



We are making things better together

Customer retention

UK & International (%)

79%



Scandinavia (%)

78%



Canada (%)

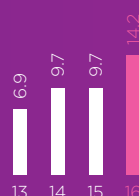
84%



Shareholder returns

Underlying return on tangible equity (%)

14.2%



Tangible net asset value (£bn)

£2.9bn



Dividend for the year (p)

16.0p



Financial summary

Net written premiums (£bn)

£6.4bn



Combined operating ratio (%)

94.2%



Underlying earnings per share (p)

39.5p



We've been protecting customers from risk and uncertainty for more than 300 years. However, the needs of our customers are constantly evolving, so we must innovate and improve to serve them well and win in our chosen markets.

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RSA at a glance

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This Annual Report and Accounts contains 'forward-looking statements' with respect to certain of the Group's plans and its current goals and expectations relating to its future financial condition, performance, results, strategic initiatives and objectives. For further details, reference should be made to the 'important disclaimer' on the inside back cover. Pages 4 to 41 constitute the Strategic Report of RSA and are incorporated by reference into the Directors' and Corporate Governance Report set out on pages 42 to 101. The Directors' and Corporate Governance Report has been drawn up and presented in accordance with, and in reliance upon, applicable English company law and the liabilities of the Directors in connection with that report shall be subject to the limitations and restrictions provided by such law.

Alternative performance measures

RSA uses alternative performance measures, including certain underlying measures, to help explain business performance and financial position. Further information on this is included on pages 22, 190 and 191.



Explore online

Visit us online to see summary information and listen to our Group Chief Executive's interview at: rsagroup.com/annualreport

RSA at a glance

We are a leading international general insurer focused on northern developed markets, with over 13,000 employees and £6.4bn premiums.

RSA Group

13,394

Employees

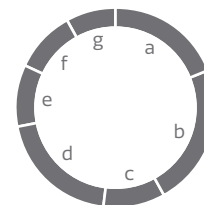
£6.4bn

Net written premiums in 2016

94.2%

Combined ratio in 2016

2016 Net written premiums by product



a. Personal Motor 19%
b. Household 23%
c. Personal Other 10%
d. Com. Property 20%
e. Com. Motor 10%
f. Liability 10%
g. Marine & Other 8%

Our ambition

- A leading international general insurer focused on the UK & International, Canada and Scandinavia.
- Aiming to compete only where we can win. And to win where we compete.
- Well capitalised, achieving sustainable attractive returns.
- Strong operational delivery; transparent and easy to understand.
- Enduring customer appeal.

For more information see pages 10-13

What we do

We are one of the world's longest standing general insurers, providing peace of mind to individuals and protecting small businesses and large corporations from uncertainty.

At RSA we operate across society, providing award-winning Personal, Commercial and Specialty insurance products and services. Whether it's direct-to-customer, via our broker relationships or partner organisations, we use our experience to anticipate and exceed customer expectations and improve outcomes across our value chain.

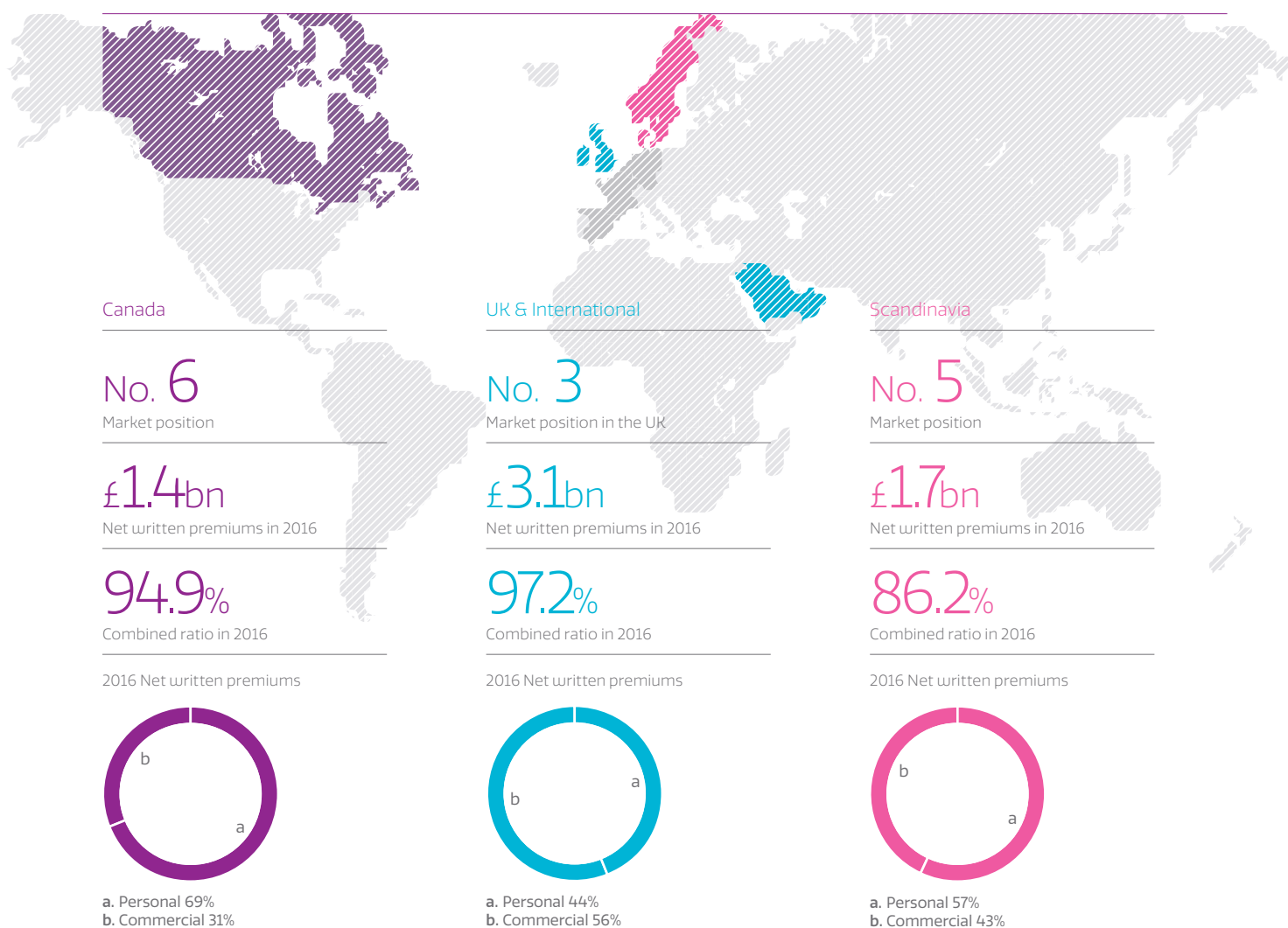
For more information see pages 8-9

Where we operate

We have tightened our strategic focus onto three core regions; the UK & International, Scandinavia and Canada.

These core markets are where we have established leadership positions, giving us the scale, relationships and track record needed to compete and win for customers, for shareholders and our broader communities.

For more information see pages 26-33



Our customer franchise

- Market-leading positions.
- Recognised strong brands.
- Award-winning products.
- Excellent broker relationships.
- Attracting leading affinity partners.
- Strong customer satisfaction metrics.
- High and stable customer retention.

➔ For more information see page 15

Production distribution and brands

We have a broad multi-product and multi-channel offering with regional leadership positions.

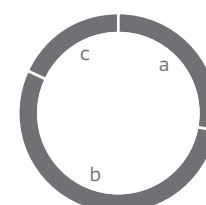
In Scandinavia we operate in Sweden as Trygg-Hansa and in Denmark and Norway as Codan.

In Canada, our main brands are Johnson, RSA, Canadian Northern Shield, and Western Assurance.

In the UK we operate through our MORE TH>N and RSA brands and in Ireland our 123.ie and RSA brands.

➔ For more information see pages 26–33

2016 Net written premiums



a. Direct 28%
b. Broker 54%
c. Agent/affinity 18%

MORE TH>N®
TRYGG HANSA

CODAN
PART OF THE RSA GROUP

RSA INSURANCE

123.ie

JOHNSON

WA
PART OF THE RSA GROUP

CNS
PART OF THE RSA GROUP

Welcome to our 2016 Annual Report



Martin Scicluna
Chairman

I am very pleased to report a year of excellent progress for RSA. Despite the uncertainty and turbulence created by some of the external political events, we have seen the organisation deliver a very strong performance.

The extensive restructuring groundwork of the recent past, which has seen the company operationally streamlined and financially strengthened, is now bearing fruit.

This year we completed the disposal programme we have been undertaking. The conclusion of the sale of our Latin American and Russian operations in 2016 and the sale of our UK legacy liabilities post the year end, leaves us with a business that is now focused on our three

Our Board engaging with employees and operations



Women in Leadership Event in Peterborough



RSA networking breakfast



The More Th>n brand launch



Visiting our John Lewis team

core regions of the UK & International, Canada and Scandinavia. This has enabled management and the organisation as a whole to focus on improving our customer service, our insurance offer and our returns to shareholders.

I am delighted to say that RSA has also delivered a year of significantly improved results for the third year in a row, building on the momentum created in the business. As a result, we have exceeded the strategic and financial objectives we set out in 2014, and remain on course for the new performance ambitions we set out a year ago. We have the opportunity to be a long-term winner in all three of our core regions as we now focus on improving the strength of our offer to customers and consolidating our market position. We are in a position to become the best-in-class performer that I believe RSA should be.

The sense of energy and commitment that our employees have shown this year is a key pillar of our success. I am extremely grateful to everyone who has played such a part in helping to improve our efficiency and effectiveness whilst ensuring that we remain focused on serving our customers better and meeting their needs. On behalf of the Board, I would like to thank them for their determination, dedication and professionalism. The high standards they have set show through in the financial results we have delivered for the year.

Premiums were up 6 percent for the Core Group to £6.3bn, although flat at constant FX. Underwriting profits have again improved significantly to £380m (2015: £220m) with a combined ratio of 94.2 percent (2015: 96.9 percent). Operating profit of £655m was up 25 percent, with profit after tax of £20m reflecting the one-time impacts of disposals. As a result we are proposing a final dividend for 2016 of 11p which would bring our total dividend for the year to 16p (2015: 10.5p), up by 52 percent.

The Board and management of the business have every confidence that there is plenty more to come. Stephen Hester's leadership has put us back on a path to success, and the strength and depth of the very capable team he has put in place is now really showing through. On behalf of the Board I would like to thank Stephen and his management team for their hard work and success in 2016. However, the effort of restructuring and refocusing the organisation was only the beginning, and we need to keep raising our ambitions to accelerate what we have begun and to harness that sense of strength and pride which is flowing through the organisation.

As a Board we are there to support, as well as to challenge, and to ensure that we become the best company we can be. To this end we added two new independent directors in 2016 with the arrival of Martin Strobel and Isabel

Hudson, both of whom have extensive insurance industry experience.

We welcome them and look forward to the insights they will bring. After nine years on the Board, Johanna Waterous, our Senior Independent Director, will retire on 5 May 2017. On behalf of the Board and the Company I would like to thank Johanna for her contribution to the Group over the past nine years and for her work as Senior Independent Director since May 2014. Isabel Hudson will succeed as Senior Independent Director with effect from 5 May 2017. I want to thank the whole Board for their unwavering commitment this year, and look forward to working with them during 2017.

Your Board believes the Company is very well positioned to drive further value. I would like to thank all our shareholders for their continued support and look forward to seeing many of you at our AGM in May.

Martin Scicluna
Chairman
22 February 2017

Our strategic response to a changing environment.



Economic

Our strategy is highly influenced by economic context, which directly impacts both the insurance and financial markets, in which we operate.



→ Low growth

What: We operate in mature and stable markets where GDP is expected to show modest to low growth.

Impact: This creates a competitive pricing environment, making profitable growth more challenging.

Response: RSA is focused in areas where we have strong customer franchises, with a balanced business model. We aim for quality over quantity and seek to achieve selective growth with cost discipline and underwriting excellence.

→ Low interest rates

What: As a result of low inflation and slow economic growth, interest rates remain at record lows.

Impact: Low interest rates means lower investment returns putting greater emphasis on underwriting performance.

Response: RSA's performance gains now produce underwriting profits in excess of investment income for the first time in its history.

→ Market volatility

What: Political uncertainty impacts financial markets, making them significantly more volatile.

Impact: Recent political developments such as the UK's EU referendum and US presidential elections have led to significant financial market reactions, particularly impacting foreign exchange rates, credit spreads and interest rates.

Response: With balance sheet strength restored and capital optimisation in progress, we have set the foundations for a resilient RSA. With over two-thirds of RSA's operating profit in non-Sterling currencies, we are net beneficiaries of Sterling depreciation.



Digital

We are responding to digital trends, ensuring we keep customers at the heart of what we do.



→ Digital evolution

What: Technology is a key enabler to all areas of business, from product design and customer engagement to operating models. Digital is transforming consumer behaviour enabling customers to be more in control.

Impact: Our world is evolving rapidly with the advancement of technology. Main areas of insurance innovation include data analytics, digitisation and strengthening of customer service levels.

Response: We are focusing on being proactive and digitally enabled, and providing tailored products that meet evolving customer requirements. Our plans are focused on investments to simplify our business and technology environment and to strengthen our delivery capability. RSA is improving quote and buy capability, pricing sophistication and online servicing with targeted investment in improving operational efficiency.

→ Digital disruption

What: The evolution of the Internet has taken a huge advance in its ability to gather, analyse and distribute data that we can turn into information and knowledge.

Impact: Connectivity and sensing technology has been discussed for over a decade but now the enablers are in place to pave the way for disruption.

Response: RSA has started to explore these opportunities, particularly in the UK where it is a leading provider of telematics insurance products to young drivers. This helps customers drive responsibly and affordably, and enables us to capture value, through more accurate underwriting, and in learnings to the rest of the Group.



Natural environment

Our business relies on energy and resources provided by the natural environment. It's our duty to ensure that we operate in a way that preserves the sustainability of our business, our communities and the natural environment.



→ Climate change, extreme weather and resource scarcity

What: Climate change poses risks to both people and the natural environment. According to PwC's megatrends report, by 2030, the world will need 50 percent more energy and 35 percent more food than it does today. This will increase pressure on finite natural resources.

Impact: Climate change is already having an impact on our environment. The frequency of catastrophic weather events is on the rise, and related insured losses have increased fourfold over the past 30 years. With growing pressure on resources, people are having to do more with less.

Response: Responding to major events and protecting our customers when they need us most is what we do. As extreme weather events have become more frequent we have expanded our resources and capabilities to manage them. We constantly monitor weather patterns and predictions to ensure we are prepared when the worst happens, and our claims teams have developed Event Plans to ensure the business is ready to respond when our customers need us.

As well as responding to specific events, RSA is also committed to doing its bit to reduce carbon emissions, having met our carbon reduction target to reduce emissions by 12 percent per person by 2018. Also, RSA is a leading insurer of renewable energy, having been involved in coverage of 90 percent of operational offshore wind farms.



Social

As an insurer we must anticipate and adapt our products and services to reflect social trends. As a business we must also be conscious of, and meet, society's expectations of us.



→ Population growth and urban living

What: The UN predicts that population growth and urbanisation will add a further 2.5bn to the world's population by 2050.

Impact: The increased demand on infrastructure, such as roads, housing and natural resources will lead to greater risks to safety and security.

Response: RSA continues to proactively educate on the risks presented by urban living and helping our customers avoid risks. For example, we run road safety campaigns across the Group. We also innovate, creating products that reflect new ways of living, such as telematics, our data-driven car insurance product.

→ Inequality, unemployment and underemployment

What: Inequality based on age, gender, ethnicity or background remains a significant social issue in the workplace.

Impact: According to the OECD, inequality harms economic growth. A lack of investment in education is a major contributor to inequality and underemployment.

Response: At RSA we believe in equal opportunities and value diversity. Females represented 55 percent (7,391) of employees¹ overall (male 45 percent – 6,145 employees). We seek greater female representation at a senior level but base all hiring and promotion decisions on merit. For more information see page 36.

We also support our communities. In the UK, employability workshops with local schools share the skills of our people with students helping them to be work-ready and our partnership with the School for Social Entrepreneurs encourages small businesses in the community to grow.

→ Trust in business

What: Public trust in businesses remains low since the financial crisis. Elderman's trust barometer shows financial services businesses are among the least trusted.

Impact: Trust is crucial to success. Our customers trust us to be there when things go wrong and shareholders trust us to deliver against our stated targets.

Response: We don't take trust for granted. We earn it, by placing customers at the heart of our business, constantly improving our products and services to meet their needs, and by providing open and honest communication with stakeholders.

Note:

1. Based on total Group permanent headcount.

Our business model provides the framework for us to serve all of our stakeholders.

Our business model framework

What makes RSA different

Best-in-class ambition

Our values and culture support a high-performing and inclusive RSA. The collective drive of everyone at RSA raises the Group's ambition and potential to improve.

Brand quality

With over 300 years of experience we have developed trusted and recognisable brands in our markets, supporting our strong customer franchises.

Insights

We understand that our business operates in a broader market context. By adapting to our environment we ensure we maintain a robust business model, relevant to our customers and marketplace.

Balance of scale and focus

Our unique mix of scale and focus across three core regions enables us to achieve agility and intense performance focus. Operating in market-leading positions, we also benefit from diversification in capital and returns.

The resources we use

Financial

£5bn of capital (equity and debt) is employed within RSA to support customers and generate shareholder returns.

Intellectual

Technical expertise is crucial to gaining competitive advantage in insurance. Our intellectual capital is stored in the underwriting expertise of our people that has built up over our history and is enhanced through our technical academies.

People

RSA is a people-centred business, with over 13,000 employees across our core business ensuring that operations run smoothly.

Relationships and partnerships

Relationships across our value chain are a key resource for RSA. We rely on relationships with brokers and partner organisations to distribute c.70 percent of our business. Relationships with our supply chain enable us to provide an efficient claims service.

Natural

We have three core regions in our business and operate across c.200 offices.

Technology

RSA is harnessing the power of technology through e-enabled distribution, increased operational efficiency in policy and claims administration and enhanced data and pricing analytics.

Where we create value

The way we manage

Strategy

Focused

A leading general insurer, focused on the UK & International, Canada and Scandinavia.

Stronger

Operate with capital strength and quality.

Better

Improve business performance and the capacity to sustain it.

Our strategy is executed within a robust risk management (see pages 38 to 41) and governance (see pages 42 to 64) framework.

Our sustainability priorities

See more on our corporate website rsagroup.com/responsibility.

Responsible business

Acting responsibly in everything that we do, helping to build trust in our business.

Safe secure world

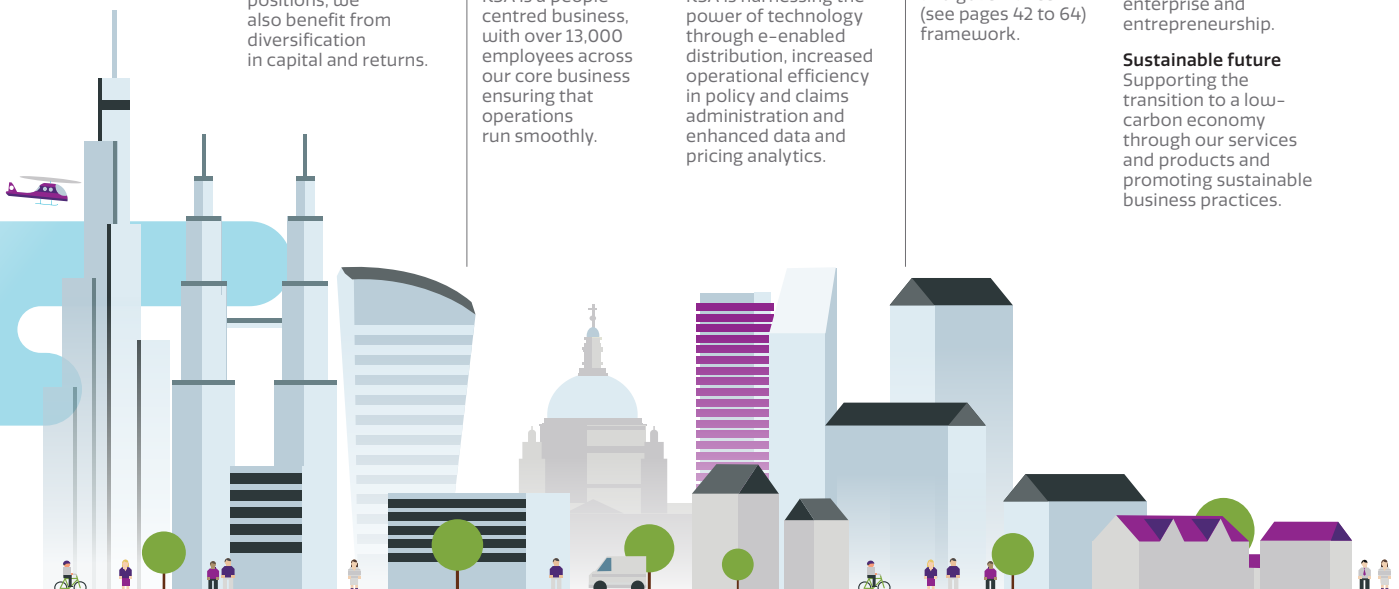
Developing products and programmes that give our customers confidence to lead their lives.

Thriving communities

Giving back to our communities through education, employability, enterprise and entrepreneurship.

Sustainable future

Supporting the transition to a low-carbon economy through our services and products and promoting sustainable business practices.



How we create value



Understanding risk and pricing effectively

We are in the business of risk management. We strive hard to understand the risks our customers want us to insure and make sure that we price our products appropriately.



Global expertise and geographic diversification

As an international business we seek to maximise the benefits of our reach without losing touch with the differing needs of the markets we operate in.



Serving customers well and proactively managing claims

Our customer expectations are increasing. We aim to constantly improve the service we offer, and pay claims quickly and efficiently.



Effective product distribution

We distribute our products through many different channels. Efficient access to customers is key if we are to continue to develop our business.



Prudent investments that protect policyholders and capital

Our business generates significant assets which are prudently invested to be available to pay claims when they are due.

Our impact in 2016



Financial value

£655m
Operating profit

14.2%
Underlying return on tangible equity



Social value

£1.7m
Value of community contributions¹

6,081
Volunteer hours in our local community



Environmental value

15%
Reduction in our carbon emissions per person



Customer value

c.80%
Customer retention

Note:

1. Payments to charities, employee fundraising, value of volunteering and gifts in kind.



Group Chief Executive's statement



In 2016 RSA took major strides forward, moving seamlessly from 'successful turnaround' to organic outperformance.

Stephen Hester
Group Chief Executive

Operating Profit

£655m

+25%

Underlying earnings per share

39.5p

+42%

Total dividend per share

16p

+52%



For more information see Financial Review on pages 22–25

The strategic restructuring and turnaround of RSA started three years ago. Since then we have accomplished everything, and more, that was targeted.

1. The Group is now focused on its strongest businesses, a key to future outperformance. Divestments to achieve this focus have raised £1.2bn.
2. RSA's balance sheet is transformed. Credit Ratings are restored, regulatory capital and related capital ratios are at the upper end of our target ranges.
3. Performance is transformed. 2016 record underwriting profits of £380m compare to a 2013 profit of £1m. Underlying return on tangible equity of 14.2 percent in 2016, is now in the upper part of the 12-15 percent target range we originally set. Dividends are restored and growing.

The quality of the foundations laid during this period, underpinned by the franchise strengths of RSA's 300-year history, gave us confidence at the start of 2016 to lay out new ambitions for the future.

We now aspire to move RSA's performance levels towards best-in-class for our markets, for customers and shareholders. If we succeed we will outperform over the coming years. 2016 performance provides an encouraging down payment on this aspiration, delivering a combined ratio ('COR') of 94.2 percent, a record for RSA.



RSA networking breakfast

Strategy and Focus

RSA is a strong and focused international insurer. We have complementary leadership positions in the major general insurance markets of the UK, Scandinavia and Canada. We have valuable franchise strength and balance across these regions, between commercial and personal customers and across product lines.

The history, dynamics and structure of our markets show that focused regional market leaders can both successfully sustain customer appeal (market position) and achieve superior shareholder performance. This is the course we have set out upon.

External Conditions

The general insurance markets we operate in are relatively mature, consolidated and stable. Attractive performance is possible despite slow growth, economic and competitive challenges. It requires intense operational focus within a disciplined strategic framework.

Financial markets are also important for all insurers. Low interest rates hurt. But they force a greater concentration on the core business of underwriting which can yield significant improvements. 2016 is the first year for RSA where underwriting profits have grown to exceed investment income, a trend we expect to continue.

2016 was a year of volatile financial markets, testing both capital resilience and profits. Bond yields at year end were below those of a year ago in our major markets. Credit spreads were narrower (hurting UK pension accounting). But conversely, a significant Brexit-induced weakening of Sterling since June helps RSA, as c.70 percent of our operating profit is earned outside the UK.

2016 Actions

Strategic Focus: RSA's three year 'focus' programme was completed with the sale of our businesses in Latin America and Russia which closed in 2016. Evidence is mounting that the concentration of management focus and resource onto our core businesses will be a key enabler of future performance gains.

Group Chief Executive's statement – continued

Financial Strength: Our 'A' grade credit ratings are strong and stable. Our Solvency II capital ratio has been improved from 143 percent (2015) to 158 percent at the end of 2016 (target range 130–160 percent), despite retirement of £200m of high-cost subordinated debt. Risk reduction in our UK pension scheme assets has also been successfully completed. And 2016 saw testing financial and insurance event volatility which RSA withstood well. Since year end our disposal of UK Legacy liabilities has given us an important boost to capital and the opportunity to improve capital quality still further.

Business Improvement: Our goal is to systematically and determinedly hunt down performance improvement opportunities across our business. We have taken RSA's performance from below that of competitors in 2013 and prior, to 'in the pack'. All efforts are now concentrated on moving towards our best-in-class ambitions. The plan is substantially the same across our businesses. Focus on improving service to customers, on underwriting and on costs.

Across the Group, our many customer initiatives have sustained retention rates and above average satisfaction measures. Core premiums were up in 2016 but on lower policy volumes. We are determined to compete on quality, with competitive but profitable pricing. We will not chase unprofitable growth. However, there are encouraging signs that continuing underwriting and service capability improvements will restore modest volume growth and we hope to deliver good evidence of that in 2017.

RSA's most important performance lever is our underwriting judgement. Across the Group portfolio disciplines, skills enhancement, data and model improvement and indemnity initiatives are producing strong benefits. Attritional loss ratios for the Core Group improved 1.4 points on 2015 and are 4 points better than those of 2013. We target further improvement still.

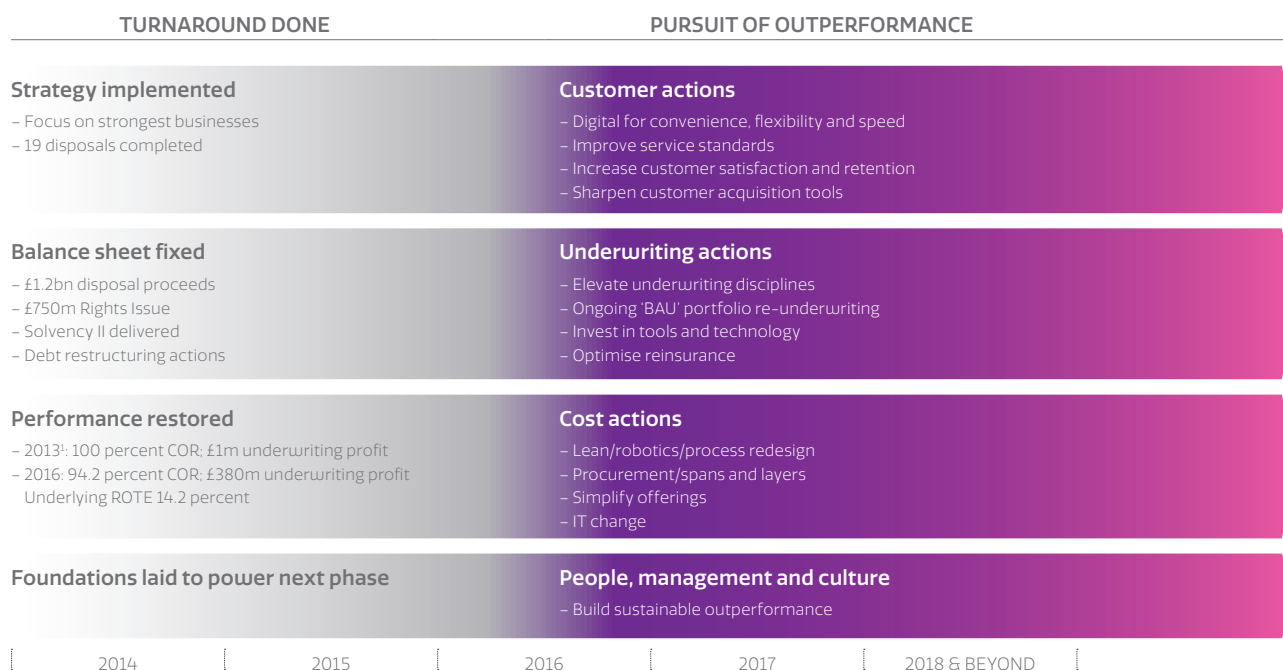
Cost efficiency is the other crucial performance ingredient. We have achieved c.£290m of gross annual savings (vs original 2016 target of

>£180m). We believe we can raise our savings target for the third time and now expect to deliver over £400m p.a. by 2018. Headcount has reduced 19 percent since 2013 in our core businesses as our people have become more productive. We expect to enhance their productivity further with continued business re-engineering, enabled by technology and infrastructure renewal programmes covering digitisation, robotics, infrastructure replacement and software upgrades which continue successfully in each region.

Financial Results 2016

Operating profits – our key ongoing measure – rose 25 percent to £655m. Underlying earnings per share (EPS) rose 42 percent to 39.5p. Statutory profit after tax of £20m reflects a particularly 'noisy' year in accounting terms. The very strong underlying results were optically offset by planned restructuring costs, debt buy-back costs and non-capital accounting charges. We plan that 2017 should be much cleaner and be the last year of material 'below the line' costs.

Pathway to outperformance



Note:

1. Like-for-like basis. Refer to page 190 for further explanation.



The More Th>n brand launch



Core premium income was up 6 percent, but adjusting for FX and price changes, volumes were modestly down. Premium income was in line with our plan on that basis.

Underwriting profits, the litmus test of performance, rose 73 percent to a record £380m. This represents a combined ratio of 94.2 percent, also a record for RSA. Reserve margins were strengthened to 5.5 percent (2015: 5 percent) building some additional cushion against future challenges.

Underlying quality of results was excellent. Current year underwriting profits were a record £271m, up 110 percent, and volatile weather/large loss items did not help us out, being 0.3 points higher than 2015 at Core Group level.

Particularly pleasing was the spread of performance. Each region hit or exceeded its operating plan targets. Scandinavia supplied 47 percent of operating profits with a COR of 86.2 percent. The UK recorded its first significant underwriting profit in a decade (£123m). And Canada did well (94.9% COR), despite natural catastrophes in the region. The one sub-regional disappointment was Ireland. Despite dramatic improvement to break even on current year operating profit, further prior year reserve strengthening was required taking the Irish COR to 116.2 percent.

Reflecting RSA's strong progress, a final dividend of 11p/share is proposed making 16p/share total for the year, up 52 percent. This represents a 41 percent pay out of underlying EPS (in line with stated policy). It remains our belief that RSA will generate attractive free capital, net of organic growth needs and regular dividend pay outs, once restructuring actions complete and bond 'pull to par' impacts reduce, probably in 2018.

Looking Forward

Our performance target of 12–15 percent return on tangible net assets is still good by industry standards and represents a creditable achievement level for RSA, implying better ongoing underwriting performance than any year prior to 2016. However, given our progress and the Legacy sale, we are raising the target to 13–17 percent ROTE¹. Additionally the supplementary ambition we have set of moving towards best-in-class combined ratio performance in our markets, if achieved, should allow us to exceed even this higher range in time. We will try to do just that.

Thanks

RSA is making terrific progress. This is thanks to the efforts of our people and the support of customers, brokers and other stakeholders. Our performance gains are not easy things to achieve, especially with a tough industry backdrop. Sincere thanks and appreciation go to all involved.

RSA has a proud history, despite bumps along the way. We are determined, in performance terms, that the future can be brighter still.

Stephen Hester

Group Chief Executive
22 February 2017

Our 2016 Strategic Report, on pages 4 to 41, has been reviewed and approved by the Board of Directors on 22 February 2017.

Note:
1. Underlying measure.

Strategic priorities

Sustainable, high-quality performance improvement is our focus.

Our ambition for RSA is to create a business capable of supporting best-in-class performance levels in each of our key regions.

We are deploying transformation programmes in each region and at the Group head office, aimed at advancing customer service, improving underwriting capabilities and driving cost efficiency.

These are supported by the important underpins of strengthening our technology and instilling a reliable high-performance culture.

Strategic priorities

1 Advance our customer offerings



2 Industry-leading underwriting



3 Drive cost efficiency



4 Make technology a strength



5 Instil reliable high-performance culture



1 Advance our customer offerings.

Our focus

- Digital platforms for customer convenience, flexibility and speed
- High service standards
- Increase customer satisfaction and retention
- Sharpen customer acquisition tools.

Achievement

Average retention across the Group

80%

- Customer satisfaction measures improving across the Group.

