a longer period, allowing for best-estimate rates of surrender irrespective of the Company's ability to terminate the contracts. This approach would result in a reduction of the Company's best estimate liabilities. The reduction to the best estimate liabilities would be partly offset by an increased risk margin and the Company's Solvency Capital Requirement would also increase. The overall effect of this would not be material to the Company's capital position.

The calculation of the Company's technical provisions on a simplified basis is considered to be an appropriate method on the basis that it is proportionate to the nature, scale and complexity of the risks underlying the Company's insurance and reinsurance obligations. The PRA has also confirmed that this is an acceptable approach in accordance with requirements of article 56 of the Delegated Regulation.

The data used to calculate the technical provisions is considered of appropriate quality with no material deficiencies.

D2.9 Reconciliation with the financial statements

All contracts written by the Company are treated as investment contracts under the accounting rules applicable to the Company, being IFRS. The accounting treatment for such contracts is to value the contracts at "fair value", essentially the market value of the assets within the unit-linked funds, and no less than the amount that would be payable upon immediate surrender. The technical provisions reported in the Company's external financial statements are therefore taken as the policyholder liabilities of £10,518.2 million (the total of the unit-linked liabilities shown in the Technical Provisions tables above). The technical provisions for solvency purposes are £0.2 million higher than the technical provisions reported in the financial statements, reflecting the PVFP and the risk margin.

D2.10 Reinsurance

The Company has no recoverable assets from reinsurance contracts and has transferred no risks to special purpose vehicles.

D2.11 Adjustments and transitional arrangements

The Company does not use the matching adjustment or volatility adjustment.

The Company is not making use of any Solvency II transitional measures.

D2.12 Other considerations

The Company has:

- No contracts that have been unbundled; and
- Not used an economic scenario generator.

D.3 Other liabilities

There is no material additional information to report, other than as reported in this document. No alternative methods of valuation have been used and no financial statements values have been used that are not Solvency II compliant.

D3.1 Insurance payables and any other liabilities, not shown elsewhere

Insurance payables are recorded initially at fair value and subsequently at amortised cost. As noted in D1.4 Insurance receivables, there is no observable market for payables and the value of discounting is expected to be immaterial. As a result, there is no difference between IFRS and Solvency II values. However, on a Solvency II basis, only amounts considered past-due are presented as insurance payables. Current amounts of insurance payables are presented in any other liabilities, not shown elsewhere.

D3.2 Trade payables

These liabilities are valued as per D3.1 above.

D3.3 Derivatives

Derivatives are measured at fair value as at the valuation date.

D3.4 Deferred tax liability

The deferred tax liability has been calculated as set out in note 10 of the Company's financial statements.

D.4 Alternative methods for valuation

Assets backing unit linked liabilities are measured at fair value in accordance with IFRS. See section D1.3. for valuation methods used.

D.5 Any other information

There is no material additional information to report.

Section E Capital management

E.1 Own funds

The Company may distribute by way of dividend:

- The full amount of distributable profits disclosed in the audited accounts each year, or
- Other amount as agreed provided that, following such payment the Company will continue to hold a level of cover, as deemed appropriate by the Board, above the appropriate regulatory requirement applicable to the Company, or such other amount as may be agreed and having regard to the Company's business plan

The Board may cancel, amend or withhold dividends at any time prior to payment if such cancellation or amendment is necessary for the Company to meet regulatory requirements or its internal targets.

There have been no material changes to the capital management policy over the reporting period. Any change in the capital management policy will be approved by the Board.

It is the Board's intention that the Company will maintain own funds of no less than the higher of 200% of the Company's Pillar 1 SCR and the capital requirement calculated under the ORSA. The Board actively monitors this position on a regular basis, taking into consideration the time horizon used for the Company's business planning. This target has been set in order that the Company is able to demonstrate adequate financial strength but is not intended to represent any particular risk appetite.

The Company performs financial projections under central and adverse scenarios to assess the capital required over its five-year business planning period.

As at 31 December 2017, Own Funds were £40.0 million (31 December 2016: £38.4 million) of which £26.5 million (31 December 2016: £26.5 million) was permanent share capital and £13.5 million (31 December 2016: £11.9 million) retained profit and loss and other reserves. There was an increase in Own Funds over the reporting period of £1.6 million predominantly due to profits after tax and other comprehensive income earned. Surplus own funds are loaned to Schroders plc or are invested in the SSSF SLP.

All of the Company's Own Funds are classified as Tier 1 basic own funds comprised of equity and retained earnings and are available to provide cover for both the Solvency Capital Requirement (SCR) and the Minimum Capital Requirement (MCR) without restriction. As at 31 December 2016, a deferred tax asset was classified as Tier 3 Capital in Own Funds, however as discussed in Section D1.1, there are no deferred tax assets as at 31 December 2017, therefore all Own Funds are now classified as Tier 1. The Company's Own Funds are materially free of any liens and encumbrances.

The Solvency ratio of the Company, i.e. Own Funds divided by the SCR, at 31 December 2017 was 395% (31 December 2016: 384%) and a summary of the actual position as at 31 December is shown below:

	31 Dec 2017 £m	31 Dec 2016 £m
Ordinary share capital	26.5	26.5
Reconciliation reserve	13.5	11.9
Total capital resources (all Eligible Own Funds)	**40.0**	**38.4**
SCR	10.1	10.0
Capital surplus	29.9	28.4
SCR cover	395%	384%
MCR	4.6	4.5
MCR cover	877%	853%

The reconciliation reserve comprises retained profits and the difference between the technical provisions for solvency purposes and the technical provisions reported in the financial statements.

As illustrated in section D, there are no material differences to the Company's excess of assets over liabilities on an IFRS basis versus a Solvency II basis. The difference arises solely from the combined impact of the PVFP and the risk margin that is not recognised in the financial statements but is reflected in the reconciliation reserve.

No Own-Funds items are subject to the transitional arrangements referred to in Article 308b (9) and (10) of the Solvency II Directive. The Company has no ancillary own funds.

E.2 Solvency capital Requirement (SCR) and Minimum Capital Requirement (MCR)

SPML uses the standard formula to calculate the SCR. SPML does not use undertaking specific parameters and does not apply a matching adjustment.

The Company has not applied any of the simplifications outlined in Articles 88 to 112 of the Delegated Regulation. SPML is taking a proportionate, simplified and prudent approach in calculating the SCR for market risk in that all unit-linked assets are assumed to be invested in "Type 2" equities as defined in Article 168 of the Commission Delegated Regulation (EU) 2015/35.

The standard formula SCR calculation for SPML is dominated by the SCR in relation to operational risk which, for the business written by SPML, is a function of expenses.

The next most significant contribution to the SCR is that in relation to counterparty default risk, which is determined on non-linked assets only. SPML transfers counterparty default risk on unit-linked assets to policyholders under the terms of it policy contract and has therefore interpreted Articles 189 to 215 of the Commission Delegated Regulation (EU) 2015/35 as there being no requirement to hold counterparty default risk capital in respect of assets held within its unit-linked funds.

The SCR and MCR at 31 December 2017 is shown in the table below:

	31 Dec 17 £m	31 Dec 16 £m
Assets	**10,618.8**	**10,275.6**
Less technical provisions		
Technical provisions as a whole	10,518.2	10,186.2
PVFP	(0.4)	(0.4)
Risk margin	0.7	0.7
Total technical provisions	**(10,518.5)**	**(10,186.5)**
Less liabilities	(60.4)	(50.7)
Own funds	**40.0**	**38.4**
SCR		
Operational risk	10.7	9.7
Market risk	0.5	0.5
Life underwriting risk	0.2	0.4
Counterparty default risk	1.6	1.6
Diversification across risk modules	(0.4)	(0.5)
Tax adjustment	(2.4)	(1.7)
Total SCR	**10.1**	**10.0**
Capital surplus	**29.9**	**28.4**
SCR coverage ratio	**395%**	**384%**
MCR	**4.6**	**4.5**

The SCR has increased by £0.1 million to £10.1 million at 31 December 2017 (2016: £10.0 million). This increase is primarily due to an increase in the operational risk component of the SCR, which increased the impact on the SCR of £1.0 million, offset by an increase in the tax adjustment. The tax adjustment, which reflects a revised methodology, had the impact of reducing the SCR by £0.8 million.