Our progress

- +54 UK GSL net promotor score (71 point turnaround since 2014) and 4.8 percentage points increase in retention rates from 2014
- +45 Johnson net promotor score
- Successful marketing campaign 'Take a Look at us Now' in Canada Broker Personal insurance resulting in new business growth
- New Live Online Chat functionality (Johnson Property and Auto in Ontario)
- Re-positioning of Codan brand with launch of 'My Page' in Norway
- 'Effortless' – new KPI in Scandinavia linked to customer loyalty which measures how easy it is to be a customer of Trygg-Hansa
- Delivered customer digital solutions by focusing investment on improving quote and buy capability, pricing sophistication and online servicing.

Good business starts with our customers, and we strive to keep customers at the heart of what we do. This means providing consistent support and excellent service. We are focusing on being proactive and digitally enabled, and providing tailored products that meet evolving customer requirements.

In many of our markets, customer experience is set to overtake price and product as the key differentiator. Our customers will compare us to their best service experience regardless of industry.

We are enhancing our customer capabilities in a number of areas. Firstly, by deploying digital tools and platforms. This means improving our web-based offering and enabling customer self-service. Examples include increasing online quote completion, moving more claims 'status' enquiries to online, digitalising customer communication and reducing reliance on paper-based methods. In short, our aim is to make it convenient and easy for our customers to do business with us.

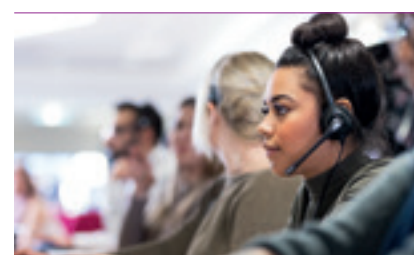
Secondly, we are improving service standards. Our aim is to offer simple products and services in a way that is easy to use and understand; to listen to our customers and proactively address their needs; and to provide a consistent and predictable experience for our customers at all interactions.

Through these, our ambition is to improve customer satisfaction and retention, as well as sharpening our customer acquisition capabilities. These measures are at the heart of sustainable business.

Fort McMurray wildfires – our response for customers

In May 2016, a severe wildfire engulfed the town of Fort McMurray in Alberta, Canada. Over 2,000 homes and buildings were destroyed and 80,000 people evacuated from the town.

The flexible and proactive response of our Johnson business reassured customers as well as provided advice and assistance in their moment of need. We immediately called and emailed all our customers to offer our support. Advice, tips and FAQs were posted on our website and across social media. We listened to our customers' needs, providing service on their terms. We were there for them, wherever 'there' was: putting 50 claims adjusters on the ground at evacuation sites; deploying mobile claims support on the ground at Fort McMurray; and maintaining an active and 24-hour monitored presence on social media.



"... to think that my insurance company has taken the time to call me to make sure my family and I are safe has lifted my spirits on such a sad day" Johnson Insurance customer.

When it was time for our customers to return to the town, we provided them with a 'Re-entry Handbook' outlining the precautions and safety measures they should take as well as providing information on the claims process.

2 Industry-leading underwriting.

Our focus

- Elevate underwriting disciplines
- Ongoing portfolio re-underwriting
- Invest in tools and technology
- Optimise reinsurance.

Achievement

Attritional loss ratio (Core Group)

55.2%

Improvement of 1.4 points

Our progress

- £380m – record underwriting profits in 2016
- 4 point improvement in attritional loss ratio since 2013
- Rebuilt technical pricing models across the Group
- Upgraded external pricing models to Radar Live and Earnix
- Improvements in organic new business growth and retention rates seen in provinces on Radar Live compared to those provinces not yet on new rating engine (Canada)
- Rate changes on new pricing models incorporate better segmentation allowing us to target growth in the segments we want to grow in
- First fully automated claims process in motor (Sweden).

Underwriting is our core discipline. It's what we do. We want to be the best we possibly can, and amongst the very best in our industry.

To do this we must elevate our underwriting disciplines. Whilst we've already achieved a lot in this area, there is still more we can do. This means having a deep knowledge of market circumstances, and focusing only on business we think can generate the appropriate level of returns, even if this means lower growth at times.

Investing in tools and technology is a key ingredient for future underwriting success. This includes increased pricing sophistication with improved price elasticity, retention and demand models, together with a segmented approach to pricing customers and risks. Better exposure modelling, for example in high flood-risk areas, is also key. Taken together, these actions should further improve our agility, with faster speed-to-market and reduced quote times.

Our ambition is to achieve consistent market-leading loss ratios, which underpin the quality of RSA's earnings stream.

UK Telematics – using product design to reduce price

In the UK, we focus our telematics offer on the 17-25 year old young driver segment, and particularly on drivers aged 17-19.

Our offering centres around providing analytical feedback and education to our insured drivers. In the majority of cases this leads to improvements in the insured's driving. The starting price of a telematics policy is already significantly lower than a standard motor policy, and good driving behaviour can lower this further.



In UK motor we've been involved in telematics for some time now, and are now a leading provider with over 500 million miles driven on our telematics products.

Upgrading our pricing tools

We have been upgrading external rating engines across the Group, principally utilising Radar Live and Earnix. These engines are our price-setting tools. They enable the use of more complex algorithms in rating and significantly increase speed in bringing prices to market.

We have already completed the upgrades to a number of portfolios in each of our regions, and we are sequencing the roll-outs to remaining portfolios in 2017 and 2018.

In Canada in 2016, we moved our Household books in Ontario, British Columbia and Alberta onto Radar Live. We are already seeing some encouraging impacts in these portfolios with improvements in new business, retention and segmentation.

3 Drive cost efficiency.

Our focus

- Deploy 'Lean', robotics, and redesign processes
- Efficient and cost-effective procurement
- Optimise spans and layers
- Simplify product offerings
- Technology change.

Achievement

Controllable cost base (Core Group)

£1.5bn

6% lower in 2016

Our progress

- c.£290m gross annualised costs savings to date
- Cost savings target upgraded to >£400m by 2018
- Longer term ambition for <20 percent controllable cost ratio
- 19 percent like-for-like reduction in headcount since start of 2014
- 'Tellus' initiative launched in Sweden to support expense challenge
- Controllable costs down in all regions in 2016
- Use of robotics to drive operational process automation in core regions (e.g. Pet Servicing in UK).

Managing our cost base is another key lever. To be competitive for customers, to invest in better capabilities and to properly deliver for shareholders, we need to permanently reduce costs.

Part of this involves the deployment of 'Lean' methodologies and robotics in our processes (see more detail below).

We're also improving the efficiency and cost effectiveness of our procurement. The biggest example of this is the transition we have made to new IT infrastructure providers. Contract negotiations were concluded in 2015 and transition completed during 2016. The new arrangements give us greater agility, market-leading terms, and meaningful cost savings. We've also renegotiated other major contracts, upgrading terms and moving toward usage based structures to shift to a more variable cost base.

We've also rationalised our office footprint across our regions. In particular, in Canada we've reduced branch footprint from 65 to 36, generating occupancy cost savings and a c.40 percent reduction in occupancy cost per employee.

Optimising management spans and layers by reducing middle management numbers, and simplifying our product offerings are also important contributors to a more efficient cost base.

Finally, technology change is an important 'enabler' in reducing costs, be that through robotics and improved IT infrastructure as set out above, or through other upgrades to policy administration and claims systems, all of which enable us to improve productivity and reduce headcount.



Robotics – improving our automation capabilities

Robotic automation uses software to automate repeatable processes and simplify agent desktops. We have run pilot programmes across the Group with positive early results.

In the UK, one of the pilots looked at a household renewal enquiry, currently a relatively complex process. The results were impressive, reducing the number of applications used by our call centre agent from eight down to one, the number of screens navigated from 28 down to one, and the number of user inputs from over 50 down to just five.

The potential benefits include increased call centre productivity, increased customer satisfaction due to reduction in call times, and a reduction in staff training times by around half.

From paper to paperless in Denmark

E-Boks is a digital mail service in Denmark enabling customers to access communications from companies and public authorities. Codan is one of the companies most requested by users to be added.

In 2016, we began to digitise certain standard customer documents, sending them to e-Boks for customer access. We expect to reduce printing and postage costs as well as modernise the customer experience.

4 Make technology a strength.

Our focus

- Improve operational technology capabilities
- Simplify core platform architecture
- Optimise IT infrastructure
- Improve IT supplier performance and value.

Our progress and achievements

- New IT infrastructure arrangements successfully rolled-out in 2016 that stabilise and simplify our infrastructure
- Deployed new Personal Lines external rating engines increasing automation
- New claims system being implemented in Canada (Guidewire)
- New policy platform rolled-out in Denmark Personal Lines (TIA)
- New policy administration system in UK providing agility and self-service (Duck Creek)
- Focus on digital initiatives in quote and buy and online self-service
- Optimised claims process through a cloud-based online claims platform in Codan (Denmark) connects our claim handlers, suppliers and customers in one online 'universe'.

Improving our technology and the use of it is a key underpin to our performance improvement ambitions in the areas of customer, underwriting and costs. RSA's technology history is one of fragmentation and relatively high running costs.

We are investing in improving our operational technology capabilities together with improving the speed and cost of change. This includes investing in pricing sophistication, customer and broker management tools, and workflow and document management. New pricing sophistication tools include the rating engines Radar Live and Earnix, which we have rolled-out across our Personal Lines businesses.

We are also investing in the simplification of our core platforms. This includes the implementation of the Guidewire claims system in Canada (see below), and new policy administration systems in Denmark and the UK. In the UK, we will deploy Duck Creek as our new policy administration system in Personal Lines, rolling this out first in Motor in the first half of 2017 and then in our new Nationwide Home book in the second half. There is also the potential for our Commercial SME business to leverage the platform.

Duck Creek offers the simplification and standardisation of processes, together with a 'componetised' architecture. This means that it is straightforward to 'plug in' our new rating engine, and also a new claims system when we come to upgrade to this. The result is a scalable model that reduces execution risk.



We've also renegotiated our contracts for IT infrastructure provision, giving us greater agility, market-leading terms, and meaningful cost savings.

Digital investment is also important for RSA and, in particular, we are focusing on improving our quote and buy functionality as well as online self-service for our customers

Guidewire – a new claims system in Canada

In Canada, customer and intermediary expectations are evolving fast. A modern claims system is crucial if we want to respond to this and create a compelling customer proposition while retaining a competitive cost base.

However, RSA's existing claims technology in Canada comprises multiple disjointed systems with significant capability gaps, built on legacy technology platforms, some of which are nearing end of life.

We have chosen to implement a single modern platform, Guidewire, to support multiple customer access channels, enhanced customer segmentation, and improved data analytics.

Overall we should see the benefits of increased efficiency and improved customer service as processes are streamlined and the claims life cycle shortened. We are expecting over c.\$150m of cumulative gross benefits over the first five years of live use.

5 Instil a reliable high-performance culture.

Our focus

- Continuing our ambition for outperformance
- Enabling our people to understand what is expected of them and how they can outperform
- Developing our people and creating great careers.

Achievement

46%

of participants of our talent programmes have new roles within 12 months of completion.

65%

of our senior leader roles have been filled by internal candidates.

Our progress

We are proud of growing talent from within; 27 percent of participants of our talent programmes have stepped into expanded roles resulting from opportunities created following organisational changes.

The transformation journey of the past few years has been challenging, with many changes seen across the Group. As a result we have a company that is Focused, Stronger and Better. With turnaround done, we are now pursuing outperformance, still with a focus on winning where it counts.

Through a strong performance culture that values personal relationships, we have developed leaders and empowered our people to outsmart the competition, while acting within our expectations of them.

Our recent journey has created an environment where our employees increasingly know how to succeed, where they are clear on what we expect of them and how they can bring their best to their role every day. In turn, we are laying the foundations for a company where great careers can be made.

To help colleagues understand our performance ambitions, our 'people expectations' are built into our performance management processes, as well as our reward and 360° feedback tools. This not only means measuring what is delivered, but also how people deliver that output. Our regular performance monitoring processes help to instil a culture of continuous feedback for individuals as well as improving ways of working across teams.

Because we now have many of the right people in place, our leaders were able to focus more on developing our people during the second half of 2016. We also started to explore our outperformance strategies, particularly around what



sustainable capabilities we need for our future success. This often means having an outward-looking focus, spotting any best practice that we can leverage and adopt, helping us to continue in delivering the best for our customers and creating an environment which attracts and retains our talent for the future.

We're committed to making sure that everyone at RSA has the opportunity to perform successfully and develop in their careers. We believe and recognise that what each of us does every day contributes to making this business a success. We know that people are motivated in different ways so we aim to create an open, clear and authentic environment to enable everyone to have honest conversations about their performance and to seek opportunities to grow, learn, outperform and fulfil their potential. This is aligned with our customer-centric ambition to be best in class.

The way we identify and develop our people and the way they are performing and delivering for customers, is what differentiates us today and for our future success. Great people create great results for our business, investment return for our shareholders and undisputable positive experiences for our customers.

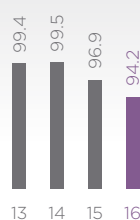
Key performance indicators

We consider the following nine key performance indicators important in measuring the delivery of our strategic priorities.

Combined operating ratio¹ (%)

94.2%

2.7 points better



Definition

A measure of underwriting performance – the ratio of underwriting costs (claims, commissions and expenses) expressed in relation to earned premiums.

Commentary

The COR is used as a measure of underwriting efficiency across the industry. The aim is to achieve a COR as sustainably low as possible – that is without uncompetitive pricing or compromising reserves.

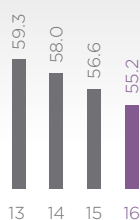
Outlook

We target further improvements in combined ratio.

Core Group attritional loss ratio (%)

55.2%

1.4 points better



Definition

This is the underlying loss ratio (net incurred claims and claims handling expense as a proportion of net earned premiums) of our business prior to volatile impacts from weather, large losses and prior-year reserve developments.

Commentary

Attritional loss ratios are a key lever in the Group's turnaround of financial performance. Improvements in the business mix together with investments in digitally enabled underwriting and claims excellence are targeted at reducing the attritional loss ratio.

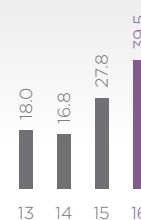
Outlook

We target improving attritional loss ratios in the medium term in line with our ambition of best-in-class performance.

Underlying earnings per share (p)

£39.5p

Up 42%



Definition

Operating profit less interest cost, tax, non-controlling interests and preference dividends, per share.

Commentary

A key measure of the underlying earnings power of the Group as it excludes shorter-term and temporary changes, such as restructuring costs which we have indicated will cease from 2018.

Outlook

We target continued growth in underlying EPS as performance improvement actions take effect.

● This icon indicates those KPIs directly linked to executive remuneration. To read more about executive variable remuneration, including the set of financial and non-financial performance measures on which it is based, please turn to pages 90 to 93.

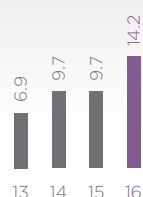
Notes:

1. Combined ratios prior to 2014 restated onto like-for-like basis, refer to page 190 for further detail.
2. Coverage ratio under Solvency II introduced in 2015.

Underlying return on tangible equity (%)

14.2%

4.5 points better



Definition

Operating profit attributable to ordinary shareholders less interest costs and underlying tax, expressed in relation to opening tangible shareholders' funds, i.e. excluding goodwill and intangible assets.

Commentary

A key measure of shareholder value and one that informs overall valuation in the insurance sector.

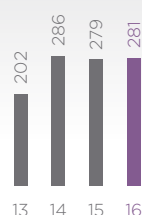
Outlook

We have upgraded our target to 13-17 percent in the medium term.

TNAV per share (p)

281p

Up 1%



Definition

The value of tangible shareholders' funds per share, i.e. excluding goodwill and intangible assets.

Commentary

Growing TNAV generally indicates improving capital metrics. It also represents the underlying asset value of the business, although it is sensitive to external market movements.

Outlook

We expect TNAV per share to increase through retained earnings.

Solvency II coverage ratio² (%)

158%

15 points better



Definition

The Solvency II coverage ratio represents total eligible capital as a proportion of the Solvency Capital Requirement (SCR) under Solvency II.

Commentary

The Solvency II coverage ratio is a measure of the capital adequacy of insurance companies. Our SCR is calculated on our risk profile using the Group's internal capital model.

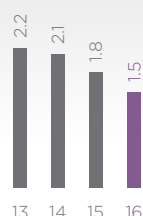
Outlook

We target a Solvency II coverage ratio in the range of 130-160 percent.

Controllable expenses (£bn)

£1.5bn

20% better



Definition

Operating expenses incurred by the Group in undertaking business activities.

Commentary

Reduction of controllable expenses is a key element of the Group's turnaround strategy. We monitor both the absolute level of expense and the expense ratio as part of the turnaround and ongoing performance focus.

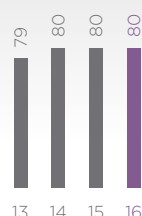
Outlook

We have upgraded our target to >£400m reduction in gross controllable expenses by 2018 and aim to improve expense ratios in the medium term, in line with our ambition of best-in-class performance.

Customer retention (%)

80%

Stable



Definition

We use direct measures of satisfaction, such as NPS and indirect measures, including retention.

Commentary

Strong customer satisfaction translates to improved underwriting results. By ensuring customers are at the heart of everything we do we can optimise business performance.

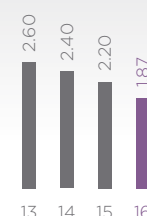
Outlook

Target a growing level of customer satisfaction and improving retention over time.

Carbon emissions per FTE (t)

1.87t

15% lower



Definition

Gross tonnes of carbon dioxide equivalent per full-time equivalent (FTE).

Commentary

We endeavour to reduce our emissions as far as possible by operating efficiently, procuring sustainable alternatives and promoting sustainable business practices.

Outlook

Having met our Group-wide carbon reduction target, we will set a new one in 2017.

Chief Financial Officer's review



I am delighted to report a strong set of results for 2016, which continues the trend we have been building over the last couple of years.

Scott Egan
Group Financial Officer



We are firmly on track to deliver on all our stated objectives, both operational and strategic, and are now in a position to set our sights higher on achieving our best-in-class ambitions.

2016 saw further excellent progress on our transformation programme and turnaround. Related to this, there continues to be a significant number of accounting adjustments impacting the financial statements as we divest of businesses and invest heavily in the future performance of the organisation. For these reasons we refer across our Annual Report and Accounts to a number of underlying performance measures which we believe are a clearer way of fully understanding the performance and progress of RSA at this point. We expect the number and quantum of accounting adjustments to reduce in 2017, which will in itself be the last year where material reorganisation costs sit outside of RSA's underwriting result. For further information on these measures please refer to pages 190 to 191.

We are reporting a strong set of results for 2016. Operating profit was £655m, up 25 percent (2015: £523m); Underlying earnings per share (EPS) was 39.5p, up 42 percent (2015: 27.8p); Underlying return on opening tangible equity of 14.2 percent (2015: 9.7 percent) was at the upper end of our 12-15 percent target range; Post tax profits of £20m reflected non-capital disposal impacts and reorganisation costs discussed on these pages.

Underwriting
Result

£380m
+73%

Underlying
EPS

39.5p
+42%

| £m unless otherwise stated | Scandinavia | Canada | UK & International ¹ | Central functions | Core Group | Total non-core ² | Group 2016 | Group 2015 |
|--|-------------|------------|---------------------------------|-------------------|------------|-----------------------------|------------|------------|
| Net written premiums | 1,721 | 1,443 | 3,081 | 36 | 6,281 | 127 | 6,408 | 6,825 |
| Net earned premiums | 1,735 | 1,454 | 3,173 | (22) | 6,340 | 188 | 6,528 | 7,012 |
| Underwriting result | 239 | 74 | 88 | (9) | 392 | (12) | 380 | 220 |
| of which current year | 213 | 6 | 82 | (28) | 273 | (2) | 271 | 129 |
| of which prior year | 26 | 68 | 6 | 19 | 119 | (10) | 109 | 91 |
| Investment result | 72 | 66 | 149 | - | 287 | 11 | 298 | 322 |
| Central costs | - | - | - | (23) | (23) | - | (23) | (19) |
| Operating result | 311 | 140 | 237 | (32) | 656 | (1) | 655 | 523 |
| Interest ³ | | | | | | | (99) | (106) |
| Adjustment for Legacy sale | | | | | | | (204) | - |
| Other non-operating charges | | | | | | | (261) | (94) |
| Profit/(loss) before tax | | | | | | | 91 | 323 |
| Tax | | | | | | | (71) | (79) |
| Profit/(loss) after tax | | | | | | | 20 | 244 |
| <i>Underlying Profit/(loss) before tax</i> | | | | | | | 556 | 417 |
| COR (%) | 86.2 | 94.9 | 97.2 | - | 93.8 | - | 94.2 | 96.9 |
| Tangible net asset value | | | | | | | 2,862 | 2,838 |
| Underlying Earnings Per Share (p) | | | | | | | 39.5 | 27.8 |
| Underlying Return on Tangible Equity (%) | | | | | | | 14.2% | 9.7% |

Notes:

1. UK & International comprises the UK, Ireland and the Middle East.

2. Total non-core comprises discontinued operations of Latin America and Russia, and non-core operations of UK Legacy.

3. On statutory basis, interest cost are £138m in 2016 which include £39m premium on debt buy back (included within our non-operating charges).

Group underwriting result (£m)

2013 | 1

2014 ■ 35

2015 ■ 220

2016 ■ 380

Premiums

Group net written premiums were down 6 percent in 2016, reflecting the impact of disposals, however Core Group net written premiums of £6.3bn were up 6 percent (flat year-on-year at constant exchange rates).

Scandinavian premiums were up 7 percent, though down 4 percent at constant FX, with growth in Sweden offset by reductions in Denmark and Norway. On an underlying basis premiums were down 1 percent. In Canada, premiums were up 6 percent, though down 3 percent at constant FX with Personal down 4 percent and Commercial flat, reflecting underwriting discipline in competitive market conditions. UK & International premiums were up 1 percent, though down 1 percent at constant FX. UK premiums were down 1 percent with Personal

down 6 percent and Commercial up 2 percent. Premiums in Ireland were up 6 percent driven by continued rating actions.

Retention trends remained broadly stable with overall retention across our Core regions of around 80 percent.

Underwriting result

Group underwriting profit of £380m, up 73 percent year-on-year (2015: £220m), was a record for RSA. The combined ratio was 94.2 percent (2015: 96.9 percent).

The current year underwriting profit was £271m (2015: £129m), reflecting a Core Group attritional loss ratio of 55.2 percent which showed a 1.4 point improvement from 2015. There were good improvements across all core regions with Canada 2.5 points better, UK 1.8 points better and Scandinavia 0.3 points better. We target further improvements still.

Weather, large losses**and prior year development**

Group weather costs were £166m or 2.5 percent of net earned premiums (2015: £219m; 3.1 percent). Included within this are net claims costs of £42m for the Alberta wildfires in May, £33m for the UK & European floods in June,

Underlying return on tangible equity (%)

2013 ■ 6.9

2014 ■ 9.7

2015 ■ 9.7

2016 ■ 14.2

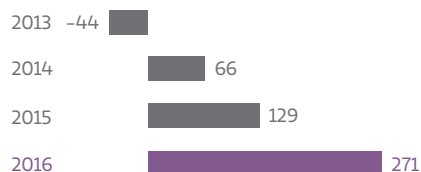
and £26m for Hurricane Matthew in October. Group large losses were £583m or 8.9 percent of net earned premiums (2015: £556m; 7.9 percent).

Prior year profits were £109m with prior year development providing a 2.0 point benefit to the Group combined ratio. This included positive prior year development from the UK, Canada and Scandinavia, and negative results in Ireland.

Current year underwriting results in Ireland improved to a small profit from a £29m loss in 2015, on the back of strong pricing action, attritional loss ratio improvement and expense reduction. However, Irish prior year reserves required further strengthening of £50m, principally for accident years 2014–15 where trend data was hard to identify due to the remediation actions we have had to take post 2013. We target a return to profitability overall in Ireland in 2017.

Financial review – continued

Current year underwriting result (£m)



In setting reserve estimates for the year end we have had regard to the increased uncertainty surrounding a possible reduction in the Ogden discount rate in the UK, and have made allowance for this in the level of margin we are holding, recognising that RSA has limited exposure to UK Motor. Our assessment of the margin in reserves for the Group (the difference between our actuarial indication and the booked reserves in the financial statements) is 5.5 percent of booked claims reserves (2015: 5.0 percent).

Underwriting operating expenses

The overall Group underwriting expense ratio improved 0.5 points to 15.2 percent in 2016. There were improvements of 1.6 points in Scandinavia and 0.2 points in Canada, whilst the UK ratio was 0.3 points higher. We expect continued improvements in the expense ratio over the coming years.

Commissions

The Group commission ratio in 2016 of 14.4 percent was down from 15.9 percent in 2015, driven mainly by the disposal of Latin America which carried a higher commission ratio. We expect the Core Group's commission ratio to be broadly stable in 2017.

Investment result

The investment result was £298m (2015: £322m, or £335m at constant FX) with investment income of £369m (2015: £403m) partly offset by investment expenses of £12m (2015: £14m) and the liability discount unwind of £59m (2015: £67m).

Investment income is down 8 percent on prior year, primarily reflecting the impact of the Latin American disposal and continued low bond yield environment, partly offset by the benefit from the weakening of Sterling. The average book yield across our major bond portfolios was down slightly to 2.5 percent (2015: 2.8 percent).

At current market forward rates, and updating for the Legacy sale, we expect investment income of £300m, £275m,

and £265m in 2017, 2018 and 2019 respectively. Discount unwind is now expected to be in the range £30–35m per annum.

Total controllable costs

As at the end of 2016 our cost reduction programme has delivered total gross annualised cost reductions of around £290m, ahead of our original 2016 target of greater than £180m. We are raising our target for a third time to greater than £400m cost reductions by the end of 2018 (up from our previous target of greater than £350m). 'Costs to achieve' is now expected to be lower than originally planned at around 1.3 times the annual cost savings once fully achieved.

Total Group controllable costs were down 16 percent year-on-year at constant exchange to £1,515m. Core business controllable costs were down 6 percent in the same period at constant exchange to £1,455m (comprising 8 percent cost reductions, offset by 2 percent inflation).

Core Group headcount is down 19 percent since the start of 2014 to 13,394 at December 2016, and is down 7 percent FY 2016 vs 2015.

Non-operating items

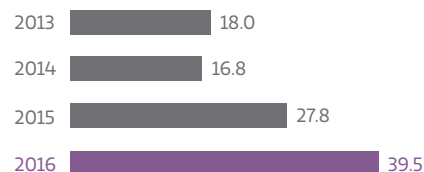
As announced on 7 February 2017, we have booked in 2016 a £204m charge (non-capital) ahead of the sale of the UK Legacy book, primarily reflecting the difference between the reinsurance premium of £799m to be paid and the IFRS carrying value of the legacy liabilities (the IFRS accounts hold the legacy liabilities using a 4 percent discount to face value, £567m vs £834m undiscounted).

In 2017, we expect to recognise an IFRS gain of c.£65m in respect of this transaction mainly relating to the realised gain on the mark-to-market of the bonds transferred to the buyer.

The sale of the legacy liabilities means the Group's Adverse Development Cover reinsurance protection bought in 2014 to partly protect these liabilities, is no longer valuable. Accordingly, we have agreed to commute it for a one-time charge in 2017 of £22m.

Other non-operating charges include the impact of the Latin America and Russia disposals which completed in the year (giving rise to a tangible disposal gain of £159m offset by a £176m non-capital charge relating to foreign exchange and intangibles). Also included in

Underlying earnings per share (p)



non-operating charges are £168m of reorganisation costs which included £49m in respect of redundancy and £119m in respect of transformation activities. Linked to our remaining and increased cost savings targets we expect to record the last of our reorganisation costs in 2017 of c.£100m. We also booked a £39m premium (non-capital) paid on the July buyback of £200m nominal value subordinated debt, and a £30m goodwill write-down relating to the requirement to IPO our Oman business in 2017. Finally, realised investment gains were £30m, mainly relating to bond sales.

Tax

The Group has reported a tax charge of £71m for 2016, giving an effective tax rate (ETR) of 78 percent. The Group underlying tax rate in 2016 was 24 percent.

The £71m tax charge largely comprises of tax on overseas profits and other overseas tax charges; net local tax costs of £12m on the Latin American disposals; and a £52m upward revaluation of UK deferred tax assets, an amount dampened by expected new UK rule changes slowing the utilisation of tax losses.

RSA's ETR is impacted by the IFRS loss on the sale of the UK Legacy liabilities. Although this loss is tax deductible in the UK, no immediate tax credit arises due to RSA's existing unrecognised UK tax losses.

The carrying value of the Group's net deferred tax asset at 31 December 2016 was £216m (of which £212m is in the UK). At current tax rates, a further c.£183m of deferred tax assets remain available for use but not recognised on the balance sheet; these are predominantly in the UK and Ireland.

In 2017, we expect the Group's ETR to return to a rate closer to the statutory tax rates in our core territories. The underlying tax rate, given the scale of unrecognised UK tax assets (which given expected changes in UK legislation are likely to last well over 10 years) may trend towards 20 percent over the next few years.

Tax strategy and contribution

Our tax strategy supports our Group objective to be a responsible business with a positive impact on society. We pay and collect tax in the markets where we operate and comply with all statutory obligations. The taxes borne by the Group's core regions in 2016 total £319m (UK £127m, Ireland £8m, Scandinavia £144m and Canada £40m). Taxes collected by the Group's core regions were an additional £606m.

We consider tax as part of every major commercial transaction undertaken by the Group. Transactions are only carried out where there is a strategic or commercial objective and they are within the Group Risk Appetite and consistent with our Corporate Responsibility Code. We operate a tax governance framework to ensure appropriate oversight of tax by management, local Boards and the Group Board.

We understand the importance of transparency and seek to have an open relationship with the tax authorities. We engage with HMRC in the UK on a real time basis and have a low risk rating.

Balance sheet and capital

RSA's balance sheet and capital position are now stronger and more resilient. Tangible net assets have increased by 1 percent to £2.9bn during 2016. The increase was driven by profits in the period (including tangible disposal gains), positive foreign exchange movements, and fair value mark-to-market gains due to lower bond yields, partly offset by negative IAS 19 pension movements due to narrower credit spreads, disposal impacts (notably the sale of UK Legacy liabilities), the payment of the 2015 final and 2016 interim dividends, and intangible asset additions.

Capital

We maintain a measured approach to capital management, targeting a single 'A' credit rating. This involves considering a range of indicators relating to capital, to operating results, and to qualitative factors.

RSA is a diversified, multi-channel, multi-product general insurer and its business mix reduces exposure to significant volatility. However, the UK pension scheme provides a degree of volatility under Solvency II for RSA. We currently consider a target Solvency II operating range of 130–160 percent capital coverage to be appropriate for the Group's risk profile.

The Solvency II surplus¹ increased to £1.1bn (31 December 2015: £0.9bn) during 2016 with the coverage ratio of 158 percent up 15 points.

Since the year end, the sale of UK Legacy liabilities has provided a boost to RSA's Solvency II position with coverage uplift of 17–20 points, giving proforma coverage of 175–178 percent.

The key drivers of the increase in the year included underlying capital generation which added 29 points of coverage. Restructuring costs and other non-operating charges reduced the ratio by 10 points. 'Pull-to-par' on unrealised bond gains accounted for an 8 point reduction. There was a 12 point benefit from the Latin American and Russian disposals, completed in the period. Market movements added 11 points of coverage, mainly driven by positive foreign exchange and narrower credit spreads. Pension movements, mainly reflecting narrower AA corporate bond spreads, reduced the coverage ratio by 15 points. The 2016 interim and final dividends reduced the coverage ratio by 10 points, and capital requirement modelling updates added 6 points of coverage.

On 12 July we completed the retirement of £200m (nominal value) of subordinated debt (the target instrument was our £500m subordinated notes with 9.4 percent coupon).

Our ambition is to further improve the quality of our capital mix and reduce the cost of our debt. We are exploring the possibility of an issuance of restricted Tier 1 securities and opportunities for early debt retirement.

Rating agencies

S&P and Moody's provide insurance financial strength ratings for the Group and its principal subsidiaries. The Group's S&P rating is A 'stable outlook' and its Moody's rating is A2 'stable'.

Pensions

At an aggregate level the pension fund position under IAS 19 deteriorated during the year from a £64m surplus to a deficit of £197m.

This was mainly driven by the UK schemes which deteriorated by £230m during the year largely due to adverse market movements (in particular tightening of credit spreads). Losses were partly offset by deficit funding contributions (£66m pre-tax) and actual pension increases being lower than expected.

Dividend

We are pleased to propose a final dividend of 11p per ordinary share (2015: 7p). Together with the interim dividend of 5p, this brings the total dividend for the year to 16p (up 52 percent), representing 41 percent payout of underlying EPS.

Our medium-term policy of between 40–50 percent ordinary dividend payouts remains, with additional payouts where justified. Potential for additional payouts should follow the completion of restructuring and progress in the unwind of unrealised bond gains.

Outlook

In 2017, our goal is unchanged: the further raising of performance levels.

Markets will remain competitive. Our priority is to maintain underwriting discipline. Nevertheless, we hope to report premium growth overall.

We target further attritional loss ratio improvements, albeit at a moderated pace, together with further reductions in controllable costs.

Costs from weather/large losses are inherently volatile though bounded by reinsurance protection at levels largely unchanged from 2016.