The Company is not required to use any undertaking specific parameters in accordance with Article 110 of the Solvency II Directive. No capital add-on has been applied to the SCR and the Company has not made use of the option provided for in the third subparagraph of Article 51(2) of the Solvency II Directive.

The MCR calculation is set out in the Delegated Regulation. Given the nature of the Company's business, the required inputs to the calculation that are not defined under the regulations are limited to:

- The technical provisions excluding the risk margin for unit-linked life insurance and reinsurance obligations of £10,517.8 million (£10,185.8 million in 2016)
- The amount of capital at risk. Given payments made under the contracts issued by the Company are not directly contingent on death, the capital at risk is taken to be zero

E.3 Use of the duration-based equity risk sub-module in the calculation of the SCR

SPML is not using the duration-based equity risk sub-module option set out in Article 304 of Directive 2009/138/EC.

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

SPML is not using an internal model.

E.5 Non-compliance with the MCR and non-compliance with the SCR

SPML currently complies, and expects to fully comply over the business planning time period, with both the MCR and SCR.

E.6 Any other information

There is no other material information regarding the capital management of the Company.

Section F Governance

F.1 Directors' confirmation

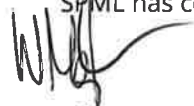
Approval by the Board of Directors of the Solvency and Financial Condition Report and Reporting Templates

We certify that:

- The Solvency and Financial Condition Report has been properly prepared in all material respects in accordance with the PRA rules and Solvency II regulations.

We are satisfied that:

- Throughout the financial year ended 31 December 2017, SPML has complied in all material respects with the requirements of the PRA rules and Solvency II Regulations as applicable to SPML.
- It is reasonable to believe, at the date of publication of the Solvency and Financial Condition Report, that SPML has continued to comply, and will continue to comply in future.



SPML Board of Directors
27 April 2018

F.2 Independent Auditor's report

Report of the external independent auditors to the Directors of Schroder Pension Management Limited ('the Company') pursuant to Rule 4.1 (2) of the External Audit Part of the PRA Rulebook applicable to Solvency II firms

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

Opinion

Except as stated below, we have audited the following documents prepared by the Company as at 31 December 2017:

– The 'Valuation for solvency purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Company as at 31 December 2017, ('**the Narrative Disclosures subject to audit**'); and

– Company templates S.02.01.02, S.12.01.02, S.23.01.01, S.25.01.21 and S.28.01.01 ('**the Templates subject to audit'**)

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

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

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

– Company templates S.05.01.02

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

In our opinion, the information subject to audit in the relevant elements of the Solvency and Financial Condition Report of the Company as at 31 December 2017 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based.

Basis for opinion

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

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

– The Directors' use of the going concern basis of accounting in the preparation of the Solvency and Financial Condition Report is not appropriate; or

– The Directors have not disclosed in the Solvency and Financial Condition Report any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the Solvency and Financial Condition Report is authorised for issue

Emphasis of matter – Basis of accounting

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

Other information

The Directors are responsible for the Other Information.