Investment income is expected to be c.£300m for 2017 assuming current market implied rates, with discount unwind in the range £30–35m. Both numbers have been adjusted for the UK Legacy sale with lower investment income broadly offset by reduced discount unwind. Financial market volatility remains a risk factor.

Non-operating items in 2017 are expected to include the last year of restructuring costs (associated with our increased cost savings target), together with legacy sale related impacts.

We expect to be able to use the capital generated from the Legacy sale to accelerate debt retirement in 2017, thereby further reducing risk, improving capital quality and improving earnings

Overall we expect attractive performance in 2017, building from the quality base now established.



Scott Egan

Group Chief Financial Officer
22 February 2017

Note:

1. The Solvency II capital position at 31 December 2016 is estimated.

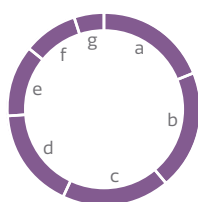
Scandinavia



Patrick Bergander
CEO, Scandinavia

Types of business

- a. Personal Motor 19%
- b. Household 20%
- c. Personal Other 18%
- d. Com. Property 17%
- e. Com. Motor 12%
- f. Liability 9%
- g. Marine & Other 5%



Net written premiums

£1.7bn

Combined ratio

86.2%

Our brands in Scandinavia

TRYGG HANSA

CODAN
PART OF THE RSA GROUP

Our operations in Scandinavia

In Scandinavia we operate in Sweden as Trygg-Hansa and in Denmark and Norway as Codan. We are the fourth-largest insurer in Sweden, the third-largest in Denmark and the seventh-largest in Norway, whilst we are the fifth-largest overall across the region. Importantly, RSA is the only international insurer operating with scale in Scandinavia.

Our business is approximately split 55 percent Personal and 45 percent Commercial lines. It is distributed mainly direct to consumer, via strong agency relationships, with a growing bancassurance channel.

We have key strengths in our Swedish Motor and Personal Accident products and in our Danish Commercial business, while our Norwegian business is developing.

Scandinavian market context

The Scandinavian economy remains stable overall but with mixed experience across the region. There is strong GDP growth in Sweden, whereas Denmark and Norway are set to pick up from relatively low growth levels.

However, insurance markets remain broadly stable and profitable across the region with incumbents generally maintaining a competitive position against market challengers.



National Reflector Day

In Denmark and Norway, Codan raises awareness of the importance of being visible on the roads, especially in the long winter nights. In October 2016 we celebrated National Reflector Day with 184 of our employees volunteering their time to hand out more than 95,000 reflectors to road users.

Summer swim schools

Every year, an average of nine children die in Sweden from drowning. Trygg-Hansa has helped provide materials and resources for the Swedish Life Saving Society's outdoor summer swim schools since 2012. This year we teamed up with Disney and the 'Finding Dory' movie to attract more children to the schools. To date, 28,500 children have attended the swim schools.

Financial performance

In 2016, Scandinavia delivered a 130 percent increase in underwriting profits (at constant FX) driven by strong current year profitability, with record current year profits in Sweden. The current year attritional loss ratio was 64.2 percent, better than 2015 at 64.5 percent. Weather and large losses across the region were relatively benign in 2016. The overall combined ratio was 86.2 percent (2015: 94.0 percent).

Net written premiums of £1,721m were up 7 percent but down 4 percent on a constant exchange rate basis (2015: £1,606m as reported), with volumes down 7 percent and rate up 3 percent. Growth in Sweden was offset by reductions in Denmark and Norway. Underlying premiums were down 1 percent.

We have made good progress with our customer agenda. In Denmark we've seen positive development in customer 'trust' scores, and we've increased our engagement with low 'trust' score customers to gain fresh insights. We're ranked second for SME customer satisfaction in Denmark, and first for overall customer satisfaction in Norway.

The Scandinavian transformation programme has delivered well in 2016, with particular success in pricing and claims sophistication improvements, process automation, online quote capabilities, and customer satisfaction.

Total controllable expenses were down 8 percent year-on-year, with 10 percent cost reductions offset by 2 percent inflation. Headcount was down 7 percent in 2016 and is now down 16 percent since the end of 2013.

Our strategy

Our focused strategy has three core elements. The first is upgrading the business by fixing the basics, the second is creating and fostering a customer culture by 'living our expectations' and the third is to develop our business and bring out the best in each country.

In 2015 we focused on fixing the basics, and in 2016 the Scandinavian businesses moved into the second stage of the transformation programme, which focuses on 'moving from average to great'. This stage has several key areas of development (digitisation and customer journey, strengthening claims and underwriting functions, increasing process efficiency and securing technology uplifts). These are designed to future-proof RSA Scandinavia and enable us to pursue our ambition of best-in-class.

Scandinavia financial summary

| | 2016 net written premiums | | Underwriting result | | COR |
|--------------|---------------------------|-----------------------|---------------------|-----------|-------------|
| | £m | % change ¹ | 2016 (£m) | 2015 (£m) | 2016 (%) |
| Personal | 981 | - | 175 | 108 | 82.0 |
| Commercial | 740 | (9) | 64 | (14) | 91.6 |
| Total | 1,721 | (4) | 239 | 94 | 86.2 |
| Sweden | 990 | 2 | 174 | 101 | 82.3 |
| Denmark | 588 | (11) | 63 | (11) | 89.6 |
| Norway | 143 | (10) | 2 | 4 | 99.1 |
| Total | 1,721 | (4) | 239 | 94 | 86.2 |

Note:

1. At constant exchange.

Outlook

We continue to expect the Scandinavian P&C markets to grow in line with local GDP growth and we target growth broadly in line with the market, subject to maintaining underwriting discipline.

Our focus remains on further improving the underlying performance of the business, particularly attritional loss ratios and cost improvements, as we drive towards our ambition COR of <85 percent.

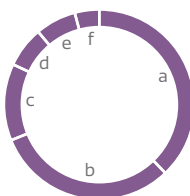
Canada



Martin Thompson
President and CEO, RSA Canada

Types of business

- a. Personal Motor 38%
- b. Household 31%
- c. Com. Property 13%
- d. Com. Motor 7%
- e. Liability 7%
- f. Marine & Other 4%



Net written
premiums

£1.4bn

Combined
ratio

94.9%

Our brands in Canada

JOHNSON

WA
PART OF THE RSA GROUP

CNS
PART OF THE RSA GROUP

Our operations in Canada

In Canada we are the sixth-largest insurer, having established our market position through a combination of organic and acquisitive growth. We operate across all provinces and provide a broad multi-product and multi-channel offering to both personal and commercial customers.

Our portfolio is balanced at around 70 percent Personal and 30 percent Commercial. We have leading market positions in affinity distribution via our Johnson brand and leading positions in Travel and Marine underwriting.

Canada market context

The Canadian market remains competitive with slowing economic growth, in part due to lower oil prices, translating into tough insurance market conditions and continued consolidation trends in the sector.

Broker distribution remains the dominant channel in both Personal and Commercial Lines while affinity and direct channels continue to gradually gain market share in Personal Lines.

In Ontario Auto pricing is regulated, driving a challenging pricing environment in this segment while Personal Household continues to respond to the impacts of severe weather events in recent years.

In Canada we have maintained underwriting discipline and continue to prioritise profitability over top-line growth.



Fort McMurray wildfires

In response to the wildfires in Fort McMurray, Alberta, we donated C\$100,000 to the Red Cross to help the victims. In addition, RSA employees raised more than C\$57,000 through the company's matched funding programme.

Living Planet @ Work

In Canada we entered a five-year partnership with WWF Canada, as the new sponsor of Living Planet @ Work, WWF-Canada's environmental employee engagement programme.

WWF-Canada has also helped RSA Canada implement corporate green teams in the majority of our offices which set and work to achieve sustainability targets. Some are conducting energy audits whilst others are persuading colleagues to think before they print. Meanwhile, in RSA's Mississauga office, the green team has launched successful programs to recycle used batteries, pens, plastic pencils, markers and even eyeglasses.

As sponsor of Living Planet @ Work, RSA Canada empowers other organisations and their employees, to make a similar impact.

Financial performance

We have had a strong and resilient year in Canada. The underwriting profit for the year was £74m (£116m in 2015) with a COR of 94.9 percent, which was in line with our expectations, even after absorbing the impact of the Fort McMurray wildfire losses in May. The attritional loss ratio showed a strong improvement of 2.5 points from prior year to 57.8 percent.

Net written premiums of £1,443m were up 6 percent but down 3 percent at constant exchange rate (2015: £1,360m as reported), with volumes down 4 percent and rate increases of 1 percent. Conditions remain competitive, particularly in the Commercial Broker channel, and our priority continues to be on sustained underwriting discipline.

We have been working hard to enhance our customer offering. In Johnson our service and sales metrics have been outperforming benchmarks. In our broker distributed businesses, faster response times and new digital tools are being offered with promising early results. Customer retention rates have improved by 2pts year-on-year to 84 percent.

Our transformation programme in Canada has progressed well during the year, delivering customer retention actions, deployment of new pricing tools, process simplification, and the implementation of the Guidewire claims system proceeding as planned.

Total controllable expenses were down 8 percent year-on-year (comprising 10 percent cost reductions, partly offset by 2 percent inflation). Headcount was down 7 percent in the year, and is down 19 percent since the end of 2013.

Our strategy

In Canada we are well-balanced by province, customer, channel and product. We offer a broad and diversified offering to customers from personal through to corporate and specialty risk.

Our Canadian transformation programme has seen significant delivery during 2016 with performance improvements right across the business. Our major focus areas include: rebalancing portfolios to leverage competitive advantage and explore market opportunities; improving customer journeys and proposition through process optimisation and digital-enablement; and investing in technology to increase claims efficiency and pricing sophistication.

Canada financial summary

| | 2016 net written premiums | | Underwriting result | | COR |
|--------------|---------------------------|-----------------------|---------------------|------------|-------------|
| | £m | % change ¹ | 2016 (£m) | 2015 (£m) | 2016 (%) |
| Personal | 994 | (4) | 91 | 104 | 91.0 |
| Commercial | 449 | – | (17) | 12 | 103.8 |
| Total | 1,443 | (3) | 74 | 116 | 94.9 |

Note:

1. At constant exchange.

Outlook

We target a stabilisation of premiums in 2017 and continued progress towards our combined ratio ambition of <94 percent. Our focus continues to be on operational improvement (in underwriting, claims, technology and process simplification) and cost reduction.

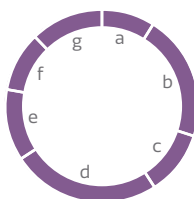
UK & International



Stephen Lewis
CEO, UK and International

Types of business (UK only)

- a. Personal Motor 9%
- b. Household 21%
- c. Personal Other 11%
- d. Com. Property 25%
- e. Com. Motor 12%
- f. Liability 10%
- g. Marine & Other 12%



Net written premiums

£3.1bn

Combined ratio

97.2%

Our key brands in UK & International

MORE TH>N® RSA
123.ie

Our operations in UK & International

In the UK, we are the second-largest Commercial insurer with key positions in Property, Motor, Liability, and Marine, and exposures across the SME, Mid Market and Global Specialty customer segments.

We also have strong positions in the UK Personal Household and Pet markets, and a presence in the UK Personal Motor market with a rapidly growing telematics offering. We have a direct insurance offering through our MORE TH>N brand, and a broker portfolio focused on profitable segments. We also have affinity partnerships with some of the major UK retailers.

We are a leading player in Ireland with particular strengths in Household insurance and in direct sales through our 123.ie business.

In the Middle East we have operations in the United Arab Emirates (UAE), Oman and Saudi Arabia, with headquarters in Bahrain. The portfolio is well balanced across all lines of business and distribution channels, with Brokers being a strong channel in all markets. RSA owns 50 percent of its Middle East business.

UK market context

The UK is a large, mature and stable market with high levels of competition.

Personal Lines in particular is highly competitive with a strong focus on price, and increasing pressure to improve digital capabilities. Commercial lines remain profitable despite prolonged soft market conditions.

The implications of the EU referendum bring a level of uncertainty for the market that will take time to play out. But RSA is well placed, with no significant structural or passporting challenges as a result of EU exit.



Supporting the community

In the UK, our flourishing community programme encourages our people to share their skills and experience to support local schools and colleges.

This includes our Ready Set Achieve programme, which addresses a key social issue by helping young people develop the skills, knowledge and confidence they need to secure employment. The programme also develops the talent of our people, and supports our local recruitment needs. Although not an initial objective of this community programme, we have been delighted to recruit four talented young people having met them at an employability workshop.

Flood response plan

In September 2016, the ABI launched a document to help flood victims understand how Flood Resilient and Resistance measures can be incorporated into a repair.

RSA has liaised with the ABI and worked with our Loss Adjusting partners Cunningham Lindsey, to ensure that our flood response plan provides the right level of information and property improvement advice and guidance for customers affected by flood damage.

UK financial performance

The UK delivered the best underwriting result in over a decade at £123m and a COR of 95.4 percent. Continued delivery from our performance improvement programme has driven this strong result against a competitive landscape.

Customer satisfaction metrics remain strong with further improvements delivered from 2015. Of note, More Than Net Promoter Scores ('NPS') increased by 39 percent from 2015 and Motability NPS remained at market leading levels of +80.

Premiums were down 1 percent overall which included the impact of portfolio remediation in personal broker motor and delegated business.

UK Personal net written premiums contracted by 6 percent following the exit of Broker Motor during 2016. However, the growth of our highly successful telematics proposition continues at pace with 90 percent growth from 2015 and helped deliver underlying 15 percent growth in Personal Motor.

UK Commercial premiums grew by 2 percent following the transfer in of the Scandinavian Marine portfolio during 2016. Excluding this transfer UK Commercial net written premium growth was flat vs 2015.

The UK underwriting result of £123m was underpinned by improving attritional loss ratios (overall 1.8 points better) demonstrating the continuing underwriting discipline across the business. Favourable weather experience was offset by adverse large loss experience, whilst prior year development of 2.5 percent included £14m of favourable development from the December 2015 Storms.

The continuing change activity across the UK helped deliver further improvements to controllable expenses which were down 1 percent, comprising 3 percent gross cost reduction offset by 2 percent inflation. Headcount was down 5 percent in the year and is down 18% since the end of 2013.

Our strategy

Our strategy in the UK market has been to invest in the business, develop our technical insurance capability, enhance our customer proposition and improve cost efficiency to enable RSA to compete in the top quartile of our competitor set.

Our transformation programme is on track and delivering the required capability to adapt and succeed in the evolving market. 2016 has been a year of significant delivery in terms of streamlining and automating processes, replacing our legacy technology, introducing new pricing and underwriting tools and developing a new operating model. Our business is building the required agility to meet the evolving needs of customers and a sustainable base from which to achieve best-in-class performance.

UK & International financial summary

| | 2016 net written premiums | | Underwriting result | | COR |
|-------------------------------|---------------------------|-----------------------|---------------------|-------------|-------------|
| | £m | % change ¹ | 2016 (£m) | 2015 (£m) | 2016 (%) |
| Personal | 1,068 | (6) | 48 | 47 | 95.7 |
| Commercial | 1,520 | 2 | 75 | (35) | 95.2 |
| UK Total | 2,588 | (1) | 123 | 12 | 95.4 |
| Ireland | 306 | 6 | (49) | (35) | 116.2 |
| Middle East | 187 | (8) | 14 | 8 | 92.8 |
| UK & International | 3,081 | (1) | 88 | (15) | 97.2 |

Note:

1. At constant exchange.

Outlook

January renewals have delivered in line with expectations and premium trends are expected to continue to deliver modest growth through 2017.

Despite the competitive and regulatory landscape in the UK continuing to be challenged, we have ambitious plans to continue transforming the UK business, investing in capabilities and delivering sustainable best-in-class performance. Our medium-term target COR of below 94 percent remains.

Regional review – continued

Ireland financial performance

In Ireland, while the headline underwriting loss of £49m is disappointing, the current year underwriting result has returned to profit with an improvement of £30m year-on-year. Full year premiums of £306m were up 6 percent at constant FX vs 2015 with significant rate being carried during 2016.

The underwriting loss of £49m comprises a £1m current year profit (2015: £29m loss) and a £50m prior year loss (2015: £6m loss). The current year improvement reflects significant rate increases, and further cost reductions.

The prior year loss reflects a combination of excessive market claims inflation and the distortion of our reserving patterns following the events of 2013 which have resulted in further strengthening of reserves during 2016. These issues have been amplified by a challenging Irish market, characterised by aggressive claims inflation, increasing litigation mitigated by a very hard rating environment.

Just over £30m of the development relates to three classes: Motor, Liability and SME where we have put through significant price increases in 2016 ahead of our plans, with further increases planned for 2017. Much of the remainder of the adverse development relates to business we have now exited.

The performance improvement plan continues in Ireland. Irish FTE was down 9 percent in 2016 and is down 33 percent since the end of 2013, with total controllable expenses down 24 percent year-on-year.

Ireland Outlook

We are targeting a return to operating profitability in 2017 through continued underwriting improvement, portfolio remediation and cost reduction.

The challenging market environment, in particular for claims inflation with the Book of Quantum revision, PPO legislation and judicial reviews, demands that we continue our focus on securing adequate rate in each of our portfolios.

Middle East financial performance

The Middle East region delivered a sub-96 percent COR for the fifth consecutive year, against a backdrop of a sustained economic downturn and tough trading conditions.

Premiums of £187m were down 8 percent at constant FX as a result of the challenging trading conditions resulting from the macroeconomic difficulties and portfolio action taken in KSA.

The underwriting result of £14m is £6m better than 2015 and the COR improved by 2.6 points to 92.8 percent.

The region secured a new major bank assurance partnership with First Gulf Bank and a new health partnership with NowHealth in Dubai, as well as the opening of new branches and the enhancement of digital offerings.

Middle East Outlook

The medium-term outlook for our Middle East business remains positive.

Targeted growth plans are in place for 2017 and work is underway to further develop capabilities throughout the region including underwriting and pricing sophistication. With our affinity and bank assurance partnerships, we are well positioned to take early advantage of any economic upturn.

Discontinued and non-core operations.

Disposal programme

In 2014 we commenced a major disposal programme with the intention of focusing RSA on its strongest businesses.

During 2016 we completed the sales of our Latin America and Russia businesses. Since the year end we also announced the sale of our UK Legacy liabilities. This marks the end of our disposal programme.

Across the entire programme, we have completed the sales of businesses in the Baltics, Poland, Canadian broker (Noraxis), Thailand, Hong Kong, Singapore, China, India, Italy, UK Engineering Inspection, Latin America, Russia, and now UK Legacy.

The transaction covers £834m of undiscounted liabilities, net of reinsurance (£957m gross of reinsurance), relating to business written in 2005 and prior. Around 75% of these liabilities relate to asbestos, with the balance mainly comprising abuse, deafness, marine and aviation liabilities.

The transaction is strongly accretive to RSA's capital position, adding c.17-20 points of Solvency II coverage. It is expected that these capital resources will be deployed to benefit earnings and capital quality through additional debt retirement in 2017.

UK Legacy

In February 2017, RSA signed contracts, to dispose £834m of UK legacy insurance liabilities to Enstar Group Limited ('Enstar').

The transaction initially takes the form of a reinsurance agreement, to be effective at 31 December 2016, which substantially effects economic transfer, to be followed by completion of a subsequent legal transfer of the business.

Discontinued and non-core operations

| | Net written premiums | | Underwriting result | |
|--|----------------------|------------|---------------------|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| UK Legacy ¹ | – | 2 | (10) | (39) |
| Other discontinued & non-core ² | 127 | 920 | (2) | 14 |
| Total Discontinued and Non-Core | 127 | 922 | (12) | (25) |

Notes:

1. Non-core.

2. Includes Latin America, Hong Kong, Singapore, China, India, Italy, UK Engineering, and Russia.

We are experiencing rapid change politically, socially, economically and environmentally.



SM>RT WHEELS workshop

Trygg-Hansa swim schools

28,500

children taught to swim

Alberta Fire support

C\$157k

donated to assist disaster relief efforts

MORE TH>N
SM>RT WHEELS

30

workshops across the UK, for 500 young people

It is important for us as a business to build trust in the way we operate, tackling issues with bright ideas for our customers, our communities and our environment.

Our approach to corporate responsibility is determined by our stakeholders' view on the environmental, social and ethical issues that they see as important for us as a business to be addressing and influencing. Our five-year strategy has four pillars which address these issues. Safe, Secure World is how we help customers avoid risks; Thriving Communities is how we support our local communities, increasing employability skills in young people; Sustainable Future is how we accelerate the transition to a low-carbon economy and improve resilience to extreme weather. Responsible Business is how we enhance our business reputation through high-quality governance and excellent customer service.

We are now halfway through our corporate responsibility strategy and as such we have reviewed our approach. To do this, we revisited our stakeholder concerns and we looked at the United Nations Sustainable Development Goals (SDGs). We wanted to make sure we were still addressing issues of importance and we wanted to understand how we could influence and support the delivery of the SDGs.

Supporting our customers to live safer, more secure lives

In Sweden, Trygg-Hansa has a long tradition of promoting safety in and around water. In 2016 they teamed up with the Swedish Life Saving Society, Disney and the 'Finding Dory' movie to promote their summer swim schools. During the summer months they sponsored 400 swim schools, teaching 28,500 children to swim.

In the UK, as one of the largest motor insurers, we support young people to drive safely. Drivers aged 17-19 only make up 1.5 percent of UK licence holders, but are involved in 9 percent of fatal and serious crashes¹. To help young drivers stay safe, MORE TH>N's SM>RT WHEELS, an insurance product aimed specifically at 17-to-24 year-olds, uses telematics to encourage safer driving which can reduce accidents by 20 percent.

SM>RT WHEELS has now partnered with leading road safety initiative Good Egg Drivers to help improve safety amongst young people learning to drive.

SM>RT WHEELS has sponsored a number of interactive workshops by Good Egg Drivers that enable schools across the UK to offer free safety guidance to students learning to drive. The first of these took place in Sunderland in June with the plan to run 30 workshops across the UK, engaging with over 500 young people.

1. <http://www.brake.org.uk/events/15-facts-a-resources/facts/488-young-drivers-the-hard-facts>

Securing a sustainable future

Our approach to climate change is three-fold. We support our customers to adapt to changing environmental risks and opportunities through our products and services. We measure, monitor and manage our impact on the environment, identifying ways to reduce our negative impact. Finally, we continue to be a leading provider of insurance to the renewable energy sector.

This year we reduced the emissions from our operations by 15 percent per person from a 2015 baseline, meeting our Group-wide carbon reduction target two years ahead of time. This was achieved through property rationalisation across our regions and encouraging sustainable working practices like recycling; and opting for environmentally sustainable alternatives where possible.

In Canada and the UK, we celebrated World Environment Day on 5 June. In the UK, we ran a 'switch-off' campaign where we rewarded employees who had turned off their IT equipment and reminded everyone of the simple things we could all do to work more sustainably. In Canada, we announced the regional 'green teams' which are being supported through our new five year partnership with WWF Canada. This partnership sees RSA become the new sponsor of Living Planet @ Work, WWF-Canada's environmental employee engagement programme.

In the UK, following another significant flood event in December, we were kept busy supporting customers to get them back to normal as quickly as possible. During the claim settlement process, we encouraged flood resilient measures where appropriate, mitigating the potential damage of future events.

With the largest number of renewable energy insurance experts in the world, we have a Centre of Excellence for Wind in Denmark. We use our knowledge and expertise to support the development of new innovative renewable energy projects like floating wind turbines.

Helping our communities thrive

During the devastating wildfires in Fort McMurray, RSA Canada employees were on the ground with a mobile response unit, providing support at the evacuation centre in Edmonton. With customers, brokers and friends impacted, RSA was keen to provide as much support as possible to the Alberta community.



RSA are committed to delivering the United Nations Sustainable Development Goals through our corporate responsibility strategy, putting our customers first whilst delivering long-term value to our environment and society.

Charlotte Heiss
Group Chief Legal Officer & Company Secretary and
Group Executive Committee Corporate Responsibility Sponsor

RSA donated C\$100,000 to the Red Cross to help the victims of the wildfires and more than C\$57,000 was raised by RSA employees through the company's matched funding programme.

In the UK, our people have been sharing their skills and experience to support our local schools and colleges. Volunteers from across the country have been designing and delivering workshops to help young people to develop the skills they need for the workplace.

Our Ready Set Achieve programme delivers benefits to the community and to our business. It addresses a key social issue as we aim to help young people to develop the skills, knowledge and confidence they need to secure employment, and it also develops the talent of our people and supports our local recruitment needs.

Although not an initial objective of this community programme, we have been delighted to recruit four talented young people having met them at an employability workshop.



We build trust in our company by having robust controls in place to run our business responsibly, minimising negative risks and taking advantage of any opportunities presented. Our corporate responsibility strategy ensures that we identify, prioritise and manage our social, ethical and environmental risks and opportunities.

William McDonnell
Group Chief Risk Officer and Group Executive Committee Corporate Responsibility Sponsor

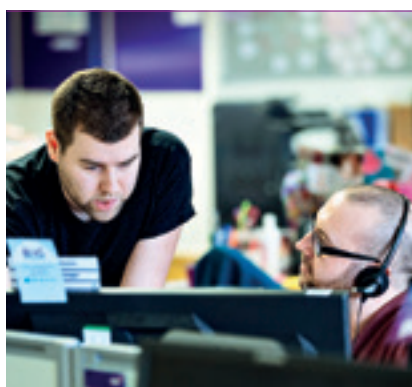
Being a responsible business

Public trust in business has declined in the last year with 75 percent of people agreeing that a company can take specific actions that both increase profits and improve the economic and social conditions in the community where it operates. We engage with customers, employees and suppliers, being open and transparent in how we manage our operations and deliver our products and services, helping us build trust. This year, in response to the UK's Modern Slavery Act, we have reviewed the way in which we recruit our employees and engage with third parties. We have strengthened our policies and procedures to make sure that modern slavery has no place within our business. Our Slavery and Human Trafficking statement will be published online by April 2017.

For more information visit our corporate responsibility webpage at: rsagroup.com/responsibility

Our people

Our people have been resilient and focused throughout this period of change.



In 2016, we were able to put the turnaround behind us and move to the next phase of our transformation journey. Our people have been resilient and focused throughout this period of change and crucial to delivering the successful company we see today.

Our programme to reduce our expense base and the number of permanent full-time equivalent (FTE) employees has made RSA focused, stronger and better. Our core regions of UK & International, Canada and Scandinavia now have a more appropriate overall headcount for the future, with programmes for ongoing improvement in place.

Total number of employees¹ at the end of 2016

| Country | Employees | Percentage of Group total |
|------------------------|---------------|---------------------------|
| UK & International | 6,925 | 52% |
| Canada | 3,190 | 24% |
| Scandinavia | 3,043 | 23% |
| Group Corporate Centre | 188 | 1% |
| Other | 48 | – |
| Total | 13,394 | |

Note:

1. Full time equivalent, including non-permanent resource.



As a Group, we are greater than the sum of our parts due to our ability to leverage opportunities and share best practice across the company.

Our model provides the opportunity for the local HR Directors to tailor the Group people strategy to local business priorities. With the drive for instilling a performance culture from the Group, the regions are focused on building and sustaining a customer-centric culture where colleagues are able to develop.

Performance culture – the foundations are in place

Our recent journey has enabled us to create an environment where people know how to succeed, are clear on what we expect of them and can bring their best to their role every day. In turn, we are laying the foundations for a company where great careers can be made.

We are building the right working environments, supportive processes, and people and communications tools for today and tomorrow.

We have continued to review our cultural risk and health index on a quarterly basis across all our businesses with input from expertise in HR, Risk and Audit, ensuring we are stress testing our organisational capacity.

Because we value a diversity of perspectives, we continue to offer all our employees a number of formal and informal platforms where they can give us feedback. These include enterprise social network service, 'Yammer', Town Hall gatherings and a Group Leaders Forum. During 2016, we have chosen a new partner to measure our

employee engagement levels. This survey ran in January 2017 and we look forward to using the outputs to build our future people strategy.

Development

In 2016, we maintained our commitment to developing talent across the organisation. We have a suite of talent, leadership development and learning tools, which are designed to provide an individualistic approach to development.

For our senior leaders this means having 360° feedback and facilitated planning to focus development with the individual but also to ensure it is aligned with the priorities of the business. We've found this to be a successful and effective way to provide tailored and focused development for our most senior leaders.

In November we held our annual Group Senior Leaders event. This brought together the community of our most senior leaders, enabling them to create new connections, learn about the challenges and trends in the market whilst determining our future priorities.

We also continue to invest in our emerging talent with our Fast Track programme. Run regionally, this is designed to accelerate the careers of the participants by deepening self-awareness and exposing them to MBA topics, such as strategy, marketing and business development.

The impact of our talent programmes is evident from the results. Of the participants in Fast Track, Senior Talent Acceleration and the Executive Development Programme, 46 percent have new roles and 27 percent have expanded roles across the Group. We are proud of growing our talent from within; with 65 percent of our senior-leader roles being filled by internal candidates.

Digital learning

The opportunities employees have for learning are now available everywhere. Unsurprisingly, employees now expect an intuitive and engaging experience when they interact with technology at work. We have looked to build our digital learning offering based on the learner being able to access content in three different ways, giving them choice when they want it.

The first of these is content our employees can find, launch and consume within 15 minutes. This satisfies the 'YouTube/Google' moment that most

people revert to when needing an immediate answer to a question. We delivered this content on both Horizon, our internal Learning and Performance platform, and Origin, our bespoke internal learning video portal.

The second is content longer than our first category, which provides a crossover between formal and informal learning. This is typically content that our employees will need to put aside 30-60 minutes for, but they can be in control of where and when the content is accessed.

And finally, we believe instructor-led training still has its place in our proposition. This is used when the topic is too complex to be covered in the other approaches and where interaction with others enhances the learning experience.

When choosing the appropriate vehicle we consider the learner experience, versus cost effectiveness.

Recognition

Within all our businesses we understand that our most valuable asset is our people and we believe that it is extremely important to recognise their hard work and contributions. Our leaders have the opportunity to recognise all our employees through a number of different tools.

Diversity and inclusion

We have reinvigorated our efforts to build greater diversity across all levels of our organisation and create a more inclusive culture which attracts, encourages and capitalises on diverse perspectives, establishing a stronger foundation for RSA's success.

We know that having a diverse workforce and a supporting inclusive culture is vital for our future. Diversity in thought, background and experience enables us to innovate and create better solutions for our customers.

We kick-started our longer-term strategy, by taking some simple steps to demonstrate our commitment in this area. Firstly, we are partnering with Stonewall to support our ambition to build an inclusive environment. Secondly, we have begun to take part in the 30% Club cross-company mentoring programme, which aims to develop our future female talent, giving them access to senior mentors in other organisations. Thirdly, we are active members in the newly created Gender Inclusion Network for Insurance.

Our Group Chief Legal Officer, who is the Executive Sponsor for diversity and inclusion, has established a group-wide Steering Committee and Working Group to collaborate on diversity initiatives and report on progress to the Board.

In conclusion, we will build the RSA of tomorrow, with our people, for our customers.

| | 2016 | |
|----------------------------|--------|-------|
| | Female | Male |
| Board | 3 | 8 |
| Group Executive | 1 | 9 |
| Senior management | 210 | 454 |
| All employees ¹ | 7,391 | 6,145 |

Note:

1. Based on Group permanent headcount.

Risk management

Promoting a risk culture which protects the customer and maximises shareholder risk-adjusted returns.

Risk management approach

As a 300-year-old insurance group we have developed considerable expertise in how to manage risk, which allows us to be selective in retaining risks within our core expertise whilst ensuring that we manage, mitigate and avoid risks where we are not adequately rewarded. As a pure play general insurer our key area of expertise is underwriting property and casualty insurance risks, which means we are able to provide our customers with competitive products

that protect them effectively against the uncertainty of future loss events whilst ensuring that the risks we accept are collectively managed to maximise risk-adjusted returns to our investors.

All insurance groups are faced with a number of different risks which for example can range from adverse movements in asset prices, external cyber-attacks and significant increases in claim trends to large catastrophic events (details of all the key risk categories are set out on page 40).

Our risk management and controls frameworks have been created to ensure that we are able to identify, measure and effectively manage these risks in all parts of the group before they adversely impact the business. This information, together with the strength of the Group's capital position, allows the Board to set a risk strategy and appetite which sets out the level of risk the Board is prepared to take in the delivery of its strategic objectives.

Operational planning cycle



1. Board sets the business strategy which is incorporated in the three-year operational plan. Risk provide robust challenge of validity and achievability of plan.

2. Risk Strategy creates the overarching principles for establishing a set of indicators (Risk Appetite).

3. Comprehensive policy suite sets the required business processes and controls to deliver the operational plan within appetite. Robust control testing used to identify risks out of appetite.

4. Regional Risk and Control Committees track actions for risks outside of appetite, and escalate to Local & Group Boards.

5. Significant changes in risk assessments are considered by the Internal Model Governance Committee and where appropriate, the Group's internal model is updated.

6. Output from the model is sense checked against non-modelled stress and scenario events to ensure it provides a reliable basis for making business decisions, including capital planning, reinsurance purchase, performance analysis and pricing.

7. The internal model is run regularly throughout the year in order to assess the risks impacting the Group and determines how much capital the Group needs to hold to remain solvent even after a major stress event(s), which forms part of the ORSA process.

8. Output from the model is reported to the Board, so that changes can be made to the three-year operational plan to ensure the Group remains in Appetite. Cycle will continue until the Board is satisfied with the future plan.

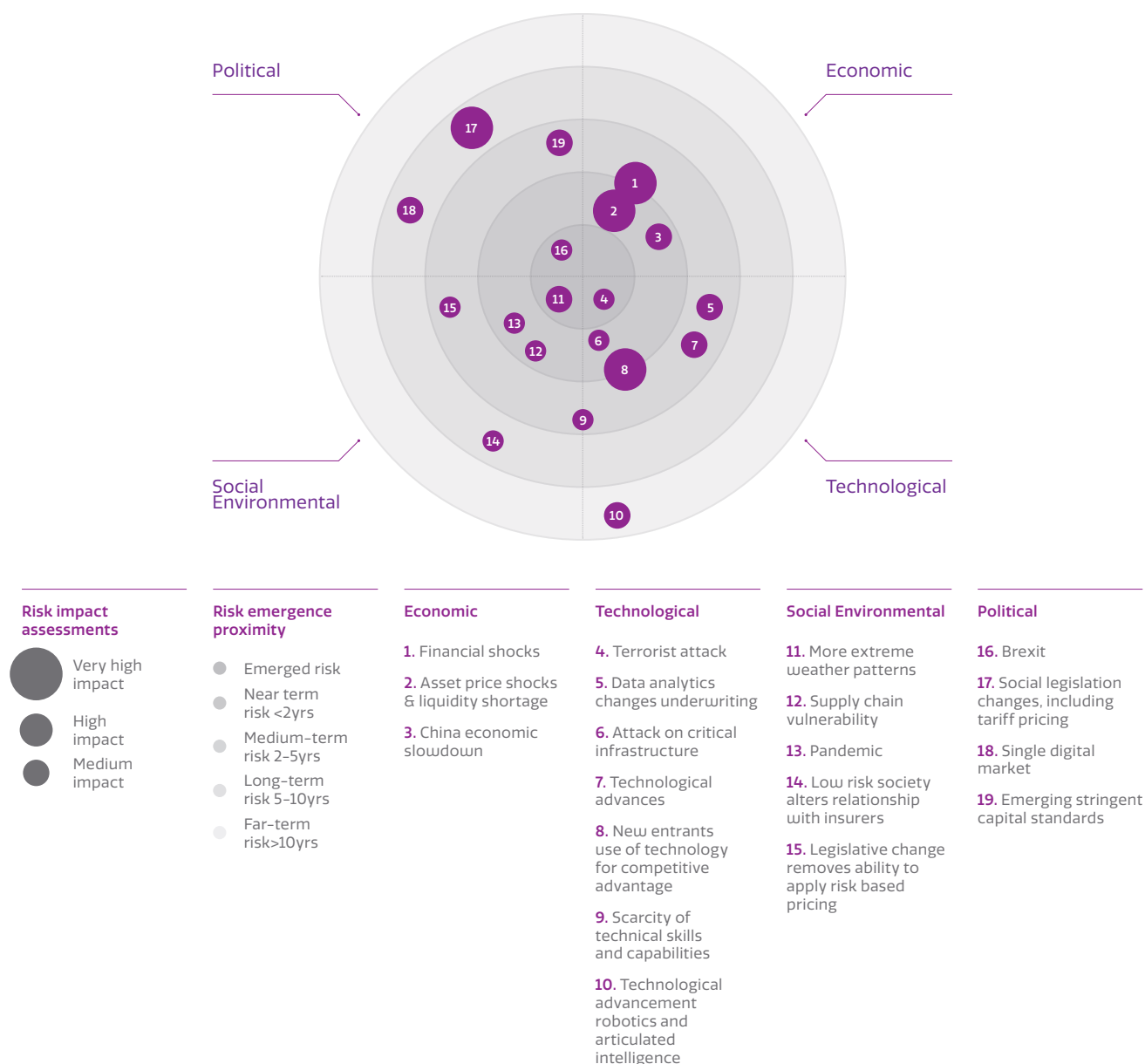
The risk appetite is refreshed at least annually to adapt to the evolving risk, regulatory and economic environment, with an increased focus on ensuring that the Group is adequately prepared for evolving IT risks including cyber-attack. Once set, the business regularly monitors compliance with the appetite, both at a regional and group level, to ensure actions can be rapidly taken to manage any risks considered to be outside of the risk appetite tolerance levels.

Keeping our focus on the road ahead

One of the key roles of the risk team is to ensure that we support the business by keeping abreast of the demands from a dynamic and ever-changing risk environment. At RSA we perform an annual deep-dive assessment of the emerging risks facing the business, which is informed through the use of subject matter experts, thematic brainstorming workshops, consulting a wide range of key external documentation as well as participating in the CRO Forum's emerging risks working group. The emerging risks set out in the diagram below were presented to the Board Risk

Committee for consideration and a decision on which risks should be subject to further deep-dive reviews including performance of appropriate scenario analysis. The results from these reviews satisfied the Board Risk Committee that the Group's risks and controls frameworks were overall effective at managing future threats to the business although it did highlight areas where further refinements could be made, including expanding the scope of our horizon scanning to keep abreast of new entrant and technological advancements.

Emerging risk analysis – Board Risk Committee April 2016



Risk management – continued

Key risks and mitigants

| Key risk and exposures | SII SCR % | Key mitigants and controls | Commentary |
|--|-----------|---|--|
| Catastrophe risk Arises from the risk of large natural disasters with our main exposure being to European windstorms and Canadian earthquakes. | 16 | <ul style="list-style-type: none"> Our reinsurance programme significantly reduces our exposure to catastrophe risks with losses arising from the 2016 Canadian wildfires being well covered by our programme. Programme is designed to cover at least 1 in 200 year events. | Consistent with our strategy and appetite of retaining risks that reside within our core expertise, where we are able to maximise risk-adjusted returns, our Solvency II Capital Requirement (SCR) is primarily comprised of insurance-related risks, including higher than anticipated underwriting losses, large retained catastrophe losses and deterioration in our stock of reserves for future claims. |
| Reserving risk Is the risk that the Group's estimate of future claims is insufficient. Longer tail line of business present more uncertainty on the size and timing of payments, with our key exposure being the Swedish personal accident lines. | 16 | <ul style="list-style-type: none"> Reserves are reviewed and challenged at the Group Reserving Committee which is attended by the Group Chief Actuary, the CRO, CFO and CEO. Group has implemented a comprehensive reserve assurance programme which has independently verified >90 percent of the Group's net reserves by value over a three year period. Economic transfer of the UK legacy insurance liabilities, effective at 31 December 2016. | Whilst our investment strategy remains deliberately conservative we continue to look for opportunities to increase returns through the purchase of less liquid high-quality assets as we are able to match the cashflow profile against that of our liabilities. |
| Underwriting and claims risk This is the risk that underwritten business is less profitable than planned due to insufficient pricing and setting of claims case reserves. Key exposures arise from large portfolios where claims trends are slow to emerge such as UK Commercial and Marine. | 14 | <ul style="list-style-type: none"> Controlled through well-defined risk appetite statements which are rigorously monitored at quarterly portfolio reviews, with remediation actions taken where deemed necessary. Claims case reserves are prudently set and reviewed at quarterly case reserving committees. Extensive control validation and assurance activities performed – with over 100 separate assurance reviews having been performed. | Another key SCR risk arises from the Group's defined benefit pension schemes. Although these schemes are well funded (95 percent per latest triennial review). Under the Solvency II rules we are required to hold sufficient capital to withstand a 1 in 200 year event. For more information on the pension schemes see note 37 of the financial statements. |
| Market, credit and currency risk Is the risk to our insurance funds arising from movements in macroeconomic variables including widening credit spreads, declining bond yields or currency fluctuations, the latter having been significantly impacted post Brexit. | 18 | <ul style="list-style-type: none"> RSA adopts a prudent investment strategy with the investment portfolio favouring high-quality fixed income bonds, which are closely duration and currency matched with insurance liabilities to hedge volatility. Investment positions are regularly monitored to ensure limits remain within appetite. | |
| Pension risk We face longevity and in particular market related risks which arise from our defined benefit pension schemes. The largest exposures arise from credit spread and equity movements, although these are partly hedged by offsetting movements in the Insurance Investment Fund. | 26 | <ul style="list-style-type: none"> Funding assets are well matched to liabilities in the pension schemes, including the use of swap arrangements. Reduced more volatile growth assets exposures from c.25 percent to c.15 percent in the year. Reaching a concluding agreement to close the UK schemes to further accrual from 31 March 2017. RSA continues to work with the Trustees in order to further explore options to de-risk the pension funds. | |
| Operational risk These risks relate to customer and/or reputational damage arising from operational failures such as IT system failure. | 10 | <ul style="list-style-type: none"> Extensive Line 1,2 & 3 challenge over the progress made in executing the Group's transformation programme. Significant progress in clearly articulating IT risk appetite and getting remediation plans and enhanced control testing under way. Extensive control review and testing with >500 control gaps closed in the year. | |

Risk culture

In our view the most important component to effectively embedding the Group's risk management framework is ensuring that senior management set the right 'tone from the top'. At RSA the senior management team have remained committed to instilling a culture which promotes openness, honesty, integrity and ethical behaviour, which is further underpinned by the Group's continued focus on our quarterly cultural health check.

A key part of our culture is ensuring that our customers are at the heart of all we do, and our staff are passionate about providing brilliant service to our customers. For example, in our UK business we have embedded a Conduct Framework which identifies and addresses conduct risks appropriately, considers the customer impact of decisions we take, and ensures that our customers receive good outcomes.

Risk management in action

As the business has continued to leverage technology to deliver a more efficient customer offering the risk team have provided significant support to the business to ensure risks arising through the increased automation and digitalisation of processes remain transparent and controllable throughout transformation.

- The first step to implementing an appropriate risk and control framework is to identify the key IT risks which can arise with the key focus being on the risks that have the highest impact and likelihood of occurrence.
- The risk team supported the business in evaluating the risks arising and helped prioritise resolution plans which focused on the most significant risks, including ensuring that resourcing needs had been appropriately allowed for in the Group's operating plan.
- All risk assessments together with resolution plans were presented to the Board Risk Committee for approval to ensure remediation plans were considered sufficient to bring risks within appetite.
- Monitoring of these risks will be performed through both a set of key risk indicators which are linked to the risks and provide an early warning if risks have moved outside of appetite as well as the development of line 1 and line 2 control testing frameworks which focus on testing the key controls.

Risk developments in 2016

Transformation risks – the risk teams have supported the business to ensure appropriate level of control and governance over the transformational changes being implemented by the Group. This includes ensuring there is appropriate control over the planning, testing and implementation stages of the programme as well as taking an active role in providing high levels of scrutiny and challenge at the regional and group transformation steering committees.

Delivery of the operating plan – The Group's operating plan provides the platform for ensuring the business remains focused on achieving its key operational and strategic goals, including delivery of profitable growth whilst maintaining a robust capital base. It is therefore essential the plan meets the right balance of achievable stretch targets with realistic assumptions and strategic actions for how this can be achieved. Risk take an active role in challenging the plan, including ensuring the validity of assumptions when compared to economic projections, peer reviews, past experience and current risk assessments, which delivery of planned transformation activity.

Pension de-risking – The Group has continued to explore opportunities for further reducing the volatility created by our pension scheme exposures, including reducing our more volatile growth asset exposures from c.25 percent to c.15 percent in the year and reaching a concluding agreement to close the UK schemes to further accrual from 31 March 2017.

Management of peripheral businesses – There has been an increased focus in strengthening the control frameworks of the Group's peripheral businesses, with all businesses having been subjected to a detailed assessment.

IT risk monitoring framework

The Group has developed an IT risk monitoring framework which links key IT risks to a set of key risk indicators. This provides management with feedback on the effectiveness of the IT control framework, which has been strengthened through the appointment of Regional Chief Information Security Officers (CISO), enhancing their teams and developing robust control frameworks and remediation plans which are in progress.

UK Legacy disposal – as described on page 33, the Group materially reduced long-tail reserve risk through the economic transfer of £834m of undiscounted UK legacy liabilities net of reinsurance.

Solvency II and Solvency Capital Requirement (SCR)

Solvency II is the new EU-wide insurance regulatory regime that became effective on 1 January 2016.

One of the key aims of Solvency II is to introduce a harmonised prudential framework for insurers promoting transparency, comparability and competitiveness amongst European insurers.

The Directive has three pillars that have impacted how RSA manages risk and how it reports to both regulators and shareholders: Pillar one relates to the quantitative requirements and introduces a risk-based methodology to calculating the Group's Solvency Capital Requirement (SCR). Insurers are required to calculate the level of capital required based on their unique risk profile. For RSA this is calculated using our own Internal Model that was approved by the regulator in December 2015.

Pillar two incorporates qualitative governance requirements, including the way the risk management function operates within the business and how key systems and controls are documented and reviewed.

Pillar three relates to enhanced and standardised disclosure requirements, including increased transparency of the risk strategy and risk appetite of the business. In 2017, RSA will publish its first 'Solvency & Financial Condition Report'; these will contain extensive information on how RSA manages its risks and exposures and report on the financial position of the company using Solvency II valuation principles.

Brexit

RSA has been actively monitoring the impact of the referendum result and the potential impact on RSA's business. The vast majority of business written within the '27 remaining countries' of the EU is written by subsidiaries domiciled in these countries. Plans are being evaluated for creating an appropriate structure for the remaining business written through branches of our main UK entity.

Chairman's governance letter



Over the past three years, the Board has worked to strengthen and enhance the effectiveness, skills and experience of the Board to align with the Group's strategy.

Martin A. Scicluna
Chairman

2016 AGM

25
Resolutions passed

At least
93%
of votes cast 'For' each resolution



For more information regarding the 2017 AGM see page 60

Throughout 2016, the Board has continued to focus on strengthening and enhancing its effectiveness to ensure promotion of the success of the business for the benefit of RSA's stakeholders.

Leadership

During the year, we have welcomed two new non-executive directors who bring a wealth of insurance and financial services experience to the Board. Martin Strobel joined the Board on 1 May 2016 bringing with him over 23 years' insurance and financial services experience, most recently as Chief Executive Officer of Baloise Group. Isabel Hudson joined the Board on 1 August 2016 bringing significant experience in general insurance and wide-ranging commercial, corporate finance and business development experience together with relevant board experience as an executive and non-executive director on the boards of a number of listed companies.

These appointments have enabled us to leverage further industry experience and commercial knowledge to help ensure that RSA continues to deliver value for its customers and shareholders while advancing its operational priorities. Full details of Martin and Isabel's experience can be found in their profiles on page 45. Following these appointments, the composition of the Board is 73 percent male and 27 percent female.

Johanna Waterous has informed the Board that she will retire as a director with effect from the Company's AGM on 5 May 2017. I would like to thank her for her significant contribution to the Board. With effect from 5 May 2017, Isabel Hudson will succeed Johanna Waterous as Senior Independent Director.

Effectiveness

Over the past three years and following the external Board evaluation in 2013, the Board has worked to strengthen and enhance its effectiveness, skills and experience. In 2014 and 2015, I undertook internal Board evaluations to ensure progress against the actions identified and to assess the Board's continued effectiveness to align with the Group's strategy. Further detail on the Board's journey over the past three years can be found on pages 54 and 55.

In compliance with the UK Corporate Governance Code, an external Board evaluation was undertaken in 2016. The results of the evaluation concluded that, over the previous three years, the Board had made meaningful progress building on its strengths, and was demonstrating significant improvement in its effectiveness and ability to add value. Full details of the 2016 Board evaluation can be found on page 53.

Accountability

The Board believes that disclosures made in respect of the Group's position and prospects are fair, balanced and understandable and that the delivery of the Company's objectives is being undertaken with the best interests of stakeholders in mind. The Company's Viability Statement is set out on page 63.

Work undertaken over the past three years to enhance the effectiveness of the Group's System of Governance is now embedded into our business as usual processes.

During the year the Board paid close attention to the expectations of the Prudential Regulatory Authority (PRA) and the Financial Conduct Authority (FCA) with particular focus on embedding the obligations of the Group under the Solvency II regime, and on conduct matters.

During 2016, the Company has complied with all of the Principles and Provisions of the UK Corporate Governance Code and this is evidenced throughout the Directors' and Corporate Governance Report.

Code Provision B.1.1 requires the Board to identify whether each of the non-executive directors is independent. Isabel Hudson has a pre-existing entitlement to a deferred pension from one of the Group's defined benefit pension schemes. This entitlement relates to a previous employment with Royal Insurance which ended in 1993 and is unaffected by her appointment as a non-executive director. The Board determined, taking into account a number of factors including the size of the pension benefit and its relative immateriality to her overall retirement planning, that Isabel Hudson, upon appointment, was independent notwithstanding this and the Board considers that her pension entitlement in no way compromises her independence of character and judgement. Neither the Company, nor Isabel has made contributions to the Scheme to secure additional pension benefits since she left in 1993. Discussions were held with major shareholders who indicated they were supportive of Isabel's appointment despite her membership of the pension scheme.

Remuneration

The Directors' Remuneration Policy (the Policy) is due for approval at the 2017 Annual General Meeting (AGM), having last been approved by shareholders at the 2014 AGM. The Policy has been reviewed during the year by the Group Remuneration Committee and a shareholder consultation has been undertaken to understand views which support the conclusions reached. The Group Remuneration Committee concluded that the Policy remains aligned to Group strategy and shareholder interests and no substantive changes are proposed. The Policy is set out on pages 80 to 87.

Engagement

The Board is committed to transparent disclosure and engagement with the Group's stakeholders. Throughout the year, senior management have actively engaged with employees, shareholders, regulators and other stakeholders on relevant matters. A pensions consultation process has been undertaken with employees and unions during the period with a view to changing pension and redundancy terms.

During the year, nearly 400 meetings were held with institutional investors focusing on the future performance potential of the Group, capital foundation and future capacity for capital return to shareholders.

Further information relating to stakeholder engagement is included on pages 58 to 62.

Conclusion

I would like to thank the Board and employees for their contribution and commitment throughout the year, which is fundamental in ensuring the Board delivers on shareholder value.



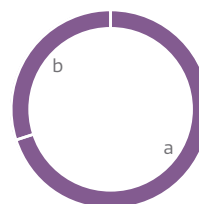
Martin A. Scicluna

Chairman

22 February 2017

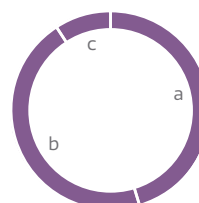
Diversity of the Board

- a. Male 73%
- b. Female 27%



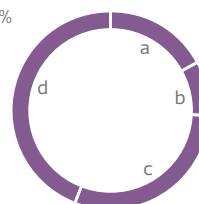
Board Tenure

- a. 0 to 3 years 45.5%
- b. 3 to 6 years 45.5%
- c. 6 to 9 years 9%



Board Experience

- a. Insurance Industry 17%
- b. Business Development 9%
- c. International 30%
- d. Financial Services 44%



Directors' and Corporate Governance Report

| | |
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Board of Directors

Board of Directors

Committee member key

- A** Group Audit Committee
B Board Risk Committee
I Group Investment Committee
N Group Nomination and Governance Committee
R Group Remuneration Committee

- Chair of Committee
 ● Member of Committee



Martin Scicluna

Role
 Chairman
 Appointment date
 January 2013
 Nationality
 British



Martin has considerable Board experience, knowledge and understanding of the financial services sector. Previous roles include Non-Executive Director and Chairman of the Audit Committee at Lloyds Banking Group plc, 34 years at Deloitte LLP, 26 years of which as Partner, Chairman of Deloitte LLP from 1995 to 2007, Director, Deloitte Touche Tohmatsu from 1999 to 2007 and membership of the Financial Services Trade and Investment Board from 2013 to 2015.

External appointments: Chairman of Great Portland Estates plc and Senior Independent Director and Chairman of the Audit Committee of Worldpay Group plc.



Stephen Hester

Role
 Group Chief Executive
 Appointment date
 February 2014
 Nationality
 British



Stephen was previously Chief Executive Officer of The Royal Bank of Scotland Group plc, 2008-13, where he led the largest ever corporate restructuring and recovery programme. Prior to that he held positions as Chief Executive, British Land plc from 2004 to 2008, Chief Operating Officer, Abbey National plc and a number of senior roles at Credit Suisse First Boston in London and New York. Stephen has over 30 years' experience in financial services and FTSE 100 companies with expertise in transforming the performance of businesses.

External appointments: Senior Independent Director of Centrica plc.



Scott Egan

Role
 Group Chief Financial Officer
 Appointment date
 October 2015
 Nationality
 British



Before RSA, Scott was Interim Chief Executive Officer at Towergate Insurance having previously held the post of Chief Financial Officer. Scott also held the post of Chief Financial Officer at Brit Insurance, after four years at Zurich Financial Services, as Chief Financial Officer UK, and latterly as Group Financial Controller. He has also held various senior finance roles at Norwich Union Insurance (now Aviva). Scott is a qualified accountant (ACMA) and has an MBA from Cranfield University.

External appointments: None



Alastair Barbour

Role
 Independent Non-Executive Director
 Appointment date
 October 2011
 Nationality
 British



Alastair retired from KPMG in March 2011. In the last 20 years of his 36 year career with the firm, in the UK and overseas, he led their financial services team in Scotland with a primary focus on insurance and investment management. Alastair has extensive experience in advising on accounting and financial reporting, corporate governance and management issues in the financial sector and is a Fellow of the Institute of Chartered Accountants in England and Wales.

External appointments: Non-Executive Director of Phoenix Group Holdings, Standard Life Private Equity Trust PLC, Liontrust Asset Management plc, CATCo Reinsurance Opportunities Fund Limited and The Bank of N.T. Butterfield & Son Limited (a company listed in Bermuda and New York).



Kath Cates

Role
 Independent Non-Executive Director
 Appointment date
 September 2013
 Nationality
 British



Kath has over 25 years' experience in global financial services. She was previously Chief Operating Officer, Wholesale Banking for Standard Chartered Bank and spent 22 years at UBS. Kath has gained a deep knowledge of control, governance and risk management, working in emerging markets and across different sectors and cultures.

External appointments: Senior Independent Director of Brewin Dolphin Holdings plc, Non-Executive Director of Threadneedle Investment Services Limited and Threadneedle Asset Management Holdings Sàrl.



**Enrico
Cucchiani**

Role
Independent
Non-Executive
Director

Appointment date
December 2014

Nationality
Italian



Enrico has over 35 years' global executive and non-executive experience across financial services including banking and insurance and a number of blue chip brands. He spent over 15 years at Allianz in a variety of international roles, including Head of Global P&C and Head of most of Europe, Latin America and Africa.

External appointments: Partner of Think Global Investments LLP and Non-Executive Director at Piraeus Bank SA.



**Isabel
Hudson**

Role
Independent
Non-Executive
Director

Appointment date
August 2016

Nationality
British



Isabel has significant experience in general insurance, both as an executive and non-executive director, along with a wealth of relevant board experience having served as committee member and committee Chairman of a number of listed companies including Standard Life plc and QBE Insurance Group Ltd, as well as The Pension Regulator. Her previous roles include Executive Director of Prudential's UK business and Chairman of Prudential International Assurance between 2002 and 2006, Chief Executive of specialised pension buyout firm Synesis Life, Chief Financial Officer of Eureko and International Development Director for GE Insurance Holdings Limited.

External appointments: Chairman of National House Building Council, Non-Executive Director of BT Group plc and Non-Executive Director of Phoenix Group Holdings.



**Hugh
Mitchell**

Role
Independent
Non-Executive
Director

Appointment date
September 2012

Nationality
British



Until 31 December 2015, Chief Human Resources and Corporate Officer of Royal Dutch Shell plc, and a member of the Shell Executive Committee. Formerly a Director of Shell International Limited, Shell Aircraft Limited and the Shell Foundation.

Advisory roles previously held at The Centre for Advanced Human Resources at Cornell University Advisory Board, IMD Business School Advisory Board in Lausanne, an Honorary Vice-President for the CIPD (UK) and Advisory Board Member of the National College for School Leadership (England and Wales).

External appointments: Currently a Fellow of the National Academy of Human Resources in the USA and a Board Member of Edinburgh Business School.



**Joseph
Streppel**

Role
Independent
Non-Executive
Director

Appointment date
October 2011

Nationality
Dutch



Joseph has a comprehensive understanding of the insurance market globally, extensive financial services expertise and a good knowledge of international and emerging markets. Previous roles include Chief Financial Officer of Aegon until 2009 and Chairman of the Monitoring Committee of the Dutch Corporate Governance Code.

External appointments: Vice-Chairman of Van Lanschot, a Dutch private banking and asset management firm, Director of Arq Foundation, Chairman of Duisenberg School of Finance, Chairman of the Advisory Board of the Royal Dutch Society of Actuaries and Chairman of Leaseplan Corporation.



**Martin
Strobel**

Role
Independent
Non-Executive
Director

Appointment date
May 2016

Nationality
Swiss



Most recently Chief Executive Officer of Baloise Group, a position he held for seven years to 2015. He joined Baloise Group in 1999 as the Head of IT at Basler Switzerland and, within Baloise Group, was responsible for major cross-functional insurance and finance projects. From 2003-08, he was a member of the Corporate Executive Committee with responsibility for the Corporate Division Switzerland. From 1993 to 1999, Martin performed various roles at Boston Consulting Group, Düsseldorf, advising business in the banking and insurance sectors.

External appointments: None.



**Johanna
Waterous CBE**

Role
Senior Independent
Non-Executive
Director

Appointment date
May 2008

Nationality
Canadian



Johanna's previous roles include Senior Independent Director of Rexam plc, Non-Executive Director of Morrisons plc, Chairman of Tate Enterprises and over 20 years with McKinsey & Company, positions including Co-leader of the Global Marketing and Sales Practice and Leader of their UK Consumer Practice and the European Retail Practice. She is also a former Director of Shoppers Drug Mart Corporation (a company listed on the Toronto Stock Exchange).

External appointments: Trustee of the Foundation & Friends of RBG Kew Foundation and Director of RBG Kew Enterprises.

Corporate Governance

Executive Committee

Executive Committee

The Executive Committee comprises Stephen Hester and Scott Egan, Executive Directors of the Group Board, and the senior management set out below.

During the year, certain changes to the Executive Committee have occurred with the departure of Derek Walsh, General Counsel and Group Company Secretary in February 2016, Rowan Saunders, President and CEO of RSA Canada in July 2016 and Paul Whittaker, Chief Operating Officer in September 2016. In addition, David Coughlan made an internal move to the UK & International Executive Team to become Personal Lines Director.

The Board focuses on management succession planning and was pleased to promote internal candidates to the Executive Committee: Charlotte Heiss as Group Chief Legal Officer and Company Secretary, Nathan Williams as Group Underwriting Director and Martin Thompson as President and CEO of RSA Canada. In January 2017, Cathy Lewis joined the executive team as Group HR Director.

Biographical details for the individuals fulfilling these roles can be found at www.rsagroup.com/thegroupecutive.



Patrick Bergander
CEO RSA Scandinavia



Ralph Daals
Group Chief Auditor



Charlotte Heiss
Group Chief Legal Officer and Company Secretary



Cathy Lewis
Group HR Director



Stephen Lewis
Chief Executive, UK & International



William McDonnell
Group Chief Risk Officer



Darren Price
Group Chief Information Officer



Martin Thompson
President and CEO RSA Canada



Nathan Williams
Group Underwriting Director

Leadership

Directors

The names of the directors, together with their biographical and committee membership details are set out on pages 44 and 45. Martin Strobel and Isabel Hudson were appointed as Independent Non-Executive Directors on 1 May 2016 and 1 August 2016 respectively.

Johanna Waterous will retire as a director with effect from the AGM on 5 May 2017. With effect from 5 May 2017, Isabel Hudson will succeed Johanna Waterous as Senior Independent Director.

The Company's Articles of Association authorise the Board to manage the business of the Company and give the directors power to appoint and replace directors as required until the next AGM. Directors are nominated by the Group Nomination and Governance Committee and are subsequently approved by the Board for election or re-election annually by shareholders at the Company's AGM. Non-executive directors are initially appointed for a three-year term with an expectation that they will continue for at least a further three years.

Details of the directors' service contracts and terms of appointment, together with their interests in the Company's shares, are shown in the Directors' Remuneration Report on pages 76 to 101 and are incorporated into this Report by reference.

In accordance with the UK Corporate Governance Code, the Board believes that it has the appropriate balance of skills, experience, independence and knowledge to enable it and its committees to discharge their duties and responsibilities effectively. The Board is satisfied that it is of a size appropriate to the needs of the business and that no individual or small group of directors can dominate the Board's decision-making.

One of the key responsibilities of the Group Nomination and Governance Committee is to keep under review Board membership, succession planning and diversity to ensure the balance remains appropriate. A review was undertaken during the course of the year. Further details of the work of this committee can be found on pages 66 to 67.



Women in Leadership event in Peterborough

Diversity

The Group is committed to diversity and the promotion of equal opportunities. We recognise the importance of diversity to the effectiveness of the Board and remain committed to maintaining the Davies Report recommendation of a minimum of 25 percent representation of females on the Board. The Board composition is currently 73 percent male and 27 percent female. The Group continues to invest in strengthening its pipeline of female employees for senior leadership positions to ensure progress towards this target and has developed a framework of initiatives designed to help retain, develop and promote our female employees and improve diversity and inclusion more broadly. These include mentoring schemes (including the 30% club cross-company scheme), recruitment initiatives, development courses and a variety of other initiatives designed both to support our people and help ensure objectivity within our processes.

During 2016, female members of the Board and senior management held Women in Leadership meetings giving employees the opportunity to meet senior female leaders of the business to discuss their careers.

When appointing new directors, regard is given to the size of the Board, the balance of executive and non-executive directors and the benefits of diversity, including gender.

The Board is aware of the proposals of the Parker Report on ethnic diversity and is awaiting publication of the final report following the consultation.

Corporate Governance – continued

Role Statements

No one individual has unfettered powers of decision making. The roles of the Chairman and Group Chief Executive are separate and clearly differentiated through role statements, which are approved by the Board annually, along with role statements for the Senior Independent Director and non-executive directors.

The Chairman is responsible for the leadership and effectiveness of the Board including the conduct at Board meetings. He promotes a culture of openness and debate ensuring effective decision-making and the provision of timely, accurate and clear information. The Chairman ensures that relevant objectives are established for the Group Chief Executive and his executive team, reviewing the overall management performance of the Company and senior management with the Group Chief Executive. The Chairman takes on the role of ambassador for the Company, participating in the engagement of and effective communication with the Company's stakeholders.

The Group Chief Executive is responsible for identifying and developing business opportunities, recommending actions to the Board with particular attention on strategic plans, risk appetite and risk exposure for the business, monitoring the performance of the Group and overseeing the delivery of objectives and business plans within agreed timescales and budget. The Group Chief Executive develops targets and goals for his executive team and ensures succession plans for senior management are in place. He represents the Company at industry events and develops the Company's communications strategy to meet the needs of and engage with all internal and external stakeholders.

The Senior Independent Director supports the Chairman in the delivery of his responsibilities as required, ensuring the views of each of the non-executive directors are given due consideration and facilitating communication between the non-executive directors and the Chairman. The Senior Independent Director holds meetings with the non-executive directors without the Chairman being present to review the Chairman's performance as part of the internal Board evaluation process and chairs the Group Nomination and Governance Committee when considering matters relating to the Chairman of the Board.

The role of the non-executive directors is to challenge and approve the Group's strategy and to assess and challenge performance against business plans, bringing an independent, objective view to the discussion. Each of the non-executive directors is a member of one or more committees for which they have the skills, knowledge and expertise required to consider topics delegated for in-depth assessment. They meet with the Chairman without the executive directors being present and meet with the Senior Independent Director without the Chairman being present to review the Chairman's performance and discuss other matters. Each committee is chaired by a non-executive director who has the specialism and experience in the relevant field.

The role of the Group Chief Legal Officer and Company Secretary (Company Secretary) is to support the Chairman and the Board. The role of the Company Secretary includes bringing all governance matters to the attention of the Board and delivering a programme of Board and committee meetings, trainings, induction programmes and senior management presentations to ensure that each director has the information required to discharge his or her statutory duties. The Company Secretary ensures that papers are produced to a high standard and in a timely manner which are circulated to directors a week in advance of any meeting. The directors have access to the services and advice of the Company Secretary, and may take independent professional advice at the expense of the Company in the furtherance of their duties.

Further information on the individuals fulfilling these roles can be found in their biographies on pages 44 to 46 and on www.rsagroup.com/thegroupexecutive.

Board Committee Structure and Membership

The Board delegates certain duties to its committees so that matters receive detailed consideration. Terms of reference for each committee detail the authority delegated from the Board, and these have been reviewed by each committee and approved by the Board during 2016. Terms of reference are available to view at www.rsagroup.com/termsofreference. Details of each of the committee's activities and priorities during 2016 are contained in the committee reports on pages 65 to 101 which are incorporated into this Report by reference.