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

In connection with our audit of the Solvency and Financial Condition Report, our responsibility is to read the Other Information and, in doing so, consider whether the Other Information is materially inconsistent with the relevant elements of the Solvency and Financial Condition Report, or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the relevant elements of the Solvency and Financial Condition Report or a material misstatement of the Other Information. If, based on the work we have performed, we conclude that there is a material misstatement of this Other Information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Directors for the Solvency and Financial Condition Report

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

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

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

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

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

A further description of our responsibilities for the audit is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

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

Report on Other Legal and Regulatory Requirements

In accordance with Rule 4.1 (3) of the External Audit Part of the PRA Rulebook for Solvency II firms we are also required to consider whether the Other Information is materially inconsistent with our knowledge obtained in the audit of the Company's statutory financial statements. If, based on the work we have performed, we

conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants
London
27 April 2018

Appendix 1 Annual QRT's as at 31 December 2017

S.02.01.02 – Balance Sheet (Template subject to audit)

	Assets	Solvency II value
		C0010
R0010	Goodwill	–
R0020	Deferred acquisition costs	–
R0030	Intangible assets	–
R0040	Deferred tax assets	–
R0050	Pension benefit surplus	–
R0060	Property, plant and equipment held for own use	–
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	15,368
R0080	Property (other than for own use)	–
R0090	Participations and takings	–
R0100	Equities	–
R0110	Equities – listed	–
R0120	Equities – unlisted	–
R0130	Bonds	–
R0140	Government bonds	–
R0150	Corporate bonds	–
R0180	Collective investment undertakings	15,368
R0190	Derivatives	–
R0200	Deposits other than cash equivalents	–
R0210	Other investments	–
R0220	Assets held for index-linked and unit-linked contracts	10,318,337
R0230	Loans and mortgages	–
R0240	Loans on policies	–
R0250	Loans and mortgages to individuals	–
R0260	Other loans and mortgages	–
R0270	Reinsurance recoverables from:	–
R0280	Non-life and health similar to non-life	–
R0290	Non-life excluding health	–
R0300	Health similar to non-life	–
R0310	Life and health similar to life, excluding index-linked and unit-linked	–
R0320	Health similar to life	–
R0330	Life excluding health and index-linked and unit-linked	–
R0340	Life index-linked and unit-linked	–
R0350	Deposits to cedants	–
R0360	Insurance and intermediaries receivables	1,050
R0370	Reinsurance receivables	–
R0380	Receivables (trade, not insurance)	56,069
R0390	Own shares	–
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	–
R0410	Cash and cash equivalents	198,151
R0420	Any other assets, not elsewhere shown	29,851
R0500	**Total assets**	**10,618,826**

S.02.01.02 – Balance sheet – Liabilities

	Liabilities	Solvency II value
		C0010
R0510	Technical provisions – non-life	–
R0520	Technical provisions – non-life (excluding health)	–
R0530	TP calculated as a whole	–
R0540	Best estimate	–
R0550	Risk margin	–
R0560	Technical provisions – health (similar to non-life)	–
R0570	TP calculated as a whole	–
R0580	Best estimate	–
R0590	Risk margin	–
R0600	Technical provisions – life (excluding index-linked and unit-linked)	–
R0610	Technical provisions – health (similar to life)	–
R0620	TP calculated as a whole	–
R0630	Best estimate	–
R0640	Risk margin	–
R0650	Technical provisions – life (excluding health and index-linked and unit-linked)	–
R0660	TP calculated as a whole	–
R0670	Best estimate	–
R0680	Risk margin	–
R0690	Technical provisions – index-linked and unit-linked	10,518,468
R0700	TP calculated as a whole	10,518,245
R0710	Best estimate	(428)
R0720	Risk margin	651
R0730	Other technical provisions	–
R0740	Contingent liabilities	–
R0750	Provisions other than technical provisions	–
R0760	Pension benefit obligations	–
R0770	Deposits from reinsurers	–
R0780	Deferred tax liabilities	20
R0790	Derivatives	2,643
R0800	Debts owed to credit institutions	–
R0810	Financial liabilities other than debts owed to credit institutions	–
R0820	Insurance and intermediaries payables	–
R0830	Reinsurance payables	–
R0840	Payables (trade, not insurance)	13,539
R0850	Subordinated liabilities	–
R0880	Any other liabilities, not elsewhere shown	44,153
R0900	**Total liabilities**	**10,578,823**