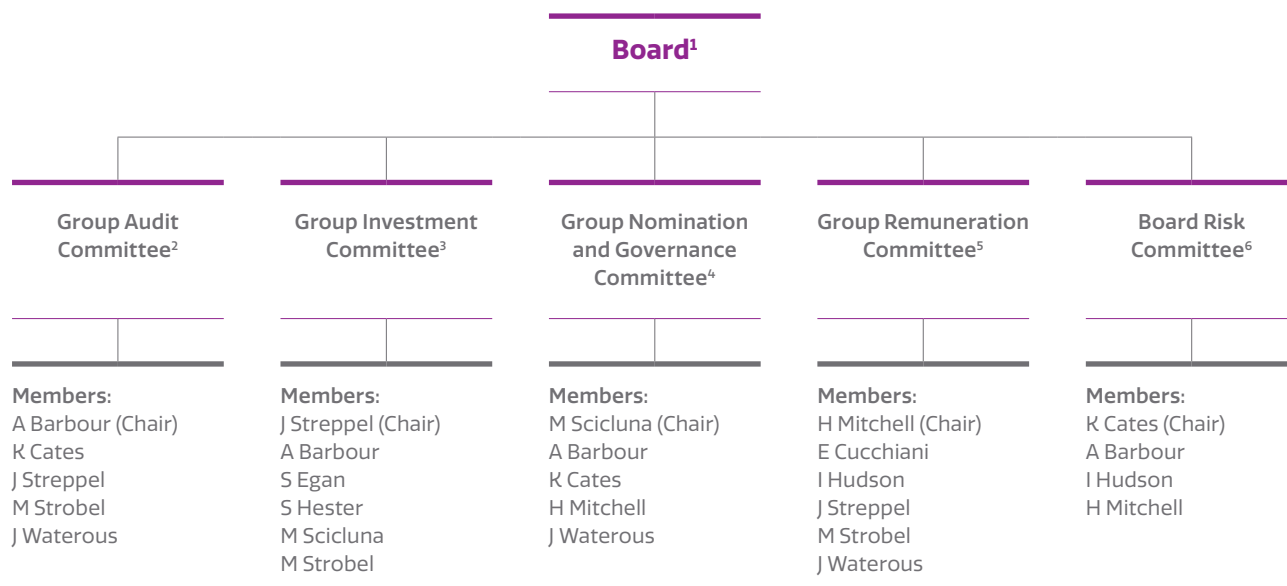
The composition of each committee is reviewed by the Group Nomination and Governance Committee annually and additionally when there is a change to the Board. Consideration is given to each individual's expertise and experience with a view to cross-committee membership to raise awareness of each committee's work and focus. In addition, the Chair of the Board Risk Committee attends the Remuneration Committee when risk matters are discussed.

Following each committee meeting, a verbal update is presented to the Board ensuring that all directors are aware of relevant topics and specific matters.

Upon appointment, non-executive directors are invited to attend each Board committee as part of their induction programme to familiarise themselves with the remit of the committee and matters discussed.

The diagram opposite shows the Group's Board-level committees and their current composition.

The key functions of Risk, Actuarial, Compliance and Internal Audit all report directly to a Board committee providing expert advice on their remits to the relevant committee and senior management.



Details of current directors, together with their biographical and committee membership details, are set out on pages 44 to 45.

Attendance at Board and Committee Meetings

Attendance at Board and Committee Meetings held during 2016 is shown in the table below.

| | Scheduled Group Boards | Additional Boards | Group Audit Committee ² | Group Nomination and Governance Committee ⁴ | Group Remuneration Committee ⁵ | Group Investment Committee ³ | Board Risk Committee ⁶ |
|------------------|------------------------|-------------------|------------------------------------|--|---|---|-----------------------------------|
| Martin Scicluna | 9/9 | 5/5 | | 5/5 | | 2/2 | 2/2 |
| Stephen Hester | 9/9 | 5/5 | | | | 2/2 | |
| Scott Egan | 9/9 | 5/5 | | | | 1/2 | |
| Alastair Barbour | 9/9 | 3/5 | 6/6 | 5/5 | | 2/2 | 4/4 |
| Kath Cates | 9/9 | 3/5 | 6/6 | 3/3 | 3/3 | | 4/4 |
| Enrico Cucchiani | 9/9 | 4/5 | | | 6/6 | | 2/2 |
| Isabel Hudson | 4/4 | 2/2 | | | 1/1 | | 2/2 |
| Hugh Mitchell | 9/9 | 4/5 | | 5/5 | 6/6 | | 4/4 |
| Joseph Streppel | 9/9 | 5/5 | 6/6 | | 6/6 | 2/2 | |
| Martin Strobel | 6/6 | 4/4 | 4/4 | | 4/4 | 1/1 | |
| Johanna Waterous | 9/9 | 4/5 | 6/6 | 5/5 | 6/6 | | |

Notes:

- For the composition of the Board, please refer to pages 44 to 45.
- Group Audit Committee: Martin Strobel joined the Committee on 1 May 2016. Regular attendees: Group CFO, Group Chief Auditor, Group & UK Regulatory Compliance Director, Group Chief Risk Officer, Group Chief Legal Officer and Company Secretary and representatives from the External Auditor. The Chairman attends ahead of RSA's full and half-year results.
- Group Investment Committee: Martin Strobel joined the Committee on 1 May 2016. Regular attendees: Group Investments Director and Group Chief Legal Officer and Company Secretary.
- Group Nomination & Governance Committee: Kath Cates joined the Committee on 1 March 2016. Regular attendees: Group CEO and Group Chief Legal Officer and Company Secretary.
- Group Remuneration Committee: Martin Strobel joined the Committee on 1 May 2016. Kath Cates ceased to be a member on 1 July 2016. Isabel Hudson joined the Committee on 1 November 2016. Regular attendees: Chairman, Group CEO, Group Chief Legal Officer and Company Secretary, Group HR Director and PWC as independent advisers to the Committee.
- Board Risk Committee: Enrico Cucchiani and Martin Scicluna ceased to be members of the Committee on 1 July 2016. Isabel Hudson joined the Committee on 1 August 2016. Regular attendees: Chairman, Group CFO, Group Chief Legal Officer and Company Secretary, Group & UK Regulatory Compliance Director and Group Underwriting Director.

Effectiveness

Role of the Board

The Board is responsible for the overall strategy of the Group and together with the Company is committed to becoming best in class. The Company has continued progress towards this ambition delivering many improvements and efficiencies across customer service, underwriting effectiveness and in respect of costs. The Board's role in the delivery of this ambition is the oversight and challenge of the operations.

The primary responsibility of the Board is to provide effective leadership to ensure that it promotes the success of the Company for the benefit of its members as a whole. The Board, supported by its committees, provides entrepreneurial leadership within a framework of prudent and effective controls. The Board is accountable to stakeholders for the creation and delivery of strong sustainable performance and the creation of long-term shareholder value.

The Board has adopted a schedule of matters reserved for the Board which is reviewed on an annual basis and updated as necessary. The Board sets annual objectives for the business in line with the current Group strategy and monitors achievement against these objectives through regular reports. These include updates from the Group CEO, the Group CFO and other relevant members of senior management or executives on all material business matters.

The directors may exercise all the powers of the Company subject to the Articles of Association, relevant law and any directions that may be given by the Company at general meetings by shareholder resolution.

Key activities of the Board during 2016

Throughout the year, the Board and its committees have focused on four key areas: strategy and growth, risk management and internal control, financial performance and governance, ensuring that a broad range of matters are considered and sufficient time is spent on these areas.

Following the implementation of Solvency II on 1 January 2016, the Board, Audit and Risk Committees are required to monitor regulatory capital measures and the delivery of additional reporting to the Prudential Regulation Authority (Regulator).

The Board has spent time in the business both collectively and as individuals, delving into specific business areas through presentations and meetings, dialogue with management and regional visits to take a closer look at and gain a better understanding of the operational side of the business. During 2016 the Board visited a Personal Lines contact centre in Peterborough to gain a better understanding of customer experiences and also met with some of the Group's Affinity partners with whom the Group carries out business.



Board visit to Peterborough Contact Centre

The Board also visited the Canadian business and attended Canadian management presentations and met with employees and local brokers to gain a deeper understanding of the Canadian business. The Board held a Board meeting during its visit and took the opportunity to meet with the Canadian Regulator, management teams in the business and directors attended regional committee meetings.

Effectiveness of the Board

The Board considers that the information provided to the Board and its committees is supplied in a timely manner and is of an appropriate quality to enable it to discharge its duties. The Board continually challenges management to ensure that the flow and quality of information to the Board is of a high standard. A review and refresh of Board and committee papers was undertaken during the year and a framework implemented to enhance the information provided to the Board. The Chairman sets the agenda for Board meetings and is responsible for the running of meetings ensuring sufficient time for discussion and constructive challenge. When a director is not available to attend a meeting, his/her views are canvassed by the Chairman prior to the relevant meeting where possible, and the Board informed of their opinions and observations. When considering matters such as the approval of financial statements and large operational contracts, the Board may delegate authority to a Board sub-committee to finalise and approve as required.

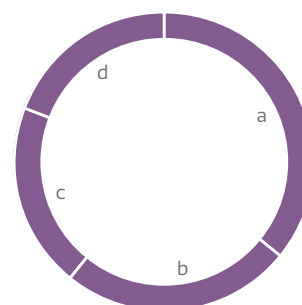
Formal minutes recording the decisions of all Board and committee meetings are prepared and circulated to each director. If a director objects to a particular decision, this is recorded in the minutes of the relevant meeting.

Focus of the Board and committees during 2016

The Chairman, in consultation with the Group Chief Executive and Company Secretary, maintains a rolling agenda of items for consideration by the Board and its committees. This is continually refreshed in line with the needs of the business. Below is a summary of key matters the Board and its committees have focused on during 2016.

Breakdown of topics discussed at Board meetings held during 2016

- a. Strategy and Growth 36%
- b. Financial Performance 25%
- c. Risk Management & Internal Control 20%
- d. Governance 19%



Strategy and Growth

- Overall Group Strategy and strategic business reviews
- Performance against objectives
- Regional and functional updates
- Business transformation
- IT development and strategy
- Business disposals
- Approval of significant business contracts
- Investor feedback and market sentiment.

Financial Performance

- Monthly review of performance
- Formulate Operational Plans and monitor delivery against them
- Financial control framework
- Financial reporting and controls
- Review of capital position
- Solvency II measures and reporting including Internal model
- Reserving
- Review of investment and pension performance: investment strategy and performance, economic and market development and outlook
- External audit plan.

Risk Management and Internal Control

- Group risk appetite
- Risk management system
- Monitoring material business risks: Insurance, financial, reinsurance operational, emerging, capital, Solvency II, conduct, customer, regulatory, FX, pension and IT risk
- Review of risk profiles
- Stress and scenario testing
- Own Risk Solvency Assessment (ORSA)
- Internal controls
- Internal Audit Plan and outcomes
- Group Policy review
- Financial control framework
- Financial reporting and controls
- Financial crime, bribery, money laundering and whistleblowing.

Governance

- Board and committee effectiveness reviews and evaluation
- Board and executive succession planning and associated appointments
- Board composition: balance, experience, skills, independence and diversity
- Director and executive remuneration
- Review of matters reserved for the Board, role statements and committee terms of reference
- System of governance and internal control
- Compliance with UK Corporate Governance Code
- Corporate responsibility
- Legal and regulatory training and updates.

Corporate Governance – continued

Commitment

The Group Nomination and Governance Committee undertakes a review of Directors' time commitment annually. The letters of appointment for the Chairman and each of the non-executive directors set out their anticipated time commitment, being an average of two days per week for the Chairman and 28–32 days per year for non-executive directors. In addition directors are required to allocate sufficient time to meet the expectations of the role, including attending Board and committee meetings, ad hoc meetings, training and briefings with senior management as part of their induction and ongoing development programme and attendance at the Annual General Meeting.

In 2016, the Group Nomination and Governance Committee concluded that the commitment set out in directors' appointment letters remained appropriate, with additional time to be spent in the business as required. During 2016, each of the directors has demonstrated flexibility and commitment by attending Board and committee meetings, some of which were called at short notice, have made themselves available to meet with the Regulator as required, and spent additional time in the business.

Martin Scicluna is also the Chairman of Great Portland Estates plc and Senior Independent Director and Audit Committee Chairman of Worldpay Group plc. The Group Nomination and Governance Committee considered these appointments when considering the Chairman's time commitment.

Stephen Hester was appointed as a Non-Executive Director of Centrica plc on 1 June 2016 and became Senior Independent Director on 1 October 2016. This appointment was considered by the Group Nomination and Governance Committee in respect of Stephen's time commitment and delivery of his duties as Group Chief Executive.

Scott Egan is not currently a director of any other listed companies but would be allowed to have one such appointment, subject to approval from the Group Nomination and Governance Committee.

The Board is satisfied that both Martin's and Stephen's appointments are not a constraint on their time or ability to carry out their duties.

Service agreements and letters of appointment, for all the Executive and Non-Executive Directors, are available for inspection at the Company's registered office and at the AGM.

**Senior Management meetings
included as part of Induction programme**

- Capital
- Claims
- Company Secretarial and Legal
- External Auditor
- HR
- Internal Audit
- Investments
- IT and e-business
- Regulatory Compliance
- Reserving
- Risk
- Underwriting.

Induction, Training and Development

The Chairman, assisted by the Company Secretary, has responsibility for the induction programme, training schedules and professional development of the directors.

The Board receives briefings on matters of importance to the Group. During the year, the Board spent a considerable amount of time outside board meetings, meeting with senior management including those from UK Commercial, UK Personal Lines and various business functions in Canada to enhance business knowledge of specific business areas.

Upon appointment to the Board, directors undertake a tailored induction programme, receiving a broad range of information about the Group. This includes information on the operational performance and business of the Group and details of Board procedures, corporate governance and directors' responsibilities, along with a series of meetings with senior management covering all aspects of the business. In addition each new director is invited to attend each of the Board committees at least once during their induction.

During the year both Martin Strobel and Isabel Hudson undertook bespoke induction programmes which included one-to-one meetings with senior management from all business areas and met with the external auditor.

Directors have attended training sessions and seminars during the course of the year to enhance their knowledge and keep their experience relevant. Each director has an individual training plan which is reviewed by the Chairman. Training themes during the year have included Solvency II, Market Abuse Regulation, Audit Committee updates and risk reporting.



My induction was both tailored and comprehensive, enabling me to understand the operations, strengths and challenges of the Group. The programme included detailed information on the insurance sector and businesses in all the regions where the Group has a presence and the journey for each to progress towards 'best in class'. This has complemented my experience in the European insurance sector and provided a useful platform for my role as a Non-Executive Director.

Martin Strobel
Independent Non-Executive Director



Having previous experience in the insurance industry, the in-depth induction programme gave me an insight into the operations of the Group during which I met with senior management in the business. The programme was tailored to my business experience, and has allowed me to better understand and challenge the business in my non-executive role. As part of my induction I spent time in the UK, Canadian and Scandinavian businesses to better understand their key operations, challenges and risks, along with their contribution to the Group.

Isabel Hudson
Independent Non-Executive Director

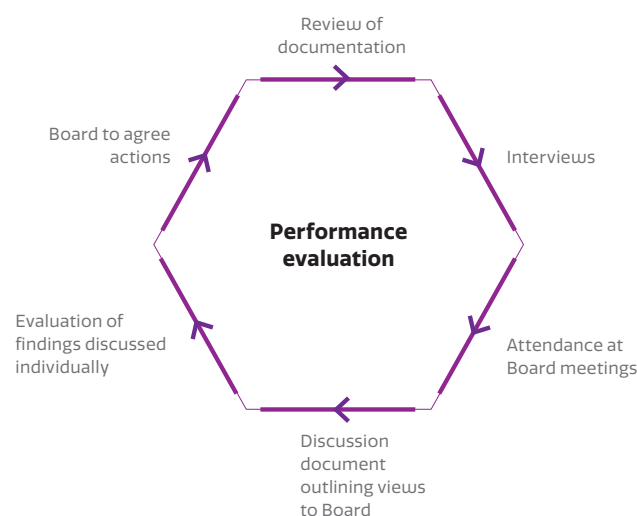
Board Evaluation

To ensure the Board remains effective, and compliant with the UK Corporate Governance Code, a performance evaluation is carried out annually. This is undertaken by an external independent party at least once every three years, with the intervening years run internally. The Chairman leads the internal process with support from both the Senior Independent Director and the Company Secretary, comprising online questionnaires and subsequent meetings. The views of directors and regular attendees to Board meetings are canvassed focusing on key areas identified in the previous year's evaluation and the business during the relevant year. The results from the evaluation are presented to the Board and an action plan developed for the following year. Each year, progress against actions is monitored for progress.

During 2016, an external evaluation was carried out by Boardroom Review Limited (Boardroom Review). Boardroom Review has been providing independent advice to boards to assess their effectiveness since 2004, and undertook the Group's Board evaluation in 2013. The Board felt that Boardroom Review was well placed to assess the progress the Board had made since the last external evaluation in 2013. Boardroom Review has no other connection with the Company.

The evaluation, which was conducted over a number of months, included a detailed review of Board and committee documentation, individual interviews with each of the directors, the Company Secretary, the Chief Risk Officer and the CEO of the UK and International business. Dr Long from Boardroom Review also attended Board and committee meetings as an observer. The review considered Board culture, composition and choreography, use of time and quality of information, strategy, risk and control, leadership

External Performance Evaluation Process



and stakeholders, with a view to providing an independent analysis of strengths and challenges, with priorities and recommendations for 2017 and beyond.

The results of the evaluation concluded that, over the previous three years, the Board had made demonstrable progress building on its strengths, and showed a significant improvement in its effectiveness and ability to add value. The Board and its committees were operating effectively and that there was a positive Board culture which demonstrated values-based leadership. The Board's composition had a good balance of skills, diversity of experience with increased sector expertise and had a good spread of tenure. Board and committee interaction had been enhanced with a mix of formal and informal meetings, including non-executive director only meetings and additional business site visits. Whilst there was a high volume of information provided to the Board, this was aided by a clear determination of matters for discussion and the time dedicated to ensure a combination of presentation and debate by directors.

The main priorities identified were:

- to consolidate focus on longer-term strategy in preparation for the completion of the transformation of the Company.
- to focus on embedding the cultural transformation and executive succession planning at all levels.

It was acknowledged that continuing to build on the existing knowledge and skills remained an important focus, with particular attention to technology, customer understanding and a geographical relevance aligned to the business operations.

Board Evaluation

Three-Year Journey

2013

External evaluation by independent consultants: review of information provided to Board and committees, individual Board member interviews, attendance at meetings as observer, and report findings to the Board

The Board has used the results of internal and external evaluations to identify areas for focus and, over the past three years, has made enhancements to its effectiveness



Personal Lines 'deep dive' at Peterborough

Long-term vision

A greater emphasis on and refinement of the longer-term strategy and vision of the Group, with additional focus on the risks emerging from culture and strategy.

Progress

Introduction of an annual two-day strategy meetings in addition to regional business updates. Recent focus on developing trends, including the digital market, and business transformation over the longer term with a view to achieving best in class. Risk reviews are undertaken against culture and transformation, along with the development of a Culture Health Assessment which aims to identify early signs of cultural risk, and support internal audits of risk culture. A refreshed focus on matters reviewed by the Board has been undertaken and is constantly under review.

Capabilities

Review the Group's operational and commercial capabilities.

Progress

The increased focus on, and interaction with, the business has strengthened the Board's insights into the business and its capabilities. The Board receives regular updates on the operating landscape, performance, market trends and the status of the transformation programme.

Board and committee interaction

To increase the visibility by non-executive directors of the work of each of the Board committees.

Progress

Board committee composition was reviewed and changes made to achieve appropriate cross-committee membership. In addition, upon appointment, each non-executive director is invited to attend all committees regardless of membership on an ongoing basis.

Additional informal meetings between the Chairman and non-executive directors are now scheduled as routine.

Alignment of performance and reward

To increase understanding and focus on performance and reward to achieve alignment of incentive systems throughout the Group, including key achievement milestones in line with the three-year strategic plan.

Progress

The Group Remuneration Policy is well aligned to the business strategy. The incentive plan performance measures have been strengthened to reflect progress made during the course of the Business Review. In addition, provisions for clawback were established in January 2015. There has been a focus by the Board to identify strategic priorities and integrate these into the Group's evolving executive culture. The Board received quarterly updates on the transformation programme and associated risks which is now part of the regional business review update.

Board experience

To identify and appoint additional non-executive directors with specific knowledge and experience within the general insurance sector, IT, operational and transformation expertise.

Progress

Since 2014, three new non-executive directors have been appointed with significant insurance, financial services and business development expertise as well as international board experience. These appointments have enhanced and broadened the diversity and relevant experience of the Board.

2014

Internal evaluation: Board and committee questionnaires covering composition, performance, oversight, knowledge and understanding

2015



Meeting with management in Canada

Stakeholders

An increased level of time spent within the business with a focus on interaction with senior management, customers, brokers, key shareholders and regulators, to obtain greater insight and technical knowledge of the business and relevant issues.

Progress

A rolling programme of visits has been established, to explore in depth specific business areas, their operational strengths and weaknesses, understand technical and topical issues to strive to become 'best in class'. The Board has met with regulators, shareholders, distribution partners, brokers and employees as part of this programme.

Quality of information to the Board

To review the information flow and quality of information submitted to the Board.

Progress

The Group Nomination and Governance Committee's responsibilities have expanded to include oversight and approval of the Board rolling agenda, ensuring that appropriate focus is given on key matters. A new framework and guidance has been implemented in 2016 for all Board and committee papers, to improve the quality of information being presented to the Board and its committees in support of the directors discharging their duties.

2016 external evaluation and action for 2017 and beyond

The results of the 2016 external evaluation concluded that, over the previous three years, the Board had made demonstrable progress building on its strengths, and showed a significant improvement in its effectiveness and ability to add value. The main priorities identified were:

- to consolidate focus on longer-term strategy in preparation for the completion of the transformation of the Company.
- to focus on embedding the cultural transformation and executive succession planning at all levels.

Succession planning

To increase the Board's role in executive succession planning and involvement in the review of the Group's culture and engagement.

Progress

The Board has received updates on culture, cultural risk and employee engagement. Members of the Board have attended global leadership conferences and a variety of executive, senior management, women in leadership and executive development programme events to build relationships with high potential executives.

Succession plans for the Board and Group Executive have been reviewed by the Board and Group Nomination and Governance Committee.

Accountability

The Group operates within a robust governance structure to ensure a well-managed business with effective decision-making, procedures and strong internal reporting, ensuring that the Group complies with all relevant legislation and regulation in each jurisdiction in which it operates.

The Group's System of Governance comprises three elements:



Corporate Governance Framework

The purpose of the Corporate Governance Framework is to ensure effective and efficient decision-making by the Board and its committees, aligning to Group strategy of focused, stronger and better.

The Corporate Governance Framework ensures that both directors and employees act within a chain of authority and powers which stretches back to the shareholders as ultimate owners of the Group. It provides the framework which supports the realisation of its business strategy, supports its long-term success and safeguards compliance with applicable laws and regulations.

The Board is accountable to shareholders for the creation and delivery of strong sustainable performance and the creation of long-term shareholder value. The Board meets frequently and is responsible for organising and directing the affairs of the Group in a manner that will promote the success of the Company and is consistent with good corporate governance practice, ensuring that the Group is carrying out its duties and continues to meet legal and regulatory requirements.

The business of the Group is overseen by the Board, who may exercise all the powers of the Group subject to the Articles of Association, relevant laws, and any directions as may be given by shareholders at a general meeting by shareholder resolution. The directors may delegate any of their powers or discretions to committees. The specific duties of the Board are clearly set out as a formal Schedule of Matters Reserved to the Board, which can only be amended by the Board itself and which is reviewed annually.

Risk Management System

The Risk Management System is underpinned by the Three Lines of Defence model. The Group Board are responsible for ensuring the effectiveness of the Group's Risk Management System; for setting the Group's overall risk strategy and risk appetite (including Group level risk limits and tolerances); and for approving the main risk management strategies and policies.

The Group operates under a common framework through which risk management and control is embedded. Each business within the Group is required to follow consistent process – using a common language – to identify, measure, manage, monitor and report its risks, in line with a consistent and comprehensive set of policies.

Risk Strategy and Risk Appetite are updated on an annual basis in line with the strategic review. The risk appetite is communicated to the Regions, countries and legal entities who set local risk limits and tolerance levels aligned to Group risk appetite.

The Risk Management processes are mandated in the overarching Risk Management Policy, which is approved by the Group Board and subject to annual update and review. The overarching Risk Management Policy establishes a framework of standard risk management processes. It also defines the dependencies and interaction with the ORSA and the Group's approach to stress and scenario testing.

Internal Control System

The Group has an effective internal control system in place which sets out the processes and frameworks required to ensure effective and efficient delivery of the Group's strategic objectives, including reliability and availability of information to identify and mitigate any potential risk of failure to achieve business objectives. It does not eliminate risk. The Board has overall responsibility for the effectiveness of the internal control system.

The Internal Control System comprises three key elements:

1. Internal Control Framework, whereby policies establish standard controls, which are implemented and operated by the business; supplemented by objective 1st Line validation and independent 2nd Line assurance processes. The Internal Control Framework includes Financial Controllershship, whereby the Group Controllershship Policy sets out the standard control processes to mitigate against material financial reporting misstatement and financial loss. It is subject to assurance through the Financial Control Framework.
2. Delegated Authority Framework, whereby authority is cascaded down from the Board to the business.

Day-to-day management of the Group is undertaken by the Group CEO and his team supported through executive level committees. Authority is delegated from the Board to the Group CEO through the Delegated Authority Framework and onwards delegation to senior management who receive an Executive Licence setting out their specific limits of authority in terms of entering into financial, underwriting, claims and other business commitments. Each executive is responsible for ensuring a similar process of delegation is in place within his or her area of responsibility. This framework enables the business to:

- ensure that all employees execute their responsibilities within clearly defined limits and subject to specified terms and conditions appropriate to their role, competence, experience and technical capability so as to mitigate the risk of the Group being exposed/committed to material financial, operational, legal, reputational and/or regulatory risk and/or loss
- ensure that the risks associated with managing and delegating authorities are mitigated through the use of appropriate preventative and detective controls and remain within the risk appetite

- ensure compliance with relevant regulatory and statutory requirements
- provide clarity to the business on who can make what type and level of decisions, enabling swift escalation to the appropriate executive.

From time to time additional authorities are delegated to the Group CEO from the Board to cover specific matters as required.

3. Regulatory Compliance Framework, whereby the Regulatory Compliance Policy sets out the standard control processes to minimise and/or prevent the risk of material loss, reputational damage or liability arising from the failure to comply with regulatory requirements. This also ensures that the Group deals with regulators in an open and co-operative manner and keeps them fully and promptly informed of all matters. Ultimate responsibility for compliance with the relevant rules and regulations rests with the Board, the executive and the senior management in each business. Advice, challenge, and interpretation is provided to these bodies by the Regulatory Risk and Compliance function.

UK Corporate Governance Code

The UK Corporate Governance Code (the Code) sets out standards and expectations on corporate governance matters for UK companies. The Group Nomination and Governance Committee monitors compliance with the Code.

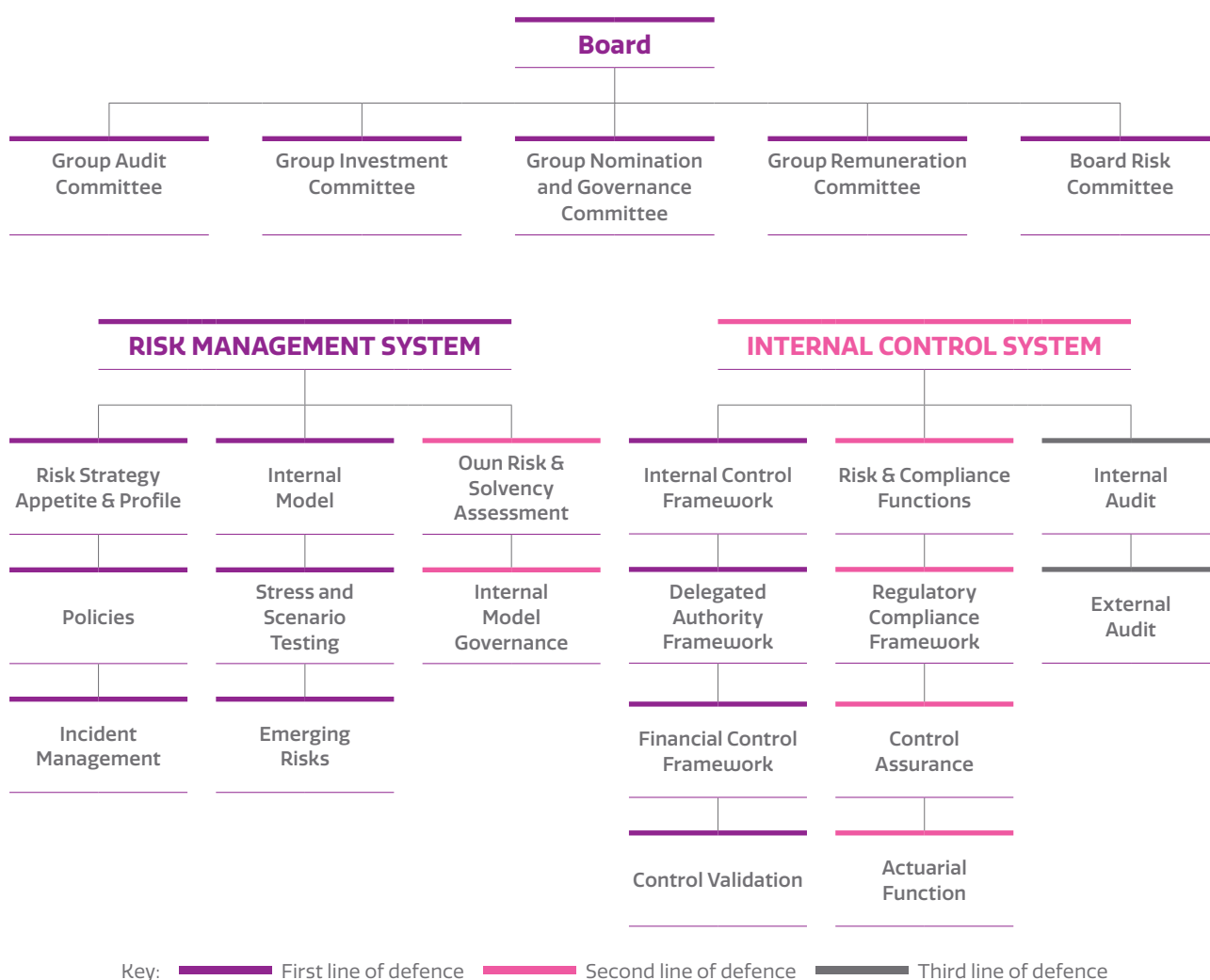
Throughout the year, the Company has complied with the Code and this report together with the Strategic Report and committee reports demonstrates how the Principles and Provisions of the Code have been applied.



Explore online

The Financial Reporting Council are responsible for the publication and periodic review of the Code. The latest version of the Code, published in 2016 can be found at www.frc.org.uk.

Corporate Governance Framework – Structure of Board and Committees



Engagement

Customer

The Group knows that customer focus is key to the success of the business. One of the Group's main strategic goals is the ambition of delivering improvements in customer service.

During the year, the Board spent time in the Peterborough contact centre which is a key centre for the Group's personal lines intermediated business, to gain a deeper understanding of the core capabilities to deliver the best products and services for the Group's customers, how the affinity and retail business is growing and the impact of the Group's business transformation. This assisted the Board in understanding the market challenges and the Group's positioning within each business segment. During the visit the Board met with senior management of some of the Group's UK affinity partners.

The Board also visited Canada to gain a deeper understanding of RSA Canada's capabilities, operational excellence, multi-channel distribution business and understand the impact of the transformation programme on the customer experience. During the visit, the Board met with representatives from over 40 broker companies who work with RSA Canada. These visits underpin the importance the Board places on customer focus in becoming 'best in class'.

For over 300 years the Group has been helping to protect customers all over the world against risk events and uncertainty. To ensure the business remains relevant, customer feedback is regularly sought to help improve service and products. The primary measure used to do this is the universally recognised Net Promoter Score (NPS), which produces a customer satisfaction score based on a scale of 1 to 10. The NPS can be collected for various elements of a customer's interaction with the Group, such as when obtaining a quote, making a claim or a general impression of the business. In addition to NPS, the Group track a range of other metrics that differ by product and region including: retention, complaint levels, trust and product advocacy. Customer retention rates are collated by product lines across the business and in 2016, the retention rate stood at 80 percent at an aggregated Group level. The business focuses on sustainably improving these metrics and specifically targets upper quartile NPS scores, by focusing on putting the customer first in everything that it does.

Employees

The performance and expertise of the Group's employees are key to the successful delivery of the Group's strategy. In 2016 Korn Ferry Hays Group were engaged to support the Group's employee enablement and engagement strategy. In January 2017 employees shared their views, ideas and suggestions through a Group-wide employee survey. The results will be shared across the organisation, benchmarked to industry and HR will support leaders and employees to build action plans to implement positive changes. The Group also continue to focus on a number of platforms where employees can provide feedback and have employed an engagement tool called Yammer across the UK, Ireland, Scandinavia and Canada.

The Group has a close working relationship with trade unions and employee associations in all parts of the business where they exist and consults with employees and representatives on relevant matters taking their views into consideration. There is also a European Works Council which consults with employee representatives on transnational matters across UK, Ireland, Sweden, Norway, Denmark, France, Spain, the Netherlands, Belgium and Germany.

In 2016, the UK business became a Living Wage accredited employer paying the Living Wage rates for London and other parts of the UK. The Company has been paying the Living Wage for many years, but is now pleased to receive this official recognition.