R1000	**Excess of assets over liabilities**	**40,003**

S.05.01.02 – Premiums, claims and expenses by line of business

	Life	Line of business for: life obligations			Life reinsurance obligations		Total
		Health insurance	Insurance with profit participation	Index-linked and unit-linked insurance	Health reinsurance	Life reinsurance	
		C0210	C0220	C0230	C0270	C0280	C0300
	Premiums written						
R1410	Gross	–	–	1,109,167	–	1,138,640	2,247,807
R1420	Reinsurers' share	–	–	–	–	–	–
R1500	Net	–	–	1,109,167	–	1,138,640	2,247,807
	Premiums earned	–	–		–		
R1510	Gross	–	–	1,109,167	–	1,138,640	2,247,807
R1520	Reinsurers' share	–	–	–	–	–	–
R1600	Net	–	–	1,109,167	–	1,138,640	2,247,807
	Claims incurred	–	–		–		
R1610	Gross	–	–	1,919,721	–	944,278	2,863,999
R1620	Reinsurers' share	–	–	–	–	–	–
R1700	Net	–	–	1,919,721	–	944,278	2,863,999
	Changes in other technical provisions						
R1710	Gross	–	–	–	–	–	–
R1720	Reinsurers' share	–	–	–	–	–	–
R1800	Net	–	–	–	–	–	–
		–	–		–		
R1900	**Expenses incurred**	–	–	36,033	–	17,252	53,285
R2500	**Other expenses**						–
R2600	Total expenses	–	–				–
							–
							–

S.12.01.02 – Life and Health SLT Technical Provisions (Template subject to audit)

		Index-linked and unit-linked insurance			Accepted reinsurance		
			Contracts without options and guarantees	Contracts with options and guarantees	Accepted reinsurance	Total (Life other than health insurance, incl Unit-linked)	Total (Health similar to life insurance)
		C0030	C0040	C0050	C0100	C0150	C0210
R0010	**Technical provisions calculated as a whole**	7,112,719	–	–	3,405,526	10,518,245	–
R0020	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	–	–	–	–	–	–
	Technical provisions calculated as a sum of BE and RM	–	–	–	–	–	–
	Best estimate						
R0030	**Gross Best Estimate**			(289)	(139)	(428)	–
R0040	Total recoverables from reinsurance/SPV and Finite Re before the adjustment for expected losses due to counterparty default		–	–	–	–	–
R0050	Recoverables from reinsurance (except SPV and Finite Re) before adjustment for expected losses		–	–	–	–	–
R0060	Recoverables from SPV before adjustment for expected losses		–	–	–	–	–
R0070	Recoverables from Finite Re before adjustment for expected losses		–	–	–	–	–
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default		–	–	–	–	–
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re		–	(289)	(139)	(428)	–
R0100	**Risk margin**	440			211	651	–
	Amount of the transitional on technical provisions						
R0110	Technical Provisions calculated as a whole					–	–
R0120	Best estimate					–	–
R0130	Risk margin					–	–
R0200	**Technical provisions – total**	7,112,870			3,405,598	10,518,468	–

S.23.01.01 – Own Funds (Template subject to audit)

	Basic own funds	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
R0010	Ordinary share capital (gross of own shares)	26,500	26,500		–	
R0030	Share premium account related to ordinary share capital	–	–		–	
R0040	Initial funds, members' contributions or the equivalent basic own–fund item for mutual and mutual-type undertakings	–	–		–	
R0050	Subordinated mutual member accounts	–		–	–	–
R0070	Surplus funds	–	–	–	–	–
R0090	Preference shares	–		–	–	–
R0110	Share premium account related to preference shares	–		–	–	–
R0130	Reconciliation reserve	13,503	13,503	–	–	–
R0140	Subordinated liabilities	–		–	–	–
R0160	An amount equal to the value of net deferred tax assets	–				–
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	–	–	–	–	–
	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	–	–	–	–	–
	Deductions					
R0230	Deductions for participations in financial and credit institutions	–	–	–	–	–
R0290	**Total basic own funds after deductions**	40,003	40,003	–	–	–
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	–				
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual – type undertakings, callable on demand	–				
R0320	Unpaid and uncalled preference shares callable on demand	–				
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	–				
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	–				
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	–				

	Basic own funds	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	–				
R0370	Supplementary members calls – other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	–				
R0390	Other ancillary own funds	–				
R0400	**Total ancillary own funds**	–			–	–
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	40,003	40,003	–	–	–
R0510	Total available own funds to meet the MCR	40,003	40,003	–	–	–
R0540	Total eligible own funds to meet the SCR	40,003	40,003	–	–	–
R0550	Total eligible own funds to meet the MCR	40,003	40,003	–	–	–
R0580	**SCR**	10,138				
R0600	**MCR**	4,562				
R0620	**Ratio of Eligible own funds to SCR**	395%				
R0640	**Ratio of Eligible own funds to MCR**	877%				

	Reconciliation reserve	
R0700	Excess of assets over liabilities	40,003
R0710	Own shares (included as assets on the balance sheet)	–
R0720	Foreseeable dividends, distributions and charges	–
R0730	Other basic own fund items	26,500
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	–
R0760	**Reconciliation reserve before deduction for participations**	13,503
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) – Life business	–
R0780	Expected profits included in future premiums (EPIFP) – Non– life business	–
R0790	Total Expected profits included in future premiums (EPIFP)	–

S.25.01.21 – Solvency Capital Requirement – for undertakings on Standard Formula (Template subject to audit)

		Regular reporting		
		C0110	C0090	C0120
		Gross solvency capital requirement	**USP**	**Simplifications**
R0010	Market risk	481		–
R0020	Counterparty default risk	1,590		
R0030	Life underwriting risk	217	–	–
R0040	Health underwriting risk	–	–	–
R0050	Non-life underwriting risk	–	–	–
R0060	Diversification	(440)		
R0070	Intangible asset risk	–		
R0100	**Basic Solvency Capital Requirement**	1,848		

	Calculation of Solvency Capital Requirement	C0100
R0120	Adjustment due to RFF/MAP nSCR aggregation	
R0130	Operational risk	10,698
R0140	Loss-absorbing capacity of technical provisions	–
R0150	Loss-absorbing capacity of deferred taxes	(2,408)
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	–
R0200	**Solvency Capital Requirement excluding capital add-on**	10,138
R0210	Capital add-ons already set	–
R0220	**Solvency capital requirement**	10,138
	Other information on SCR	
R0400	Capital requirement for duration-based equity risk sub-module	–
R0410	Total amount of Notional Solvency Capital Requirements for remaining part	–
R0420	Total amount of Notional Solvency Capital Requirement for ring fenced funds	–
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	–
R0440	Diversification effects due to RFF nSCR aggregation for article 304	–

S.28.01.01– Minimum Capital Requirement – Non-Composite (Template subject to audit)

	Linear formula component for life insurance and reinsurance obligations	C0040		
R0200	MCR_L Result	73,625	C0050	C0060
			Net (of reinsurance/SPV) best estimate and TP calculated as a whole provisions	**Net (of reinsurance/SPV) total capital at risk**
R0210	Obligations with profit participation – guaranteed benefits		–	
R0220	Obligations with profit participation – future discretionary benefits		–	
R0230	Index-linked and unit-linked insurance obligations		10,517,817	
R0240	Other life (re)insurance and health (re)insurance obligations		–	
R0250	Total capital at risk for all life (re)insurance obligations			–
	Overall MCR calculation	C0070		
R0300	Linear MCR	73,625		
R0310	SCR	10,138		
R0320	MCR cap	4,562		
R0330	MCR floor	2,534		
R0340	Combined MCR	4,562		
R0350	Absolute floor of the MCR	3,251		
R0400	**Minimum Capital Requirement**	4,562		