During 2016, major changes were made in the UK to the terms and conditions of employees in relation to pension and redundancy. This involved a lengthy process of engagement and consultation with employees and their representatives which took into account employee views in the decision making process and resulted in the closure of the UK Defined Benefit Schemes to future accrual effective from 31 March 2017. There is also a new UK Redundancy Policy effective from 1 January 2017 for those employees recruited before April 2013.

The Group is committed to diversity and the promotion of equal opportunities through its Equal Opportunities Policy. Following the launch in 2013 of a new diversity and inclusion programme, the Group has continued to invest in strengthening its pipeline of female employees for senior leadership positions. The Group is committed, wherever possible, to employing and supporting people who are disabled, or become disabled during their career with the Group. In 2016, the Group reinvigorated its efforts to build greater diversity across all levels of the organisation and create a more inclusive culture which attracts, encourages and capitalises on diverse perspectives, establishing a stronger foundation for the Group's success. The Group recognises that having a diverse workforce and supporting inclusive culture is vital for the future of the Group. Diversity of thought, background and experience enables the Group to innovate and create better solutions for our customers. Additional information, together with a breakdown of the Group's diversity statistics, can be found in the Strategic Report on pages 4 and 41 and are incorporated into this Report by reference.

Regulators

The Board is responsible to the PRA and the FCA for complying with the Group's UK insurance regulatory obligations. The Board attaches great importance to its regulatory responsibilities and is committed to dealing with regulators in an open, co-operative and transparent manner. The Board paid close attention to the expectations of the PRA and FCA with particular focus on embedding Solvency II and conduct matters. During the year the PRA and FCA conducted private meetings with several members of the Board and executive management and the PRA attended a Board meeting to discuss their supervisory strategy for the forthcoming year with the Board. Regular management information is provided to assist the Regulators with the supervision of the Group. The Group comprises a number of regulated entities across different jurisdictions and is committed to maintaining effective relationships with each of its regulators across the world, believing this to be integral to the success of the Group's strategy and its long-term value.

Rating agencies

The Group is rated on an interactive basis by Standard & Poor's and Moody's. Their insurance financial strength ratings as at 22 February 2017 are A (stable outlook) and A2 (stable outlook) respectively. These ratings were affirmed following the 2016 half-year results and the positive progress on implementing the strategic restructuring programme previously announced by the Company. In addition, both agencies spent a day with senior management discussing Group strategy, financial plans, capital and risk management.

Public affairs

The Group contributes to public policy debates on issues relevant to the business, either individually or through industry bodies such as the Investment Association, the Association of British Insurers and the Confederation of British Industry. This can include issues such as fraud, motor and pet insurance, asbestos, compensation culture, financial services regulation and renewable energy. The Group engages with policymakers to improve understanding of the role the insurance industry plays in society and the economy.

Employees apply the principles of openness, transparency, honesty and integrity to all of their activities with policymakers. The Group adheres to principles of best practice, declaring the interests which it represents and ensuring that, to the best of its knowledge, information provided is unbiased, complete, up to date and not misleading. Each year the Company proposes a resolution authorising political expenditure up to £100,000 for each of donations to political parties and independent election candidates, donations to political organisations and incurring political expenditure. This resolution is proposed in the event that the funding of seminars, functions and charitable donations by the Group may be regarded as political in nature. During the year the Group has not made any donations to political parties or independent election candidates.

The challenging political landscape following Brexit is by no means played out, and the potential problems it brings to the financial markets remain. The Group is however shielded from any substantive impact by virtue of its non-sterling profits and legal group structure which broadly comprises regulated European subsidiaries. The majority of the Group does not rely on Freedom of Services 'EU passporting' to transact a significant amount of business. Although the Group may need to apply for some additional licences following Brexit, it is not currently anticipated that the Group will need to make wholesale changes to the structure of its operations.

Corporate Responsibility

The Group's Corporate Responsibility Strategy 2014–18 addresses the Group's most relevant environmental and social issues. The Group's Corporate Responsibility approach is based on the Board's commitment to run the business in a way that all stakeholders can be proud of, at the same time as making a positive impact on society and the environment. More detail can be found in the Strategic Report on pages 34 to 35 and on the Group's website at www.rsagroup.com/responsibility.

Annual greenhouse gas emissions

In accordance with Part 7 of The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, certain disclosures are required in respect of greenhouse gas emissions (the Strategic Report GHG Emission disclosures). The information to fulfil this requirement can be found here and on our Corporate Responsibility webpages www.rsagroup.com/responsibility.

Greenhouse gas emissions for RSA Insurance Group plc (tonnes of CO₂e)

| | 2016 | 2015 | 2014 |
|--------------------------------------|--------|--------|--------|
| Scope 1 [Ⓐ] | 3,336 | 6,115 | 12,279 |
| Scope 2 [Ⓐ] | 12,364 | 17,275 | 24,717 |
| Scope 3 | 11,470 | 15,907 | 16,376 |
| Business travel [Ⓐ] | 9,238 | 13,050 | – |
| Total gross tonnes CO ₂ e | 27,170 | 39,297 | 53,372 |

Notes:

The emissions for 2015 and 2016 have been calculated using a different organisational scope to previous years, reporting all sources of emissions from operations with 50 or more full-time equivalent (FTE) employees. In previous years, emissions from offices with less than 50 employees were estimated, but these have been removed from the scope of the 2015 and 2016 reported emissions. Previously, some Scope 3 emissions were misreported as Scope 1 emissions. This has resulted in a significant reduction in Scope 1 emissions from 2014–15 and again in 2015–16. Due to these changes, we restated our baseline year as 2015 for our carbon reduction target and amended our target accordingly.

Selected data for 2016 as indicated by the symbol [Ⓐ] has been independently assured by PwC in accordance with ISAE 3000 (Revised) and ISAE 3410. For further information, please refer to our reporting criteria and PwC's assurance opinion which can be found on our Corporate Responsibility pages at www.rsagroup.com/responsibility.

Scope 1: Emissions from the Group's sources that are controlled by us, including the combustion of fuel, company-owned vehicles and the operation of our facilities.

Scope 2: Emissions from the consumption of purchased electricity, heat or steam.

Scope 3: Emissions from non-owned sources that are related to the Group's activities, including business travel and the use of water, paper and waste generated.

Business travel: Emissions from flights, trains, taxis, hotels and vehicles not owned by the organisation. This has been separately assured and reported in 2015 and 2016.

Methodology

Our disclosures cover all sources of greenhouse gas emissions as required by the Strategic Report GHG Emission disclosures, aligning with our financial control boundaries and including all emissions from operations with 50 or more full-time equivalent employees, covering the period 1 January 2016 – 31 December 2016.

Corporate Governance – continued

Calendar of Investor Relations Activity

February

- 2015 Full Year Results
- Post-results roadshow – UK

March

- Barclays UK Select Conference – New York
- Morgan Stanley European Financials Conference – London

April

- Corporate Governance dinner with top shareholders

May

- First quarter trading update
- Annual General Meeting
- Redburn European Conference – Toronto

June

- Deutsche Bank Global Financial Services Conference – New York
- Goldman Sachs European Financials Conference – Paris
- Autonomous Insurance Conference – London

July

- Investor roadshow – Switzerland

August

- 2016 half-year results

September

- KBW UK & European Financials Conference – London
- Barclays Global Financial Services Conference – New York
- Post results roadshow – London
- BofAML Financials CEO Conference – London

October

- Ad hoc inbound investor meetings

November

- Third quarter trading update
- UBS European Conference – London
- J.P. Morgan Cazenove 'Best of British' Conference – London

December

- Ad hoc inbound investor meetings

Where data is not provided by the operating entity, estimates have been provided based on relative calculations against other businesses within the Company. Our reporting has been carried out with consideration of the World Business Council for Sustainable Development and World Resources Institute's (WBCSD/WRI) Greenhouse Gas Protocol, a Corporate Accounting and Reporting Standard, together with the latest emissions factors from recognised public sources including, but not limited to, Department of Environment and Rural Affairs, the International Energy Agency, the US Energy Information Association, the US Environmental Protection Agency and the Intergovernmental Panel on Climate Change.

Shareholders

During 2016, the Company held nearly 400 meetings with institutional investors, and met with 17 of the top 20 shareholders on at least one occasion. The key themes of these meetings centred on the future ambition and capability of the Group and capital foundation. The Group's share register includes institutional investors predominantly from the UK, Europe and North America with a range of investment styles. Further information is set out later in this section.

The Group remains committed to maintaining high levels of transparency and disclosure to investors to aid understanding of the Company's investment case. The Group continually monitors and evaluates its disclosures to ensure they remain informative and relevant.

AGM

At the 2016 AGM, an average of 71.1 percent of the total issued share capital was voted across all resolutions, with an average of 98.3 percent voting 'For' each resolution.

The 2017 AGM will be held at 200 Aldersgate, St Paul's, London EC1A 4HD on Friday, 5 May 2017 at 11.00am. A letter from the Chairman and the notice convening the AGM (Notice) is made available to all Ordinary Shareholders at least 20 working days before the meeting and can be found on the Company's website at www.rsagroup.com/AGM2017. Presentations will be given on the Group's performance and activities during 2016 and the financial results of the Company prior to the formal business of the meeting. All directors attend the AGM if they are able to do so, with the Chairman and each Board committee Chairman making themselves available to take questions from Ordinary Shareholders.

Separate resolutions are proposed on each item of business. In accordance with the provisions of the Articles of Association, any proxy form sent by the Company to shareholders in relation to any general meeting must be returned to the Company, whether in written form or in electronic form, not less than 48 hours before the time for holding the meeting, excluding non-business days (or, in the case of a poll taken otherwise than at, or on, the same day as the meeting, not less than 24 hours before the time appointed for the taking of the poll). At any general meeting, every Ordinary Shareholder present shall have one vote on a show of hands and on a poll, every Ordinary Shareholder present in person or by proxy shall have one vote for each Ordinary Share of which he/she is the holder. Each resolution will be put to a poll at the AGM in 2017. The results of the vote on each resolution will be announced to the London Stock Exchange and will be available on the Company's website, www.rsagroup.com/AGM2017.

Preference Shareholders are only entitled to receive notice of, attend, speak and vote at general meetings if the dividend payable on the Preference Shares is in arrears at the date of the Notice, a resolution is proposed that affects the rights of the preference shareholders, a resolution is proposed to wind-up the Company, a resolution is proposed to reduce the capital of the Company (other than a redemption or purchase of shares), or in such other circumstances as the Board shall determine. In any of these situations the Preference Shareholders may only vote on the relevant resolution and not on all the business of the general meeting.

Share Capital

The Company is listed on the London Stock Exchange under the ticker symbol 'RSA'. The Company has two classes of shares: Ordinary Shares of £1.00 each and Preference Shares of £1.00 each. The Preference Shares are entitled to a fixed income, but the Ordinary Shares carry no right to a fixed income. The Preference Shares rank on a winding-up in priority to the Ordinary Shares.

As at 31 December 2016, the Ordinary Shares and Preference Shares represented 89 percent and 11 percent respectively of the Company's total issued share capital. Directors are limited as to the number of shares they can allot (save in respect of employee share schemes). Renewal of the directors' authorities to allot shares will be sought at the 2017 AGM. In addition, directors are restricted by the limits set out by the Investment Association. During 2016, the directors exercised their authorities to allot shares only in respect of employee share schemes. The average total daily trading volume on the London Stock Exchange during 2016 was approximately 2.7m Ordinary Shares. The opening market price of an ordinary share on 4 January 2016 was 418.0 pence and the closing market price on 30 December 2016 was 586.0 pence which was the highest daily closing price of an ordinary share during 2016. The lowest daily closing price was 373.2 pence on 9 February 2016. There are no specific restrictions on the size of a shareholding nor on the transfer of shares, which are both governed by the general provisions of the Articles of Association and legislation. The directors are not aware of any agreements between the Company's shareholders that may result in restrictions on the transfer of securities or on voting rights. The Company may purchase any of its own shares (including any redeemable shares). An authority from ordinary shareholders for the Company to purchase up to 101,754,340 of its own Ordinary Shares (representing 10 percent of its issued share capital as at 7 March 2016), was passed at the 2016 AGM. This authority will expire at the conclusion of the 2017 AGM and a new authority will be sought. The authority was not exercised during the year.

During the year, the Company operated two employee benefit trusts to hold Ordinary Shares in the Company which are used to satisfy grants under the Group's share incentive schemes. Capita Trustees Limited and Capita IRG Trustees, respectively, are the Trustees. The Trustees may vote in respect of any shares held in the trusts but have no obligation to do so, and Trustees may have regard to the financial interests of the beneficiaries in exercising their voting rights over the Company's shares. Standard dividend waiver agreements are in place for the employee share trusts to receive dividends of 0.01 pence per share.

The Company operates a sponsored American Depositary Receipts (ADR) programme which is managed by JP Morgan Chase NA. The programme allows shareholders to invest in the Company through US dollar denominated funds. One ADR represents one Ordinary Share of £1.00 each.

More information on the Company's share capital can be found in note 32 on page 157.

Financial Calendar

2 March 2017

Ex-dividend date for the ordinary final dividend for 2016 and the first preference dividend for 2017.

3 March 2017

Record date for the ordinary final dividend for 2016 and the first preference dividend for 2017.

3 April 2017

Payment date for the first preference dividend for 2017.

4 May 2017

Q1 Trading Update.

5 May 2017

Annual General Meeting.

12 May 2017

Payment date for the ordinary final dividend for 2016.

3 August 2017*

Announcement of the half-year results for the six months ended 30 June 2017.

10 August 2017*

Ex-dividend date for the second preference dividend for 2017.

11 August 2017*

Record date for the second preference dividend for 2017.

7 September 2017*

Ex-dividend date for the ordinary interim dividend for 2017.

8 September 2017*

Record date for the ordinary interim dividend for 2017.

2 October 2017*

Payment date for the second preference dividend for 2017.

13 October 2017*

Payment date of the ordinary interim dividend for 2017.

2 November 2017*

Q3 Trading Update.

*provisional date

Corporate Governance – continued

Dividends

Following the implementation of regulatory changes applicable to the Group from 1 January 2016, in order for the Company's Ordinary Shares to be counted towards the new group capital requirements, any dividends declared by the Company must be capable of being cancelled and withheld or deferred at any time prior to payment, if the relevant capital requirements have been breached or payment of the dividend would lead to non-compliance with those requirements. An amendment to the Articles of Association reflecting this requirement was passed by shareholders at the 2016 AGM. Directors do not expect to exercise this right, other than where they believe that it may be necessary to do so in light of the applicable legal or regulatory requirements.

The directors therefore recommend a final dividend (subject to the dividend being cancelled, withheld or deferred) of 11 pence per Ordinary Share (2015: 7 pence) to be paid on 12 May 2017 to holders of Ordinary Shares on the register at the close of business on 3 March 2017, subject to Ordinary Shareholder approval. An interim dividend of 5 pence was paid during 2016, making the total proposed dividend for the year 16 pence (2015: 10.5 pence). The Company will not be offering a Scrip Dividend alternative in respect of the final dividend. The Company's Preference Shares receive a dividend at the rate of 7.375 percent per annum paid in two instalments on, or as near as practicably possible, to 1 April and 1 October each year subject to approval by the Board.

Substantial share interests¹

The following table shows the holdings of major shareholders as disclosed to the Company in accordance with the Disclosure Guidance and Transparency Rules as at 31 December 2016 and at the date of this Report.

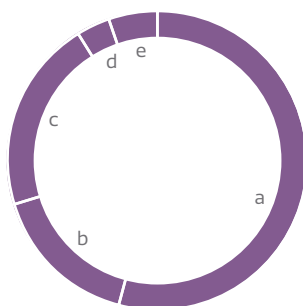
| Shareholder name | 31 December 2016 | | | 22 February 2017 | | |
|--|-----------------------|--------------------|------------------------------------|-----------------------|--------------------|------------------------------------|
| | No of Ordinary Shares | % of voting rights | Nature of holding | No of Ordinary Shares | % of voting rights | Nature of holding |
| Ameriprise Financial, Inc, and its group | 75,871,245 | 7.46% | Direct & Indirect | 75,871,245 | 7.46% | Direct & Indirect |
| BlackRock, Inc | 55,359,399 | 5.43% | Indirect, Securities Lending & CFD | 55,359,399 | 5.43% | Indirect, Securities Lending & CFD |
| Cevian Capital II G.P. Limited | 133,068,287 | 13.12% | Indirect & CFD | 133,068,287 | 13.12% | Indirect & CFD |

Notes:

1. Where the Company has been informed that the threshold for notifications is 5 percent in accordance with DTR 5.1.5, interests below this threshold are not included in this table.

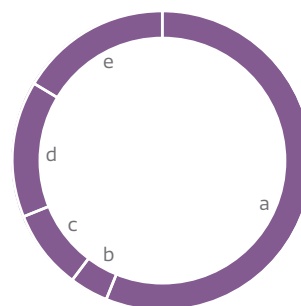
Distribution of shares by geography as at 31 December 2016

- a. UK 54.22%
- b. Europe 16.08%
- c. US and Canada 20.98%
- d. Rest of World 3.50%
- e. Unanalysed 5.22%



Analysis of Registered Holders as at 31 December 2016

- a. Unit Trust/Mutual funds 56.2%
- b. Private/Retail 4.2%
- c. Pension funds 8.7%
- d. Insurance 14.7%
- e. Other 16.2%



Registered shareholdings by size as at 31 December 2016

| | No of Holdings | No of Shares | % of Holdings | % of Shares |
|-----------------------------|----------------|---------------|---------------|-------------|
| 1 and 24,999 | 30,055 | 26,432,672 | 97.87 | 2.59 |
| 25,000 and 99,999 | 255 | 13,476,663 | 0.83 | 1.32 |
| 100,000 and 499,999 | 214 | 50,805,763 | 0.70 | 4.98 |
| 500,000 and 999,999 | 62 | 46,000,941 | 0.20 | 4.51 |
| 1,000,000 and 1,999,999 | 50 | 73,092,894 | 0.16 | 7.18 |
| 2,000,000 and 9,999,999,999 | 74 | 809,746,053 | 0.24 | 79.42 |
| Total | 30,710 | 1,019,554,986 | 100 | 100 |

Other Statutory Information

Statement by directors

Section 414A of the Companies Act 2006 requires the directors to present a Strategic Report of the Company for the financial year ended 31 December 2016. The information that fulfils the requirements set out in section 414C can be found on pages 4 to 41, and is incorporated by reference into this Report.

So far as each director of the Board is aware, there is no relevant audit information (as defined in section 418(3) of the Companies Act 2006) of which the Company's external auditor is unaware, and each director has taken all reasonable steps to make himself/herself aware of, and to establish that the external auditor is aware of, any relevant audit information.

A balanced and understandable assessment of the Group's position and prospects, and an explanation of its strategy for delivering the objectives of the Company are contained in the Strategic Report on pages 4 to 41 which includes:

- Use of financial instruments by the Company and details of financial risk management objectives and policies of the Company, including the policy for hedging each major type of forecasted transaction for which hedge accounting is used
- The Company's exposure to price risk, underwriting risk, reserving risk, credit risk, liquidity risk and cashflow risk
- An indication of likely future developments in the Company's business.

A full list of the Group's subsidiaries and related undertakings is in Appendix B on pages 176 to 179.

Details of events which have occurred after the reporting period are set out on page 171, which is incorporated by reference into this Report.

The Directors are responsible for preparing the Annual Report and Accounts and consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy. Further explanation on the assurances undertaken by the Group Audit Committee on behalf of the Board are set out in the Group Audit Committee Report found on pages 70 to 75. A report from the external auditor can be found on pages 104 to 108.

Viability statement

In accordance with the UK Corporate Governance Code, the directors have assessed the viability of the Group over a three-year period. The directors have determined that a three-year period is an appropriate period over which to provide its viability statement as this is the period focused on by the Board during the operational planning process and is also aligned to the short-tail nature of the business insurance contracts. In assessing the viability of the Group, using the Group's Own Risk and Solvency Assessment (ORSA), the directors have assessed the Group's principal risks and uncertainties, and how these are managed and mitigated,

as detailed in the Strategic Report on pages 38 to 41.

This includes, but is not limited to, the Group's reinsurance programme which is structured to mitigate the impact of catastrophe and large loss events on earnings and capital, and the Group's underwriting strategy and portfolio management which is used to mitigate the impact of underwriting and claims risk. The Group's three-year cashflow forecast demonstrates its ability to sustain positive cashflows in its businesses through targeted underwriting, portfolio and distribution actions, and to pay dividends as forecasted. This is further supported by the Group's credit facilities and highly liquid investment portfolio which provide further sources of short-term cash if needed.

As part of its operational planning process, the Group prepares annually a three-year operational plan and capital forecast along with sensitivity analysis (based on the Group's approved Internal Model for Solvency II reporting) which support the Group's strategy. These forecasts are subject to review and challenge by the directors on at least an annual basis.

In addition the Group, as part of its ORSA process, uses PRA set stress tests to assess the capital resilience of the Group to a range of severe but plausible scenarios including a reverse stress test (which includes a combination of insurance, market and economic stresses). These tests allow the Board to review and challenge the Risk Management strategy and consider potential mitigating actions.

Based on the results of this analysis, the directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three-year period of their assessment.

Going concern

In considering the appropriateness of the going concern basis, the Board has reviewed the Group's ongoing commitments for the next 12 months and beyond. The Board's review included the Group's strategic plans and updated forecasts, capital position, liquidity and credit facilities and investment portfolio. Based on this review no material uncertainties that would require disclosure have been identified in relation to the ability of the Group to remain a going concern for at least the next 12 months, from both the date of the balance sheet and the approval of the consolidated financial statements. It is therefore concluded that the going concern basis is appropriate for the preparation of the 2016 full-year consolidated financial statements.

Conflicts of interest and related party transactions

In accordance with section 175 of the Companies Act 2006, each director has a duty to avoid conflicts of interest. Under Articles 91 and 92 of the Company's Articles of Association, conflicts of interest may be authorised by the Board or a Board Committee. Directors are required to notify the Company Secretary when a potential conflict of interest arises. Each director's conflicts of interest are reviewed on an annual basis. Any director who has declared a conflict of interest shall not count towards the quorum or vote on any resolution to authorise the conflict of interest and, at the Board's discretion, may be excluded from any meeting at which the conflict of interest is under consideration. Where a conflict of interest is authorised, restrictions may be imposed on the conflicted director, such as excluding the director from the discussion or restricting the receipt of information in connection with the conflict of interest. The Board confirms that it has reviewed the

Corporate Governance – continued

schedule of directors' conflicts of interest during the year and that the procedure in place operated effectively in 2016. None of the directors had any interest in any contract of significance with the Company or any of its subsidiaries during 2016.

Essential contracts and change of control

The Company does not consider that there are any significant agreements to which the Company is a party that take effect, alter or terminate upon a change of control of the Company following a takeover bid that are required to be disclosed pursuant to paragraph 13(2) (j) of Schedule 7 of the Large and Medium Sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended).

The Company does not have agreements with any director or employee that would provide compensation for loss of office or employment resulting from a takeover except that provisions of the Company's share schemes and plans may cause some options and awards granted to employees under such schemes and plans to vest in such circumstances.

Directors' Indemnity

Article 140 of the Articles of Association provides that, among other things and insofar as permitted by law, the Company may indemnify its directors against any liability and may purchase and maintain insurance against any liability. The Company has granted an indemnity to each of the directors pursuant to the power conferred by Article 140 of the Articles of Association. The indemnities granted constitute qualifying third-party indemnity provisions, as defined by section 234 of the Companies Act 2006 and is in addition to appropriate insurance cover.

The Company believes that it promotes the success of the Company to provide this indemnity to its directors in order to ensure that the Group attracts and retains high calibre directors through competitive terms of employment in line with market standards. The directors and officers of the Company and its subsidiaries also have the benefit of insurance which provides suitable cover in respect of legal actions brought against them.

In addition, the Company has indemnified the directors of SAL Pension Fund Limited, a majority-owned subsidiary of the Group, in relation to its role as Trustee of an occupational pension scheme. This indemnity constitutes a qualifying pension scheme indemnity provision under section 235 of the Companies Act 2006.

Articles of Association

The Company's Articles of Association may be amended by special resolution of the Company's Ordinary Shareholders. The current Articles of Association were amended at the 2016 AGM and are available on the Company's website at www.rsagroup.com/articles.

Borrowing powers

Article 98 of the Articles of Association sets out the restrictions on the borrowings of the Company. The aggregate amount, for the time being, remaining borrowed by the Group must not, without the previous sanction of an ordinary resolution of the Company, be more than one-and-a-half-times the aggregate of:

- (i) the amount paid up on the issued share capital of the Company; and
- (ii) the total of the capital and revenue reserves of the Group (subject to certain adjustments).

Modern Slavery

In accordance with section 54(1) of the Modern Slavery Act 2015, the Group will be publishing our Slavery and Human Trafficking Statement online by April 2017. The statement covers the activities of RSA Insurance Group plc and its subsidiaries and details policies, processes and actions we have taken to ensure that slavery and human trafficking are not taking place in our supply chains or any part of our own business.

Disclosures required under Listing Rule 9.8.4R

The following table sets out where in the Annual Report and Accounts the information required to be disclosed to meet the requirements of Listing Rule 9.8.4R, where applicable to the Company, can be located:

| Information required | Location in Annual Report and Accounts |
|-----------------------------|--|
| Dividend Waivers | Page 61 |
| Long Term Incentive Schemes | Pages 76-101 |

Directors' responsibility statement

The Directors' Responsibility Statement appears on page 103 and is incorporated by reference into this Report.

By order of the Board


**Charlotte Heiss**

Group Chief Legal Officer
and Company Secretary
22 February 2017

Board Committee Reports

Group Investment Committee Report

Introduction

I am pleased to present the Group Investment Committee Report for 2016.

The Committee is authorised by the Board to manage all aspects of investment policy and strategy for the Group and provide oversight of the operation of the Group's investment portfolios within established strategy and risk frameworks.

The Group Investments Director attends all meetings of the Committee to provide an update on the economic and market background and outlook affecting the Group, the investment activities carried out since the Committee last met, an overview of performance and proposed changes to investment strategy, which require the Committee's approval.

The Committee Chairman reports to the Board on the outcome of Committee meetings and the Board also receives the minutes of Committee meetings.

The Committee members and their attendance at meetings are shown on page 49.

Key activities during 2016

The global investment environment remained challenging in 2016. Although there was evidence of recovery in some areas, the combination of weak growth expectations and limited inflation pressure saw bond yields fall back to historical lows in the Group's key markets. This has placed further pressure on investment income for the Group as maturing bonds are reinvested at the prevailing low yield level.

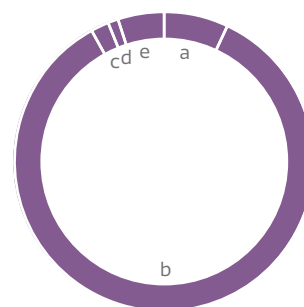
Despite these pressures the Group maintained its core commitment to a high-quality investment portfolio. Asset allocation continues to be dominated by bond and cash instruments, representing 92 percent of assets at year end. The bond portfolios also remained high quality with 70 percent rated AA or above and only 1 percent rated lower than BBB. Exposure to the more volatile equity and property asset classes remains modest being just 3 percent of the Group's total investments.

In line with 2015, the Group has continued to make measured allocations to less liquid bond and loan instruments. These investments have been targeted to take advantage of the additional yield offered for illiquidity relative to traditional quoted bonds whilst maintaining a strong underlying credit quality and have included loans backed by property and trade receivables. In total the Group now has intended investment allocations to these assets approaching £1.2bn with around £1.1bn of this invested at the year end.

Allocation to illiquid credit assets has been built gradually over several years, ensuring diversification of exposure with each investment being subject to extensive due diligence. The Committee has reviewed and agreed limits for the illiquid credit allocation and continues to review progress on implementation as well as performance.

Total assets as at 31 December 2016: £13.64bn

- a. Cash 7%
- b. Fixed Income 85%
- c. Property Investment 2%
- d. Equities 1%
- e. Alternatives and other 5%



Details of the Group's investments are contained in notes 24–27 on pages 145 to 153.



Joseph Streppel

Non-Executive Director and
Chairman of the Group Investment
Committee
22 February 2017

Board Committee Reports – continued

Group Nomination and Governance Committee Report

Introduction

I am pleased to present the Group Nomination and Governance Committee Report for 2016.

The Committee plays an important role in ensuring that the composition of the Board and its committees have the balance and diversity of experience and skills to operate effectively, and in the best interests of the Company's stakeholders. The Committee also ensures that the Company is operating with high standards of governance and measures compliance against the UK Corporate Governance Code.

The Committee has four main areas of responsibility:

- Board composition: managing the process to identify Board candidates and advising and making recommendations on Board membership, Committee membership and related appointments
- Succession planning: ensuring appropriate succession plans are in place for members of the Board and senior executive roles
- Governance: monitoring the Group's compliance with the UK Corporate Governance Code
- Effectiveness: evaluating Board and committee performance.

The Committee members and their attendance at meetings are shown on page 49.

Key activities during 2016

This year the Committee's responsibilities expanded to include consideration of succession planning and the Board's commitment to diversity and these changes have been included in the Committee's terms of reference.

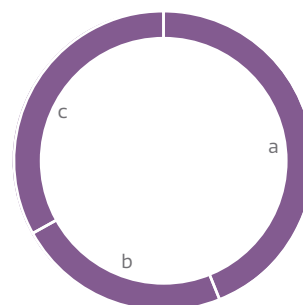
Board Composition

The Committee ensures that the Board is comprised of individuals with a diverse yet relevant set of skills, knowledge and experience who will work well together to lead the Group.

At the 2015 AGM, we confirmed our intention to recruit two new Independent Non-Executive Directors with a proven track record in insurance, particularly in the Group's core markets and in transformation. During the year, the Committee considered candidates for these roles and was pleased to recommend the appointment of Martin Strobel and Isabel Hudson to the Board. Martin Strobel joined the Board on 1 May 2016 bringing over 23 years' insurance and financial services experience, most recently as Chief Executive Officer of Baloise Group. Isabel Hudson joined the Board on 1 August 2016 bringing significant experience in general insurance and wide-ranging commercial, corporate finance and business development experience

Breakdown of topics discussed at Committee meetings held during 2016

- a. Governance 44%
- b. Succession Planning and Recruitment 23%
- c. Other 33%



together with relevant board experience as an executive and non-executive director on a number of listed companies. The Zygos Partnership were engaged to conduct the search for independent non-executive directors, and has no other connection with the Group. Zygos are accredited by the Davies Review under the Enhanced Code of Conduct for Executive Search Firms as they have a strong track record in assisting boards to enhance their gender diversity.

Johanna Waterous has informed the Board that she will retire as a director with effect from the Company's AGM on 5 May 2017. With effect from 5 May 2017, Isabel Hudson will succeed Johanna Waterous as Senior Independent Director.

The Committee continually monitors the balance of skills, experience, independence and knowledge on the Board as well as gender diversity. The Board currently comprises 73 percent male and 27 percent female directors. We remain committed to Lord Davies' target for female board composition although all appointments are made on merit against the agreed selection criteria. Further information relating to diversity is included on page 47.

Succession planning

During the year, the Committee undertook a detailed review of the current composition of the Board and committees, from both a short and long-term succession planning perspective.

Kath Cates was re-appointed for her second three-year term during the year. The Committee considered her independent contribution to the Board and Committees and the balance of her skills, knowledge and experience with those of the other directors. The Committee concluded that Kath continued to add value to the Board, remained independent and therefore recommended that she be re-appointed for a further three-year term commencing September 2016. Kath absented herself during discussions on her re-appointment.

The Committee has also reviewed succession plans for Executive Committee members, noting that the simplification of the Group and spans of control could lead to greater gaps in succession planning. To address this, tailored development plans are created for those individuals that are identified as

being possible candidates to join the Executive Committee in the future. The aim of the succession plans is to develop a pipeline of talented individuals in each region in which the Group operates. The succession plans were utilised during the year when Charlotte Heiss, Group Chief Legal Officer and Company Secretary; Nathan Williams, Group Underwriting Director; and Martin Thompson, President and CEO RSA Canada, all internal candidates, were each appointed to succeed members of the Executive Committee.

Korn Ferry Hay Group are regularly engaged by the Group to provide executive search services for roles across the Group and assisted with the appointment of Cathy Lewis, Group HR Director.

Governance

The Committee monitors the Group's compliance with the UK Corporate Governance Code ensuring that there are clear governance processes in place to aid effective, efficient and risk-aware decision-making at a Group level. A formal assessment of compliance against the Code is carried out by the Company Secretary twice a year and reviewed by the Committee. Any non-compliance is discussed and it is agreed whether action is required to remedy the non-compliance, or if there are circumstances which justify the non-compliance. The Company has complied with the Principles and Provisions of the Code throughout the year.

The Committee is in the process of undertaking a review of subsidiary board governance to ensure overall alignment to Group objectives and that good levels of governance apply.

The Committee considers that each non-executive director devotes sufficient time to discharging his/her duties and that he/she remain independent. The Committee considers new external appointments to ensure that they do not give rise to conflicts of interests and do not impact the director's time commitment to the Company. In each case considered in the year, the Committee was satisfied that external appointments could be authorised.

The Committee undertakes an assessment for appointments and re-elections against the requirements of the UK Corporate Governance Code. It is against this assessment that each of the non-executive directors are recommended for election or re-election to the Board. Further, the Committee recommended the Chairman and executive directors for re-election to the Board. Based upon these recommendations from the Committee, the Board are proposing the elections and re-elections as set out in the 2017 Notice of Annual General Meeting.

Board and committee evaluation

During the year, the Committee has reviewed progress against the actions identified as part of the annual evaluations over the period 2013-16. Details of the Group's three-year journey setting out the focus are set out in the Board evaluation pages on 53 to 55.

The 2016 Board evaluation was carried out using an independent external provider, Boardroom Review who reviewed information provided to the Board and its committees, conducted individual Board and senior management interviews, and attended meetings as an observer. The Group Nomination and Governance Committee will track the actions identified and will build on these through 2017 and 2018 to support the Chairman through the internal evaluation process.

Martin A Scicluna



Martin A. Scicluna

Chairman and Chairman of Group
Nomination and Governance Committee
22 February 2017

Board Committee Reports – continued

Board Risk Committee Report

Introduction

I am pleased to present the Board Risk Committee Report for 2016.

During 2016, the Committee fulfilled a key purpose in providing advice to the Board on risk management issues, overseeing the risk management arrangements of the Group and the Group framework of risk limits and risk appetite. The Committee members, their attendance at meetings and regular meeting attendees are shown on page 49.

This year, the Committee's effectiveness has been assessed through an externally facilitated evaluation, more details of which can be found on page 53. The evaluation concluded that the Committee was effective.

Role and responsibilities

The Committee's main duties are to:

- Ensure that the material risks facing the Group have been identified and understood, including emerging and potential risks, and, where appropriate, actions have been implemented to mitigate and maintain risks within appetite
- Review and challenge the results of quarterly risk appetite assessments, which include capital adequacy assessments, and any actions necessary to maintain or bring capital within appetite
- Consider and approve the Group risk appetite framework and risk limits for recommendation to the Board
- On behalf of the Board, review the Group's Own Risk and Solvency Assessment (ORSA) approach and report, including the selection of appropriate stress and scenario tests
- Review and challenge the outputs and key assumptions from the Internal Model, any changes and the validation process
- Review Solvency II compliance
- Undertake an annual review of the Group's System of Governance and recommend it to the Board for approval
- Work with the Group Remuneration Committee to ensure risk is properly considered in setting the remuneration policy for the Group.

Private meetings are held ahead of each Committee meeting to discuss any concerns and areas on which to concentrate with management and advisers. The Committee has held four private meetings without management being present as well as a private meeting with the Group Chief Risk Officer.

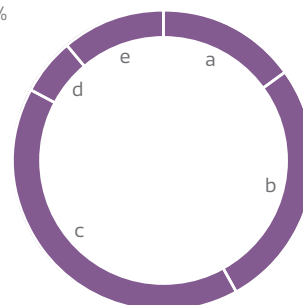
Key activities during 2016

Regional Focus and Deep Dives

The Committee has met with representatives from the Group Corporate Centre, Scandinavia, the UK and International regions. The Board visited Canada in the year, spending time with the Chief Risk Officer in-region, all of which allowed the Committee to better understand the detail of the risks present in each region and how to use and communicate best practice on a cross-regional basis to aid the management and mitigation of these risks.

Breakdown of topics discussed at Committee meetings held during 2016

- a. Risk and Compliance Updates 15%
- b. Capital and Solvency II 27%
- c. Specific Risk Deep Dives 41%
- d. Regional Deep Dives 6%
- e. Governance 11%



The Committee has looked in detail at the IT risk appetite framework, both against internal and external standards, focusing on the key deliverables and any risks to these. The monitoring of IT risk and controls, including data security will remain an area of key focus, particularly given increasing external threats and the extensive level of transformational change being rolled-out across the Group.

The Committee has also maintained a focus on capital sensitivities and buffers, and how capital levels have responded in the first year of Solvency II during a period of heightened financial market volatility.

Risk Management System

The Risk Management System is designed to identify, measure, manage, monitor and report risk and is underpinned by the three lines of defence model. The Committee oversees the Group's Risk Management System to ensure it is robust and operating effectively throughout the year.

The overarching Risk Management Policy, approved annually by the Board on the Committee's recommendation, provides the framework of risk management processes which are embedded throughout the Group. It also defines the dependencies and interactions with the Group's ORSA and the Group's approach to stress and scenario testing. There are further policies setting out risk assessment standards and risk appetite and detailed procedures which set minimum requirements, internal controls and details of controls testing. Members of the Group Executive own different policies and are responsible for ensuring they are embedded through regional, local and functional owners who are responsible for identifying and reporting any non-compliance through rigorous assessments. The results of these assessments are reviewed and challenged by local and Group risk teams, the responsible senior Group executives, regional risk committees and the Committee.

Further information on the Group's risk strategy and appetite can be found in the Risk Management section of the Strategic Report on pages 38 to 41.

Own Risk and Solvency Assessment (ORSA)

Throughout the year, as in previous years, the Committee considered a range of activities in order to assess the risks and solvency needs of the Group which constitutes the ORSA process. A summary of these activities and associated decisions taken during the ORSA assessment were reviewed by the Committee.

Business Risk review

The Group Chief Risk Officer provides a quarterly update to the Committee on the key risks and risk themes impacting the Group, including an assessment of whether risks are within appetite and any actions necessary to maintain or achieve this. This review is supplemented by subject matter expert assessments of the risks impacting the business including insurance risk, financial risk, operational risk, reinsurance risk and strategy. As an example with respect to insurance risk, the Committee discussed specific themes, such as special high risk business, analysis of large losses, pension and financial risk and reserving risk. The Committee also focused on remediation progress on specific risk portfolios and considered the reinsurance options available. In addition, key emerging risks and trends were considered with a focus on inflation risk, Brexit, and the potential for, and impact of, a major breach of flood defences.

The Committee reviewed the Group's risk strategy and appetite where updates were made to maintain effectiveness during the first year of Solvency II.

**Kath Cates**

Non-Executive Director and
Chairman of the Board Risk Committee
22 February 2017

Board Committee Reports – continued

Group Audit Committee Report

Introduction

I am pleased to present the Group Audit Committee Report 2016. The Committee plays a key role in overseeing the integrity of the Company's financial statements and robustness of the Group's systems of internal control and financial and regulatory risk management systems.

During the year the Committee has closely monitored the Group's control environment, particularly in relation to IT and Information Security and ongoing transformation activity, to ensure that the control environment remains sound. A joint meeting of the Committee and the Board Risk Committee was held to focus on the Group's ongoing work to improve the management of IT risk, the Group's preparedness and controls for the management of cyber risk, and of customer data, with a focus on line one ownership of controls and actions to mitigate and minimise the impact of a cyber event.

There have been further regulatory and corporate governance changes impacting the role and work of the Committee during the year, with revised FRC Guidance for Audit Committees published, changes to the UK Corporate Governance Code (the Code) which will come into force during 2017, the implementation of the EU Audit Directive 2014 into UK Regulations and changes to International Financial Reporting Standards (IFRS). The Committee has received appropriate training on these areas and is able to continue to challenge management effectively and fulfil our duties to shareholders and other stakeholders.

This year, the Committee's effectiveness has been assessed through an externally facilitated evaluation, more details of which can be found on page 53. The evaluation concluded that the Committee was effective.

Role and responsibilities

The purpose of the Committee is to:

- Coordinate and oversee the integrity of the financial reporting process
- Monitor compliance with relevant regulations, industry codes and legal requirements
- Oversee the effectiveness and objectivity of the internal and external auditors
- Monitor the effectiveness of the systems of internal controls
- Provide assurance to the Board on the effectiveness of the Group's financial and regulatory risk management arrangements.

The Committee has unrestricted access to management, information and external advisers as required in order to fulfil its duties, and is satisfied that it has received sufficient, reliable and timely information during 2016 in order to discharge those duties.

Committee composition, skills and experience

Details of membership and attendance at Committee meetings are shown on page 49.

The Committee comprises five independent Non-Executive Directors and the Board is satisfied that the Committee has recent and relevant financial experience as required by the Code. The members bring diverse experience, knowledge and skills to the Committee, which enables the members collectively to act as an effective Committee. In particular, Jos Streppel brings financial, governance and industry experience through his former roles as CFO of Aegon and as Chairman of the Dutch Corporate Governance Monitoring Committee. Kath Cates has in-depth knowledge of controls, governance and risk management through roles including Chief Operating Officer, Wholesale Banking at Standard Chartered. Johanna Waterous brings expertise in sales and marketing as well as her experience as a chairman and non-executive director. Martin Stobel joined the Committee on 1 May 2016 and brings knowledge of financial services from his recent role as CEO of Baloise Holding AG and a background in IT consulting for financial services. Alastair Barbour brings audit experience and knowledge of financial reporting requirements through his former career at KPMG LLP (KPMG). In addition, Kath Cates and Alastair Barbour are members of the Board Risk Committee, ensuring that risk is taken into account in the Committee's decisions and that information flows appropriately between the two Committees.

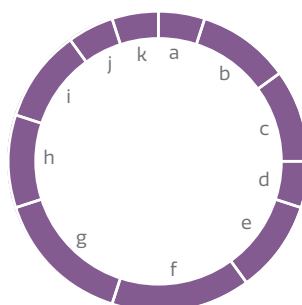
The Committee held six scheduled meetings during the year and has held private meetings with the Group Chief Auditor, the Group & UK Regulatory Compliance Director, the Group Financial Officer, the external auditor and the Group Chief Actuary without other members of management being present. The Committee members regularly met privately to discuss issues on which to concentrate with management and advisers in the subsequent audit committee meeting. Ad hoc meetings were organised to cover topics in more detail, including IT and cyber risk, a training session on corporate governance and IFRS changes and with Group Internal Audit's leadership team to discuss and review their proposed plans for 2017.

The Group Chief Financial Officer, the Group Chief Auditor, the Group & UK Regulatory Compliance Director, the Group Chief Risk Officer, the Group Chief Legal Officer and Company Secretary and representatives of the external auditor, KPMG, are regular attendees at Committee meetings. The Chairman is invited to attend the meetings where the interim and final results are considered. Other members of management and external advisers may attend at the invitation of the Committee.

The Committee Chairman reports to the Board on the outcome of Committee meetings and the Board also receives the minutes of Committee meetings.

Breakdown of topics discussed at Committee meetings held during 2016

- a. Accounting policies, methodologies and practices 5%
- b. Reserves 10%
- c. Other balance sheet valuations 10%
- d. Pension assumptions 5%
- e. Financial results 10%
- f. Internal Controls 15%
- g. Governance and compliance 15%
- h. IT Matters 10%
- i. Solvency II 10%
- j. External Audit 5%
- k. Internal Audit 5%



Key activities during the year

In addition to the significant issues in relation to the Annual Report and Accounts set out below, the Committee considered the following issues during the year:

- Monitored compliance with the Group's reserving policy by each business to ensure that the Group's reserve margin remained adequate and that the uncertainty considerations were appropriate
- Reviewed the Solvency II opening balance sheet alongside the basis of preparation and provided appropriate challenge of the key judgements in relation to Solvency II. The Committee also reviewed the quarterly Solvency II Balance Sheets produced by management and monitored the Group's ongoing development of the Solvency and Financial Condition Report
- Monitored the Group's compliance with anti-money laundering requirements and anti-bribery and corruption laws, including the progress in implementing new screening software across the Group. The Committee also approved a new Anti-Money Laundering and Sanctions policy and Fraud Risk policy
- Monitored the sustainability of control improvements, including the number of risk acceptances in place and their cumulative impact on the Group's risk appetite, and the Group's risk and control culture
- Monitored the integrity of the control environment during transformation and considered the appropriateness of the design of key initiatives in relation to their impact on the Group's control environment
- Considered whether it was appropriate to adopt the 'going concern' method of accounting for the 2016 Annual Report and Accounts and the viability statement, recommending to the Board that both are appropriate.

Financial reporting and significant financial issues

The Committee attaches considerable importance to the work, opinions and findings of the external auditor, KPMG, who participates in all Committee meetings and who met with the Committee in private on two occasions during the year. The principal interactions with KPMG during the year in relation to financial reporting were:

- Consideration of the strategy and plan for the audit of the financial statements including discussion and challenge in relation to materiality levels set; the scope of the proposed coverage by business unit; determination and approach to the audit of key areas of risk; understanding the oversight by the group audit team of subsidiary business unit audit teams and visits by the group team to business units
- At the half year and year end, detailed discussion and consideration of their findings and opinions in relation to the key risk areas, judgements made, any changes to the plan and to materiality and discussion of the underlying reasons
- Consideration of KPMG's wider comments on governance, financial reporting processes and efficiencies as well as information systems and controls
- Consideration of their observations on controls and processes as reported to management and follow up with relevant management to be satisfied that the observations are being appropriately actioned
- Reporting on the Solvency II opening balance sheet and reviewing key areas of judgement in relation to Solvency II.

The main matters and primary areas of judgement addressed and concluded on by the Committee were as follows:

Valuation of insurance liabilities

The Committee has ensured that management exercised appropriate judgement and control in estimating insurance contract liabilities including assessing the impact of claims trends and other influencing factors consistent with previous years. This year the Committee again examined the appropriateness of discount rates on certain long-tail liabilities and assumptions on indexation, particularly in light of fluctuating bond yields.

The Committee received and reviewed actuarial reserving reports which described the basis for judgement in valuing insurance liabilities. Particular areas of focus for the Committee were trends emerging in parts of the Group Legacy portfolio, trends observed in Canadian Auto and General Liability portfolios and reserve strengthening for Irish long-tail lines in response to adverse experience. The Committee satisfied itself that management reflected available and reliable information when setting the reserves and that an appropriate margin was maintained.

Board Committee Reports – continued

The results of independent internal reviews carried out in the year with respect to all long-tail lines in Ireland, Denmark's Workers Compensation and Swedish Personal Accident were considered by the Committee. The Committee also confirmed the completeness and appropriateness of the planned programme of future reviews.

The Committee received and considered detailed written and verbal reporting from KPMG setting out their observations and conclusions in respect of the recorded insurance contract liabilities and Solvency II Technical Provisions based on their audit procedures as further described in their report on pages 104 to 108.

IT Systems and controls

The Group's IT infrastructure, including retained legacy systems, is complex and financial reporting is dependent on the operational and financial IT systems operating correctly and the control environment in which they operate. This is a key area of focus for both Audit and Risk Committees and during the year they received updates from management on progress to enhance IT general controls, the oversight of IT testing processes and improvements in documentation and standards, together with regular reporting from internal audit on the results of their reviews and testing. In light of the ongoing transformation activity, the Committee closely monitored IT and information security to ensure the control environment was maintained. With respect to financial reporting controls the Committee received detailed updates from KPMG on their assessment of general IT controls including information on areas where additional controls or substantive testing was required, the reasons therefore and the conclusions reached in support of the audit. After consideration and discussion with management and KPMG, the Committee concluded that the financial results as prepared from the IT systems were appropriate and reliable.

Pension and post-retirement obligations

During 2016, the Committee received reports on the valuation of the pension schemes. As the pension schemes are sensitive to changes in key assumptions, management completed an assessment as to the appropriateness of the assumptions used, including benchmark data, where appropriate, and reported their findings to the Committee. The Committee supported the conclusion that the assumptions used were appropriate and within an acceptable range of other companies with similar schemes. In addition, any non-standard changes in assumptions and judgements are reviewed by the Committee and, following a review, a change to the method of valuation of the liability matching arrangements was approved, as the Committee was satisfied that this resulted in a value that was compliant with the relevant standards and best represented the economics of the arrangement.

The triennial funding review of the two largest UK pension schemes was formally completed during 2016. The Committee discussed the key outcomes of this review, which included a reduction to investment risk and a revised schedule of contributions payable by the Group into the schemes.

Valuation of deferred tax assets

The Committee reviewed the key assumptions and financial projections supporting the UK deferred tax asset. The forecasts presented by management were assessed and, in particular, the longer-term projections of profitability in light of the changes to business plans as a result of the strategic review, restructuring activities and other management actions in progress or contemplated. After discussion and challenge, the Committee concluded that management's proposed assessment as to the recoverable deferred tax was reasonable.

Review of 2016 Annual Report and Accounts

At the request of the Board, the Committee considered whether the 2016 Annual Report and Accounts were fair, balanced and understandable, and whether the disclosures were appropriate. To ensure that new accounting standards were understood and appropriately reflected in the financial statements, the Committee received quarterly updates of all relevant accounting standards that could impact the financial statements. The Group has not made any significant changes to its accounting policies during 2016 and has complied with updates to IFRS's as required during the year. Taken as a whole, the Committee is satisfied that the 2016 Annual Report and Accounts are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

Financial Control Framework

The Financial Control Framework (the Framework) aims to deliver a consistent approach to finance-related controls across the Group and embed a control culture that strengthens the Group's finance environment by ensuring that financial processes are managed effectively in order to mitigate the risk of financial misstatement. The process involves documenting and testing the operation of key financial controls, thereby providing an acceptable degree of assurance around the financial control environment. The primary focus of the Framework is the production of information for the Group Annual Report and Accounts. In addition, the Framework mitigates material risks at the local operational level. Local teams carry out control validation work and a Group Controllershship Team provides assurance over this work and reports on findings and actions to the Committee quarterly.

During the year, the Committee received quarterly updates on the assessment and testing of controls including any breaches and the action taken as a result.

Due to the level of transformation taking place within the Group's finance function, the Committee commissioned KPMG to undertake a review of the financial control environment to assess whether greater reliance can be placed on key controls; the extent of duplication of controls and dependence on manual controls that could be automated and whether the current level of governance is appropriate and commensurate to the risk being managed. As the Group's external auditor, the Committee believes that KPMG is best placed to carry out this work as it already has a detailed understanding of the Framework and control environment. In December, the Committee considered the results of this review and agreed actions to take advantage of opportunities for improvement.

Internal control

The Board has overall responsibility for the effectiveness of the Group's Internal Control System (the System) with the implementation and maintenance being delegated to the Executive Directors and senior management.

The Committee reviews the performance of the System quarterly, with an annual review undertaken by the Board. The System comprises three key elements:

- Internal Control Framework – policies establish standard controls, which are implemented and operated by the business
- Delegated Authority Framework – authority is cascaded down from the Board to the business
- Regulatory Compliance Framework – the Regulatory Compliance Policy sets out the standard control processes to minimise and/or prevent the risk of material loss, reputational damage or liability arising from the failure to comply with regulatory requirements.

In addition, the Board, through the Board Risk Committee, considers reports from risk specialists across the Group and reviews Group level risk management information. The System is designed to identify and mitigate, rather than eliminate, the potential risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material financial misstatement or loss.

In February 2017, the Committee reviewed the System in operation during 2016 and concluded that it was appropriate and operated effectively during the year.

The Committee received regular reports from the Group Chief Auditor, external auditor and Group Chief Risk Officer on the integrity of the control environment and also received regular reports on the Regulatory Compliance Framework which is described in greater detail below. These reports enable the Committee to continually assess the effectiveness of the Group's internal controls systems. The Committee discussed findings and recommendations from these reports, together with any control improvements recommended.

The Committee considers that an effective and appropriate ongoing process for identifying, evaluating and managing the significant risks faced by the Group has been in place during 2016 and up to the date of approval of the Annual Report and Accounts. For more information about the Group's Risk Management Framework, see pages 38 to 41.

Whistleblowing

New rules on whistleblowing from the PRA and FCA are now in force and the Group's whistleblowing policy and procedures were revised to reflect these. The Group takes whistleblowing extremely seriously and the Committee has taken responsibility for oversight of the Group's whistleblowing arrangements. In addition, Alastair Barbour has nominated responsibility for oversight of whistleblowing arrangements in compliance with the PRA's Senior Insurance Managers Regime. A senior manager within HR has also been appointed as the FCA Whistleblowing Champion.

The aim of the policy is to provide employees with a confidential forum to raise concerns in good faith where they either do not feel comfortable raising the matter with local management or are not satisfied with the local management response. Concerns can be raised by contacting local or Group senior management, including the Group Chief Auditor, or via an externally provided website and helpline.

All employees are required to complete online training to ensure they are aware of how and when to report concerns under the policy and the Committee has requested an analysis of cultural differences across the Group that may discourage some employees from reporting concerns to identify how these could be addressed.

A summary of all whistleblowing incidents, underlying investigations and actions undertaken is provided to the Committee on an annual basis. Any material incident would be reported to the Committee immediately.

The policy's effectiveness during the year has been assessed and the Committee is satisfied that it is appropriate, fit for purpose and effective and is sufficiently embedded across the Group.

Regulatory risk and compliance

The purpose of the Regulatory Risk and Compliance function is to ensure that the Group meets all relevant regulatory requirements in each jurisdiction in which it operates. The function is an influencer in ensuring a strong regulatory compliance culture and ensure mechanisms are in place to monitor the regulatory environment, identify, report and resolve issues to avoid or minimise business impact and surprises. The function is part of the Group's second line of defence which monitors and validates first line activities. The Group and UK Regulatory Compliance Director provides regular reports to the Committee.

The Group Regulatory team leads and develops the relationship between the PRA, Group and businesses to achieve a mutually beneficial relationship. It also updates the FCA regarding relevant Group level strategic matters.

During the year, the Committee has monitored progress towards full Solvency II reporting compliance; overseen embedding of the new Financial Crime Framework and implementation of new anti-money laundering screening software and received updates on regulatory issues.

The function's annual Compliance Plan sets out the compliance work to be undertaken in the upcoming year to ensure compliance, maintain an open, constructive and cooperative relationship with the Group's regulators, ensures the Board and employees understand their regulatory responsibilities and provides assurance, advice and guidance to the Board and the business. The Committee reviewed and approved the 2017 Compliance Plan in December 2016.

Board Committee Reports – continued

Group Internal Audit

Group Internal Audit's (GIA) primary purpose is to 'keep RSA safe and improving'. Specifically, GIA helps the Board and Executive Management to protect the assets, reputation and sustainability of the Group. GIA does this by assessing whether all significant risks are identified and appropriately reported by management and the second line of defence to the Board and Executive Management; assessing whether they are adequately controlled and by challenging Executive Management to improve the effectiveness of governance, risks management and internal controls.

GIA is an independent and objective function reporting to the Board. The Group Chief Auditor is a member of the Executive Committee and has a primary reporting line to the Chairman of the Group Audit Committee, with a secondary reporting line to the Group Chief Executive. Regional Chief Auditors report directly to the Group Chief Auditor, whilst recognising local regulation.

GIA's scope of activities is unrestricted and includes first line of defence control validation and second line of defence assurance activities, as well as the risk and control culture of the Group.

GIA's planning process is risk based and takes into consideration the key strategic and emerging risks facing the Group. GIA operates a six monthly rolling audit plan, allowing for a frequent and dynamic risk assessment and the Committee may request additional audits throughout the year as required. Rolling plans were approved by the Group Audit Committee in May and December 2016.

On a semi-annual basis, the Group Chief Auditor provides the Group Audit Committee with an assessment of the effectiveness of the governance, risk and control framework in each Region. Quarterly, GIA reports on the outcome of its work and management's progress in mitigating issues. Its report includes any thematic issues arising and root-causes identified.

Annually, the Group Chief Auditor provides the Group Audit Committee with an assessment of the skills and capabilities required to conduct the work needed, and whether budget is sufficient to allow the function to recruit and retain staff with the expertise and experience necessary to provide effective challenge throughout the Group and to Executive Management.

The results of the latest assessment were reviewed by the Committee in December 2016 and the Committee was satisfied that GIA was operating effectively, sufficiently resourced and that the risk to their independence and objectivity was low.

Compliance with professional standards is monitored within GIA through a quality assurance process, outsourced to Deloitte and operated on a continuous basis. GIA is governed by an Internal Audit Charter which sets out the function's role, mandate and authority, and includes independence and objectivity criteria. An updated Charter was approved by the Committee in August 2016.

External auditor

Appointment, tenure, independence and objectivity

KPMG was appointed as the Group's external auditor in 2013 following a formal competitive tender process and has been reappointed at each subsequent AGM. The external auditor forms part of the third line of defence. The current audit partner is Stuart Crisp who has been the Group's audit engagement partner since KPMG's appointment. In line with Financial Reporting Council's standards, KPMG will rotate the audit engagement partner at least once every five years. There are no contractual obligations restricting the Company's choice of external auditor and there is no limitation of liability in the terms of the appointments of KPMG as auditor to the Company.

The Committee has provided clear guidance to KPMG on the Committee's expectations of them as part of their role as auditor; that the Committee, not management, is KPMG's client; that they are expected to challenge appropriately; that they are expected to raise issues and concerns with the Committee as soon as is appropriate and on material matters they are expected to indicate their agreement to the position taken by management, or to explain why they do not, and the implications. The Committee has met with the external auditor twice during the year without management present to ensure that the external auditor has an opportunity to raise any concerns they may have and to ensure they remain independent and objective.

The Company complies with the requirements of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014, which relates to the frequency and governance of tenders for the appointment of the external auditor and the setting of a policy on the provision of non-audit services. It is the intention of the Committee that the Company will tender the external auditor appointment at least every 10 years and in accordance with the Financial Reporting Council's best practice notes concerning the conduct of such tenders.

Fees and non-audit services

The audit fee for the 2016 Annual Report and Accounts was discussed between the Committee and the external auditor and approved by the Committee on behalf of the Board.

The Group operates a non-audit services policy to assist with maintaining the independence of the external auditor and its personnel. All permitted activity must be authorised in advance by the Committee Chairman and subsequently ratified by the Committee. In addition, the total value of non-audit fees incurred by the external auditor is capped at 25% of total audit fees for the relevant financial year.

In exceptional circumstances the auditor will be considered for additional services where there is an overwhelming business rationale, but only with full Board approval. A summary of the policy is available on the Company's website at www.rsagroup.com/termsofreference. The Group's non-audit service policy will be reviewed against the requirements of the Financial Reporting Council's Revised Ethical Standard 2016 concerning the provision of non audit services and, if considered appropriate, updated in the first half of 2017.

Each quarter, the Committee receives and reviews a report on non-audit services, together with information on fees agreed and billed by the other major accounting firms.

Details of KPMG's remuneration during 2017, including that for provision of non-audit services, are provided in the notes to the financial statements on page 138.

Effectiveness

The Company undertakes a thorough review of the effectiveness of the external auditor on an annual basis, usually on completion of the audit process. The review is compliant with the UK Corporate Governance Code and was updated during 2016 to incorporate the guidance issued by the Financial Reporting Council. The review has covered the mind-set and culture, skills and knowledge, quality control and judgement of the external auditor through an assessment of their perceived quality, effectiveness, objectivity and independence.

The review was conducted by both a questionnaire distributed to and completed by the Committee, senior management and members of the Group financial reporting team, seeking opinions against set criteria and the performance of the external auditor against those criteria and through Audit Committee meetings with the external auditor whereby the Committee challenged the auditor's planning, strategy, risk identification process and conclusions.

On the basis of the review, the Committee is satisfied with the work of KPMG and that they are objective and independent. Accordingly the Committee has recommended to the Board that a resolution be put to the 2017 AGM for the reappointment of KPMG LLP as external auditor, and the Board has accepted this recommendation.




Alastair WS Barbour FCA

Non-Executive Director and Chairman
of Group Audit Committee
22 February 2017

Directors' Remuneration Report

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Committee Chairman's letter



Underlying Profit
before tax
(PBT)

£556m
+33%

For more
information,
see page 23

Underlying Return
on Tangible Equity
(ROTE)

14.2%
4.5 points better

For more
information,
see page 21

On behalf of the Group Remuneration Committee, I am pleased to introduce this year's report.

It contains the Directors' Remuneration Policy on pages 80 to 87 and the Annual Report on Remuneration on pages 88 to 101.

The Policy is due for renewal this year and will therefore be submitted for a binding vote at the AGM on 5 May 2017.

The Annual Report on Remuneration, which describes how the Committee has implemented the Policy in 2016 and plans to do so in 2017, is subject to an advisory vote.

Linking performance and remuneration in 2016

The Committee has continued its focus on ensuring that the remuneration received by executives is aligned to the Company's underlying financial performance, shareholder value creation, and achievement of individual and business review performance targets.



Remuneration remains closely aligned to underlying financial performance.

Hugh Mitchell
Independent Non-Executive Director

The Group has delivered a truly excellent set of results in 2016, as outlined in the Chairman's Statement on pages 4 and 5. Underlying Earnings per Share (EPS) is up 42% and the company's share price rose 43% in 2016, outperforming the European insurance index (SXIP) by 45%.

Key performance indicators include Group underlying Return on Tangible Equity at 14.2%, Combined Operating Ratio at 94.2%, and Operating profit at £655m, as detailed on pages 20 to 23.

The capital position has further strengthened with a Solvency II coverage ratio of 158% and a ratio of Tangible Net Asset Value to Net Written Premium (TNAV:NWP) of 45%.

The strong headline results were supported by improvements to all key underlying measures of performance including attritional loss ratios and costs.

Prior to making its incentive award decisions, the Committee reviews a report from the Group Chief Risk Officer on material risk factors and controls. On this occasion, no adjustments were considered necessary to award outcomes.

Based on the Committee's assessment of performance:

- The Group Chief Executive and Group Chief Financial Officer will receive bonus awards for 2016 at 100% and 86% of the normal maximum respectively, of which half is deferred into shares for three years.
- The long-term incentive awards from the 2014–16 cycle are forecast to partially vest at 43% of the maximum (this is subject to confirmation following the end of the measurement period for the Relative TSR performance condition, which by exception is measured up to March 2017 in this cycle).

The Chief Executive's bonus award was considered reflective of Stephen Hester's excellent personal contribution in the year. The targets applicable to these incentives are set out on pages 90 to 93.

The conditional long-term incentive awards granted during 2016 are subject to stretching performance conditions. Awards which vest will do so after three years. Executive Directors must retain vested shares for at least a further two years.

Directors' Remuneration Policy renewal

The Committee is not proposing any significant changes to the content of the Policy, which it considers to be aligned to shareholder interests, the promotion of good risk management and sustainable company success.

Since the Policy was last approved by shareholders in 2014, there have been a number of executive changes, planned business changes and an unsolicited bid by Zurich in 2015. The Committee has reflected on these experiences and is satisfied that the Policy remains well designed to cover varying business demands and situations.

It is worth noting that within the remuneration framework:

- The current incentive structure will remain in place. This is based on an Annual Bonus Plan and a long-term incentive where awards vest over a three-year period (followed by a further two-year retention period), which supports RSA's strategy built around annual and longer-term goals.
- The existing incentive opportunity levels are market-aligned and will remain unchanged.
- The arrangements for share-based deferral, malus and clawback included in the existing Policy will continue, as the Committee considers these to be robust and in line with good corporate governance.

Implementing our plans for 2017

We are proposing no major changes to how our Policy is implemented in 2017.

Strategy and incentive measures

The measures in our incentive plans are aligned to the performance improvement being delivered by the Company across the different targeted dimensions.

Since 2014, RSA's transformation programme has focused on capital and balance sheet strengthening, strategic refocusing and performance improvement. Our incentive plan measures have included a Business Review Scorecard designed to measure the successful delivery of this agenda.

With the turnaround phase essentially complete, RSA is concentrating on winning for customers and shareholders in the markets where we compete. This involves maintaining a resilient capital base and efficiently managing risk; driving towards our 'best in class' performance ambitions through expense reduction and improvements in pricing, underwriting and technology; and ensuring business sustainability by enhancing our customer franchise through optimal service levels and digitisation.

This means it is the right time to adjust the Business Review Scorecard. However, many of its performance indicators remain important as we transition to a more business-as-usual strategy.

As a result, our 2017 incentive plans will:

- Place continued emphasis on profit and shareholder value, with a substantial weighting given to the key financial performance indicators of Relative Total Shareholder Return (TSR), Group underlying Return on Tangible Equity (ROTE), Group underlying Profit before Tax (PBT) and Combined Operating Ratio (COR); and

Directors' Remuneration Report – continued

- Also include a Business Scorecard, which will be focused on key components of management activity essential to the success of the Company. This will cover three principal areas of Risk and Resilience, Underlying Performance and Business Sustainability (including Customer franchise), and allow the Committee to take account of those elements of performance that may not be wholly reflected by headline financial metrics; and
- In the case of the Annual Bonus Plan, continue to incorporate goals bespoke to each executive, with emphasis placed on both what is delivered but also how results are achieved.

Reflecting the Group's success in recent times and ambitious plans, the ROTE target range used for the 2017-19 long-term incentive grant will increase to 12-18% (from 11-16%). The on-target levels for both the 2017 Annual Bonus Plan and 2017-19 LTIP grant have been set in line with the latest operating plan. This targets continuing significant performance improvements even vs the record results delivered in 2016.

The Committee has approved in principle that Stephen Hester's performance share opportunity in the 2017-19 long-term incentive cycle will be for 230% of salary at maximum vesting, which is the Group's usual level of award for the Chief Executive, and that Scott Egan's opportunity will be for 200% of salary at maximum.

Base Salary and Chairman's fee

The Group Chief Executive and Chief Financial Officer's salaries will increase by 2.5% from 1 April 2017, which is in line with the level of increase for the Group's UK-based employees.

The Chairman's fee, which has remained unchanged since his appointment in 2013, is increased by 5% from 1 January 2017.

Shareholding

The Committee believes that executives should hold a significant number of shares in the Company, as this ensures alignment with the experience of other investors. It conducts regular reviews of RSA's provisions in this area. As a result, the Group Chief Financial Officer's target shareholding level will rise from 150% to 200% of salary from 5 May 2017. The Group Chief Executive's target shareholding level will be maintained at 300% of salary.

Stakeholder engagement

The Committee values and encourages an open dialogue with shareholders. It actively consulted the Group's largest shareholders, and the Investment Association (IA), Pension and Lifetime Savings Association (PLSA) and ISS, during the year, and the feedback received was considered in the course of reviewing the Directors' Remuneration Policy and when determining the incentive plan performance measures for 2017.

Further, the Committee closely monitors external debates related to executive pay, and will continue fully to comply with our disclosure obligations as they evolve.

While acknowledging public concerns about the general levels of executive remuneration and comparability with the wider workforce, at the same time we face the reality of competing in our different markets to attract talented executives who have choices about where they work. This has been particularly relevant at RSA, where we have had to recruit an executive team to deliver a challenging turnaround.

We continue to aim to treat all employees fairly in the markets in which we operate, as demonstrated for example by our accreditation as a Living Wage Employer, while ensuring we continue to have a high calibre executive team to deliver strong business performance to the benefit of all of our stakeholders.

I remain committed to providing shareholders with a transparent view of our remuneration decisions, and ensuring that these fairly reflect performance. I hope you find this report useful, and the Board looks forward to your support for it at the AGM.



Hugh S Mitchell

Non-Executive Director and Chairman of Group Remuneration Committee

22 February 2017

Remuneration snapshot

How is RSA implementing its Remuneration Policy for Executive Directors?

| Policy summary (full details on pages 80 to 87) | Implementation in 2016 (pages 88 to 98) | Implementation in 2017 (pages 98 to 101) |
|---|---|--|
| Base salary <ul style="list-style-type: none"> Market competitive. Reviewed annually. Other than exceptional circumstances such as a role change, salary increases will not exceed the level of increases applied to other RSA employees. | <ul style="list-style-type: none"> Group Chief Executive salary increase of 2% effective 1 April 2016. | <ul style="list-style-type: none"> Group Chief Executive and CFO salary increases of 2.5% effective 1 April 2017. |
| Annual Bonus Plan <ul style="list-style-type: none"> Targets aligned to operational plan. Half of any award is deferred into shares for three years. Subject to RSA's Malus and Clawback Policy (see page 94). 80% of salary for on-target performance, 160% of salary for maximum. | <ul style="list-style-type: none"> Group Chief Executive and CFO bonuses at 100% and 86% of the maximum respectively. | <ul style="list-style-type: none"> Performance measures: Group underlying ROTE and PBT, Group COR, a Business Scorecard and objectives bespoke to each executive. |
| Long-term Incentive Plan <ul style="list-style-type: none"> Performance Shares granted annually. These vest subject to performance conditions measured over three years. Two-year additional retention period applies to vested awards. Subject to RSA's Malus and Clawback Policy (see page 94). Up to 230% of salary for maximum performance. | Awards granted (2016–18 cycle) <ul style="list-style-type: none"> Group Chief Executive grant at 230% of salary, CFO grant 200%. Group underlying ROTE 'on-target' requirement increased from 2015–17. Awards vesting (2014–16 cycle) <ul style="list-style-type: none"> 43% of performance-based awards forecast to vest. | Awards to be granted (2017–19 cycle) <ul style="list-style-type: none"> Group Chief Executive grant at 230% of salary, CFO grant 200%. Group underlying ROTE target range increased from 2016–18 cycle. Required shareholding <ul style="list-style-type: none"> Group CFO required shareholding increased to 200% of salary (CEO required shareholding at 300%). |

How have we linked strategy, performance and variable remuneration? (details on pages 90 to 93)

Annual Bonus Plan 2016

| Strategic priorities | Performance measures | Actual performance | Weighting (% total bonus) | Scott Egan award | Stephen Hester award |
|--|--|--|------------------------------|---------------------|-------------------------|
| <ul style="list-style-type: none"> Shareholder Value Profitability | Group underlying ROTE Group underlying PBT Group COR | | 40% | 40% | 40% |
| <ul style="list-style-type: none"> Capital Business performance | <i>Business Review Scorecard:</i> Solvency II coverage ratio, TNAV:NWP, Controllable expenses, Attritional loss ratio, Strategic plan initiatives (including disposals, risk items) | Performance targets, results and narrative on pages 90 to 92 | 30% | 23% ¹ | 30% |
| | Personal Scorecard | | 30% | 23% | 30% |
| Total (% of maximum) | | | 100% | 86% | 100% |

Long-term incentive cycle 2014–16

| Strategic priorities | Performance measures | Actual performance | Weighting | Vesting (% of maximum) ² |
|--|--|--|------------------|-------------------------------------|
| <ul style="list-style-type: none"> Shareholder Value Profitability | Relative TSR Group underlying ROTE | | 33.33% 33.33% | 0% 9.33% |
| <ul style="list-style-type: none"> Capital Business performance | <i>Business Review Scorecard:</i> Capital metrics including Solvency II coverage ratio and TNAV:NWP, Credit rating, Cumulative earnings, TNAV growth per share, Controllable cost savings, Disposal proceeds, Attritional loss ratio. | Performance targets, results and narrative on pages 92 to 93 | 33.33% | 33.33% |
| Total (% of maximum) | | | 100% | 42.7% |

What remuneration did the Executive Directors receive in 2016? (details on page 90)

| | Salary | | Taxable benefits | | Bonus | | LTIP | | Pension related benefits | | Other remuneration | | Total | |
|-------------------------------|--------------|--------------|------------------|-----------|--------------|--------------|--------------|----------|--------------------------|------------|--------------------|--------------|--------------|--------------|
| (£'000) | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| Scott Egan ³ | 525 | 131 | 23 | 6 | 722 | – | – | – | 79 | 13 | – | 1,605 | 1,349 | 1,755 |
| Stephen Hester | 964 | 950 | 69 | 71 | 1,550 | 1,163 | 1,453 | – | 289 | 285 | – | – | 4,325 | 2,469 |
| Richard Houghton ³ | – | 174 | – | 7 | – | – | – | – | – | 23 | – | – | – | 204 |
| Total | 1,489 | 1,255 | 92 | 84 | 2,272 | 1,163 | 1,453 | – | 368 | 321 | – | 1,605 | 5,674 | 4,428 |

Notes:

- Modified down from 30% to 23%, as detailed on page 91.
- Provisional results: Relative TSR is measured up to 31 March 2017, and its vesting outcome will be finalised following this date. Business Review Scorecard outcome to be confirmed shortly after the Annual Results are published, as detailed on page 92.
- 2015 salary figures reflect time served as directors during the year.

Directors' Remuneration Policy

1. Introduction

This Policy Report describes the principles and policy that will be used to set and manage the Directors' remuneration with effect from 5 May 2017, subject to shareholder approval at the AGM on that date. It is intended these will apply over the next three years.

There are no significant changes to the content of this Policy, compared to the existing version which has been in place since it was approved by shareholders in May 2014.

Specifically, on the following pages 80 to 87 the Policy covers:

- How decisions on Directors' remuneration will be made at RSA, and the philosophy and strategy which underpin these decisions;
- How remuneration packages will be structured for current, newly appointed and departing directors;
- What impact business and individual performance will have on the potential value of Executive Directors' remuneration;
- What key contractual terms will apply to current and newly appointed directors; and
- RSA's engagement with its shareholders and employees on the subject of executive remuneration.

For reference, the Policy approved in 2014 is available at www.rsagroup.com/financial-reporting, on pages 71 to 79 of the 2013 Annual Report and Accounts.

2. RSA's remuneration principles

The remuneration philosophy and strategy are directly informed by the business strategy. The remuneration principles that the Group Remuneration Committee ('the Committee') follows are:

- Remuneration is aligned to the long-term interests of the Company, its business strategy and performance;
- The remuneration framework is designed to promote sound and effective risk management in line with the company's risk profile;
- Each component of the total remuneration package is simple and transparent, so as to be effective and understood by executives, shareholders and regulators;
- Pay is linked to performance, with variable remuneration fully contingent on the achievement of stretching short- and long-term objectives which directly support the achievement of strategic priorities and are aligned to shareholders' interests;
- Executive Directors and other executives are required to hold a significant number of shares in the Company; they are encouraged to act in shareholders' best interests by having a personal investment in RSA;
- Competitive remuneration packages are offered in order to attract, retain and reward the levels of high calibre talent which are essential to RSA's success in today's competitive global insurance market; and
- The remuneration framework is reviewed regularly to ensure that it continues to appropriately reward executives, while protecting shareholders' interests and complying with principles of good risk management and reward governance and avoiding conflicts of interest.

3. Remuneration Policy for Executive Directors

The following table sets out the components of the Executive Directors' remuneration package and how they operate.

| Purpose and Strategic Link | Operation | Maximum opportunity | Performance measures |
|--|--|--|---|
| Base salary (fixed remuneration) This element is designed to attract and retain high calibre executives, essential for ensuring RSA's ongoing success. | <p>Salaries are reviewed annually considering factors including: market positioning, internal pay relativities, levels of pay for other RSA employees, inflation, affordability, job scale and content, individual's experience and expertise.</p> <p>Salaries are benchmarked referencing peer group companies of comparable size and complexity.</p> <p>There is no automatic right for any Director to receive a salary increase.</p> <p>Only annual base salary is pensionable.</p> <p>An existing Executive Director's salary may be increased outside of the normal review cycle for material role changes.</p> | <p>Other than exceptional circumstances such as a role change, salary increases will not exceed the level of increases applied to other RSA employees.</p> | <p>Performance conditions do not apply, but business and individual performance may be considered when conducting the review process.</p> |
| Benefits (fixed remuneration) This element forms part of a market competitive package and supports the executive. | <p>Benefits typically cover the areas of: health and well-being, leave of absence, car and business travel, sickness benefit, insurances, professional subscriptions, external advice and employee discounts on certain insurance products. Home to work travel may be covered where appropriate.</p> <p>Some benefits are delivered as taxable cash-in-lieu allowances. Tax changes are not compensated.</p> <p>Assistance would be available under RSA's relocation policy or global mobility policy should this be required.</p> <p>Expenses can be claimed according to RSA's business and travel policies, including tax thereon where such expenses do not qualify for tax relief.</p> <p>Executive Directors in participating countries can acquire shares in RSA's all-employee share plans (Sharesave and Sharebuild), and those in the UK can participate in RSA's flexible benefits programme.</p> <p>Benefits are determined with reference to market practice within the same peer group companies referred to in respect of salaries. The Committee can also source information from bespoke benefit surveys to aid decision-making.</p> <p>The Committee can amend any benefit or introduce new ones to ensure the remuneration package remains market competitive or to respond to regulatory, legal or best practice changes.</p> | <p>Benefits are valued and determined with reference to the benchmarking peer groups and other surveys reviewed by the Committee.</p> <p>Benefits are fixed remuneration, however the cost to provide them can vary from year to year in line with market conditions, which therefore determine the maximum value.</p> | <p>None.</p> |
| Pension (fixed remuneration) This element forms part of a market competitive package and enables executives to save for retirement. | <p>Pension benefits take the form of employer contributions to a pension plan, or a full/partial cash allowance in lieu. The RSA UK defined benefit pension schemes are closed to all new entrants and close to future accrual effective 31 March 2017.</p> <p>Pension cash allowances are paid monthly and are subject to statutory deductions.</p> <p>The Committee can adjust contribution or allowance levels to ensure these remain appropriate and market aligned. It can also agree changes to the terms of the Directors' pension plan(s), as appropriate.</p> | <p>No Executive Director will receive a pension benefit in excess of 30% of salary.</p> | <p>None.</p> |

Directors' Remuneration Report – continued

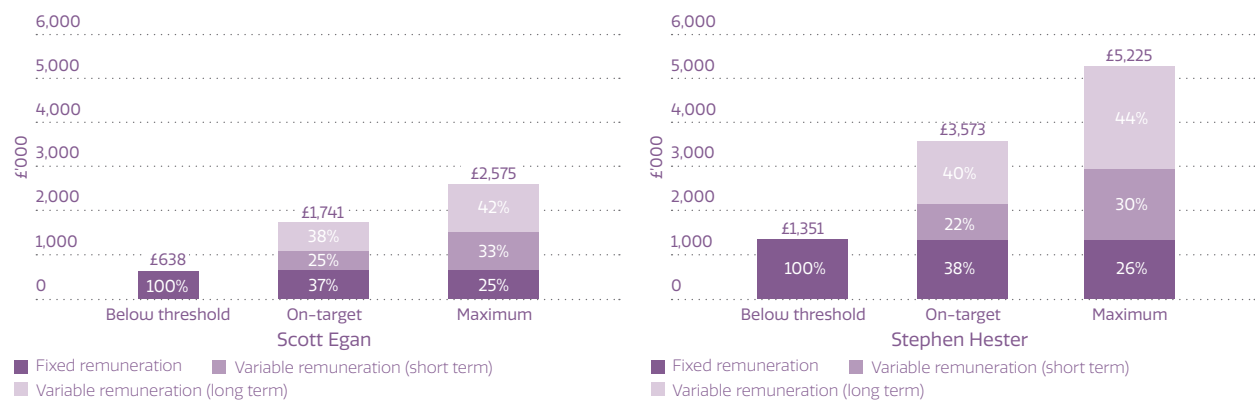
| Purpose and Strategic Link | Operation | Maximum opportunity | Performance measures |
|--|--|--|--|
| <p>Annual Bonus Plan (variable remuneration)</p> <p>This element incentivises the achievement of short-term financial and non-financial goals, in line with RSA's risk profile.</p> <p>Deferral into shares enhances shareholder alignment.</p> | <p>Bonus awards are calculated against stretching annual financial and non-financial targets, as well as the performance of the individual executive.</p> <p>50% of the bonus is deferred into a share award for a period of three years, and 50% is awarded in cash.</p> <p>Vested shares must be retained until the relevant shareholding level is reached, excluding any sold to satisfy statutory deductions. The applicable shareholding levels are detailed on page 86.</p> <p>Awards are subject to the Malus and Clawback Policy, which is reviewed annually, and is noted on page 94.</p> <p>Dividend equivalents accrue on the deferred shares, and are awarded at the end of the deferral period.</p> <p>The Committee can exercise discretion to change the bonus measures, how they are weighted, calculated and targeted. It can adjust bonus outcomes provided this is appropriate and in shareholders' interests, including adjustment downwards for current or future risk exposure, and make such amendments as are necessary to respond to regulatory, legal or accounting requirements. Shareholders will be notified if this has been carried out by disclosure in the relevant Directors' Remuneration Report.</p> | <p>The normal maximum bonus opportunity is 160% of salary.</p> <p>An additional bonus opportunity of up to a further 40% of salary may be available, at the Committee's discretion, to recognise highly exceptional circumstances. Full disclosure will be given if an increased bonus opportunity is applied.</p> <p>Actual bonus awards are linked to achievement as follows:</p> <ul style="list-style-type: none"> Below threshold – no bonus Threshold – 10% of maximum opportunity Target – 50% of maximum opportunity Maximum – 100% of maximum opportunity | <p>Performance measures and weightings are set each year considering the Company's strategy and shareholder interests, and will vary based on each Directors' area of responsibility where appropriate.</p> <p>Measures typically cover profit, underwriting performance, risk management, expenses, capital and balance sheet strength, customer and business sustainability, and objectives personal to the executive.</p> <p>A majority weighting is given to financial metrics. Measures can be assessed on a Scorecard basis.</p> <p>Performance is measured over one financial year.</p> <p>Targets are set with reference to the Group's operational plan.</p> <p>The performance measures and targets used to inform the 2016 bonus awards are on pages 90 to 92.</p> |
| <p>Long-term Incentive Plan (LTIP) (variable remuneration)</p> <p>This element supports RSA's long-term strategy, performance and priority to create shareholder value through sustained earnings and share price growth.</p> <p>The share-based nature of the plan enhances shareholder alignment.</p> | <p>Conditional long-term incentive awards are granted annually in the form of Performance Shares, and may vest wholly or partially subject to company performance conditions.</p> <p>A two-year retention period applies to vested Performance Shares, excluding any sold to satisfy statutory deductions. This applies while the Director remains in employment.</p> <p>Vested shares must be retained until the relevant shareholding level is reached, excluding any sold to satisfy statutory deductions, as detailed on page 86.</p> <p>Awards are subject to the Malus and Clawback Policy, which is reviewed annually, and is noted on page 94.</p> <p>Dividend equivalents accrue during the performance period and are added to the shares that vest.</p> <p>The Committee can act within the parameters of the Plan's rules as approved by shareholders and its performance conditions, enabling the LTIP to be appropriately administered under both normal and exceptional circumstances.¹ The Committee can make such amendments as may be necessary to respond to legal, accounting or regulatory changes. Awards can be reduced or otherwise amended, provided the action is fair and justifiable, for example, to guard against a windfall award or the converse generated by an accounting treatment. Vesting can be adjusted downwards for current or future risk exposure.</p> | <p>The normal maximum LTIP opportunity is 230% of salary.</p> <p>For recruitment purposes, or in highly exceptional circumstances, such as for retention, the Committee may agree to a conditional performance-related award being made up to an additional 170% of salary. This would be considered a 'one-off' award. Where an exceptional award is made, full disclosure will be given on the rationale.</p> <p>Award vesting is linked to achievement against the performance conditions as follows:</p> <ul style="list-style-type: none"> Below threshold – 0% vesting Threshold – 25% vesting Target – 62.5% vesting Maximum – 100% vesting | <p>Performance conditions are reviewed for each new cycle and set in line with the Company's operational plan, long-term strategy and considering shareholder interests.</p> <p>Measures are typically linked to value creation through performance of the Group's share price, profit, capital and balance sheet strength and underlying performance.</p> <p>The LTIP will include at least two measures. A majority weighting is given to financial metrics. Metrics can be assessed through a Scorecard.</p> <p>The performance period will normally be at least three years for all measures, with no re-testing.</p> <p>Shareholders will be consulted if material changes to the measures are proposed by the Committee.</p> <p>The measures and targets for the 2017-19 cycle are on pages 99 to 100.</p> |

Notes:

1. The current LTIP, referred to as the Performance Share Plan 2014 (PSP), was approved by shareholders at the 2014 AGM. It is also used as a vehicle for granting deferred bonus shares, and restricted shares where these are awarded as part of an Executive Director buy-out as noted on page 84.
2. The overall remuneration principles in this Policy apply across the Group. Employee remuneration packages are set with reference to the relevant competitive markets in which the Group operates, and remuneration levels therefore reflect differences in location and job role. All permanent UK-based employees are eligible to receive a bonus award, but deferral is only operated for senior leaders and where required by Solvency II. The LTIP policy provisions are the same for all other participants who receive performance-based awards, with exception to the two-year post-vesting retention period which only covers Executive Directors. LTIP award opportunities vary for individuals below the Board. Members of the Executive Team and selected senior leaders across the Group are also required to hold shares in RSA.

4. Illustrations of the Remuneration Policy's application

The following charts illustrate how Executive Directors' remuneration potential changes according to varying levels of performance achievement, and the balance between fixed and variable remuneration. The Committee's aim is that superior levels of remuneration will only be paid in return for delivering superior levels of performance. The variable element is fully flexible such that no award is guaranteed. The assumptions used in preparing these charts are noted in the table below. Figures relate to the 2017 financial year.



| Basis of calculation | Below threshold scenario | On-target scenario | Maximum scenario |
|----------------------|---|--|--|
| Scott Egan | | <ul style="list-style-type: none"> Fixed remuneration Annual Bonus 80% of salary LTIP 125% of salary (this assumes 62.5% vesting, i.e. half-way between the 25% threshold vesting and 100% maximum vesting) | <ul style="list-style-type: none"> Fixed remuneration Annual Bonus 160% of salary LTIP 200% of salary (this assumes 100% vesting of the award in the 2017-19 grant) |
| Stephen Hester | Minimum remuneration receivable: <ul style="list-style-type: none"> Fixed remuneration (includes the value of base salary and pension for 2017, and benefits based on the value included in the total remuneration 'single figure' for 2016) Annual Bonus 0% of salary LTIP 0% of salary | <ul style="list-style-type: none"> Fixed remuneration Annual Bonus 80% of salary LTIP 144% of salary (this assumes 62.5% vesting, i.e. half-way between the 25% threshold vesting and 100% maximum vesting) | <ul style="list-style-type: none"> Fixed remuneration Annual Bonus 160% of salary LTIP 230% of salary (this assumes 100% vesting of the award in the 2017-19 grant) |

Note:

1. There are no assumptions relating to share price growth or dividend equivalents included in the above scenarios.

The remuneration structure is intended to promote the long-term interests of the Company and its shareholders. The table below illustrates when each variable component of the Executive Directors' remuneration package would be delivered to them once any performance conditions or other restrictions have ended.

| Variable remuneration component | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|------|------|------------------------------|------|--|------|
| Annual Bonus Plan 2017: cash award | | ◆ | → Clawback may apply | | | |
| Annual Bonus Plan 2017: deferred shares | | ◆ | → Malus adjustment may apply | | ◆ | |
| LTIP 2017-19: performance share award | | ◆ | → Malus adjustment may apply | ◆ | → Share retention period, clawback may apply | |

◆ Year of cash bonus award, or share award granting ◆ Year of share award vesting
 → Year when any restrictions or clawback provisions have ended

Directors' Remuneration Report – continued

5. Approach to recruitment remuneration

The Committee ensures a consistent and transparent approach is taken when appointing Executive Directors to the Board, as shown in the following table. When a new Executive Director is recruited, the Committee will provide details of how the Policy has been implemented in respect of their appointment terms in the relevant Directors' Remuneration Report.

| Remuneration component | Notes on approach |
|---|---|
| Base salary | <ul style="list-style-type: none"> Set using the same approach as for existing Directors' salary reviews. The Committee can exercise discretion on the timing and level of salary reviews for newly appointed Directors reflecting the individual's development and performance in the role. |
| Benefits, pension and contractual terms | <ul style="list-style-type: none"> Same as those offered to current Executive Directors, but the Committee may exercise judgement to flex the package to accommodate any specific terms bespoke to the individual, e.g. related to health, annual leave, pension or insurance benefits. Where the Director is an internal appointee to the Board, or appointed following a corporate transaction, he/she may be permitted to retain any legacy benefits or terms at the Committee's discretion, or a buy-out may be made depending on the benefit type and circumstance. Continuity of service with the Group will be maintained. |
| Incentive awards | <ul style="list-style-type: none"> Under normal circumstances, a new Executive Director will be eligible for incentive awards in line with the usual policy as detailed on page 82. However, in exceptional circumstances, a higher bonus opportunity of up to 200% of salary may be agreed and a performance-related LTIP award may be approved by the Committee in the Director's first year of service up to the limit of 400% of salary. If the director is entered into an RSA LTIP and made an award of Performance Shares, these will be subject to the same performance conditions and vesting terms as applies to other plan participants. |
| Buy-outs | <ul style="list-style-type: none"> Where the Director is an external appointment, the Committee may agree to a compensatory package reflecting the value and terms of incentives or benefits forfeited upon resignation. <ul style="list-style-type: none"> This will only be permitted on receipt of reasonable evidence of loss. Typically, the form of award that is being forfeited (e.g. cash or shares) will be replaced by the same form of award at RSA. Performance-linked awards will normally only be compensated with Restricted Shares where a performance condition has been achieved or is nearing testing and there is a reasonable expectation of the vesting level. Cash bonuses may be bought out with Restricted Shares in order to give the Director an early 'stake' in RSA. The Committee may agree to reduce the value of the compensatory award below the anticipated or actual loss value if the compensation is paid at an advanced date (i.e. early settlement). Any compensatory award using cash or restricted shares will always carry a service condition and an appropriate repayment schedule to protect shareholders' interests. |

6. Service contracts and policy for payments on loss of office

Each of the Executive Directors is employed under a service agreement, which contains a variety of contractual terms and conditions. Contracts are available for inspection by shareholders at the Company's registered office. Terms are designed to ensure fair treatment for departing executives while avoiding reward for failure.

| Key terms | Notes on approach |
|-----------------------------------|---|
| Notice period | <ul style="list-style-type: none"> No Director will be appointed on a notice period exceeding 12 months. The current Executive Directors' employment can be terminated by the Company or the individual, by the serving of 12 months' notice. In the case of summary dismissal, no notice will be served by the Company and no compensation will be paid in lieu of it. Notice periods are approved by the Committee, and at its discretion, can be reduced in the event an Executive Director resigns and wishes to leave prior to the end of his or her contractual notice period. The Company can require accrued annual leave related to the year of termination to be used during a notice period or garden leave, although payment of untaken days can alternatively be made in lieu. |
| Garden leave | <ul style="list-style-type: none"> The Company has the contractual right to place the Executive Directors on garden leave for part, or all, of their notice period. Salary, benefits and pension contributions continue during garden leave, but this time will not count towards the calculation of any Annual Bonus award that may subsequently be due. |
| Payment in lieu of notice (PILON) | <ul style="list-style-type: none"> A Director may be paid in lieu of an unexpired portion of their notice period, covering base salary, pension and benefits, regardless of which party has served notice. Generally, in the event of termination and in all cases of termination on performance grounds, PILON would be made on a phased basis subject to mitigation, and would be reduced or ceased if the Director starts to receive payment or remuneration from alternative employment. |
| Termination payment | <ul style="list-style-type: none"> There are no pre-determined special provisions for Directors with regard to compensation for loss of office. If a loss of office were to occur giving rise to a redundancy payment under prevailing employment legislation, the payment will be calculated taking account of the Director's length of service with the Group and his/her annual gross basic salary as at their employment termination date. In the normal course of events, reasonable professional fees may be paid in relation to a Director's employment termination. No payment or compensation for loss of office made to any departing Director will be disclosed if it is less than £10,000 gross. Executive Directors do not have terms which provide additional rights or payments to them in the event of a change of control, reconstruction or amalgamation of the Company. |
| Restrictive covenants | <ul style="list-style-type: none"> Restrictive covenants are in place to help protect RSA's interests should the individual leave the Company for any reason. |
| External appointments | <ul style="list-style-type: none"> Executive Directors may hold one external non-executive position of a FTSE 100 company provided this does not give rise to any conflict of interest, with the approval of the Group Nomination and Governance Committee. If there is any remuneration arising from this role, the individual can retain it. |

Directors' Remuneration Report – continued

The Committee's approach to incentive treatment for Executive Director leavers is set out in the following table. Based on the leaving circumstances and having regard of shareholders' interests, the Committee can exercise discretion to reduce or lapse awards or enable a proportion of awards to be received but only in highly exceptional circumstances and where appropriate. Shareholders will be informed if discretion is applied, and details will be provided wherever possible.

| Leaving circumstances | Approach to Annual Bonus | Approach to Deferred Bonus Shares | Approach to unvested LTIPs |
|--|---|---|---|
| Resignation or dismissal for cause | <ul style="list-style-type: none"> Not eligible if left or under notice at the date of payment. | <ul style="list-style-type: none"> Forfeited if dismissed for cause. Normally vest in line with the normal timetable if resignation. | <ul style="list-style-type: none"> Forfeited. |
| Good leavers <ul style="list-style-type: none"> At the Committee's discretion, and normally including such circumstances as planned retirement, death, disability/medical severance, transfers outside of the Group and redundancy¹ | <ul style="list-style-type: none"> Eligible for the proportion of the bonus year served. Performance is tested in line with the normal performance timetable. In cases of death in service and, with Committee discretion, medical severance, performance can be tested and awards made sooner than the scheduled date. The Committee has the discretion to make the final bonus award in cash and so waive deferral, subject to any regulatory requirements. | <ul style="list-style-type: none"> Normally vest in line with the normal timetable. In cases of death in service and, with Committee discretion, medical severance, awards can vest sooner than the scheduled date. | <ul style="list-style-type: none"> Performance is tested in line with the normal timetable. In cases of death in service and, with Committee discretion, medical severance, performance conditions can be tested early and awards vest sooner than the scheduled date. Awards vest subject to performance and time pro-rating. |
| Change of control | <ul style="list-style-type: none"> Normally good leaver treatment applies as above. Where this is the case, performance can be tested and awards made sooner than the scheduled date. | <ul style="list-style-type: none"> Awards can vest sooner than the scheduled date. The Committee can determine whether a pro-rata for time is applied to these awards. | <ul style="list-style-type: none"> Performance conditions are tested early and awards can vest sooner than the scheduled date. Vesting level determined with regard to performance and time served. |

Note:

- The Committee will make reasonable judgement on determining whether a Director qualifies for good leaver status by reason of retirement, by understanding the individual's intentions post employment termination and taking account of the context of his/her departure from the Group.

7. Legacy incentive plans

The Policy provides for any outstanding awards granted under legacy incentive plans to continue in place, although the current Executive Directors do not hold any such awards.

Existing incentive awards granted under the Remuneration Policy approved by shareholders in 2014 will continue in place.

8. Required shareholding

RSA believes it is in shareholders' interests for its executives to hold shares in the Company and build a stake in the business. They are expected to retain vested shares arising from the Company's share plans to build and maintain a minimum shareholding level.

Shareholding provisions

- Executive Directors must build up a shareholding in RSA according to specified levels, expressed as a salary multiple.
- With effect from 5 May 2017, the shareholding levels to be reached are:
 - Group Chief Executive: 300% of salary
 - Other Executive Directors: 200% of salary
- Executives have a targeted five years in which to build up their holding, commencing from the first date an unconditional share award is made to them as a Director. No shares are to be sold until the holding level is reached, except where required to cover statutory deductions.
- The shares which count towards the holding level are those held either in the executive's own right or that of immediate family members and any awarded by RSA which cease to be bound by any performance or service conditions. Vested Performance Shares count towards the holding level during the two-year retention period.
- The Committee can exercise discretion to temporarily waive or reduce the holding requirement or allow shares to be sold in exceptional business or personal circumstances (e.g. ill-health, divorce, financial hardship).
- The shareholding levels were determined with reference to the practice across the Company's benchmark peer groups.
- The Executive Directors' shareholding levels as at 31 December 2016 are noted on page 95.

9. Policy for Non-Executive Directors

The following table outlines the components of Non-Executive Directors' remuneration:

| Purpose and Strategic Link | Operation and maximum level of remuneration |
|--|--|
| Fees <ul style="list-style-type: none"> This element ensures competitive remuneration is paid to attract high calibre non-executives and recognise their time commitment on the Board. | <ul style="list-style-type: none"> Non-Executive Directors (aside from the Chairman) receive a base fee, further fees are then paid to reflect membership of a committee, and for chairing a committee. A separate fee is paid to the Senior Independent Director. The Chairman receives a fee for his role and this is set by the Committee. Director Fees will not exceed the limit stated in the Company's Articles of Association, as approved by shareholders. Fees are paid in cash, subject to any required statutory deductions. Fees are reviewed annually but an annual increase may not always be applied. When assessing fee levels, account is taken of the required time commitment and the degree of expertise necessary to fulfil the particular role (such as chairing a committee). The fees are benchmarked using the same peer groups as for the Executive Directors' remuneration, and will have regard to the market median. The Company has the discretion to introduce new fees or change the Non-Executive Directors' terms. Details of the Chairman's fee and the Non-Executive Directors' fees earned for 2016 are noted on page 90. |
| Other key terms of office <ul style="list-style-type: none"> Reflects current good governance. | <ul style="list-style-type: none"> Non-Executive Directors may claim expenses in accordance with RSA's business and travel policies, including tax thereon where such expenses do not qualify for tax relief. They receive no other benefits, but they can have RSA insurance products at a discount. As the Non-Executive Directors are not employed by the Company, they are not eligible to receive a bonus award or participate in any of RSA's share plans. Non-Executive Directors may hold shares in RSA but this is a personal matter and is not mandatory. |

Non-Executive Directors are not employed by RSA, but they are engaged on a contract for services basis. They are issued with an appointment letter for an initial three-year term, which can be extended with the Board's agreement. The term of office can end prior to its expiry with either the individual or the Company serving one month's notice, or three months in respect of the Chairman. No notice will be served by the Company in the event of gross misconduct. Appointment letters are available for inspection by shareholders at the Company's registered office.

Non-Executive Directors are expected to disclose any conflicts of interest prior to, and during, the course of their tenure. They will not participate in making a decision if any conflict is considered to impact their independence or limit their ability to discharge their duties to shareholders. Since Non-Executive Directors and the Chairman receive only fees and expenses, no individual can have a loss of office payment, although payment in lieu of notice can be made.

10. Shareholder engagement

The Committee is dedicated to maintaining an active and open dialogue with RSA's shareholders. It believes that a transparent approach on all matters connected to boardroom pay is essential for building and maintaining trust and integrity. Similarly, the Committee values constructive feedback, regardless of whether it is from an institutional investor or a retail shareholder.

When reviewing the Directors' Remuneration Policy, the Committee actively engaged its leading shareholders, and took on board their feedback when assessing whether any changes were needed.

This dialogue continues the Committee's regular engagement with shareholders, the Investment Association, Pension and Lifetime Savings Association and ISS, since the Policy was last approved by shareholders in 2014.

11. Consideration of remuneration of other employees

To provide the Committee with context when considering Executive Directors' remuneration, and when developing the Policy, it received background information on the remuneration of the Group's employees in general (for example, information on employee salary increases). In 2016, the Company was accredited by the Living Wage Foundation as a Living Wage Employer.

While employees are not specifically consulted on the Directors' Remuneration Policy, RSA is actively committed to employee engagement and information is exchanged between employees, the Board and RSA's leaders. This takes place through a range of forums and channels, for example, through employee surveys which include questions linked to reward and town hall meetings. In addition, remuneration topics are discussed at the European Works Council (EWC).

Annual Report on Remuneration

1. Introduction

This Annual Report on Remuneration provides details of how the approved Remuneration Policy has been implemented for Directors in the financial year ended 31 December 2016, and how the Group intends to implement its Policy in 2017.

At the 2017 AGM, this report on pages 88 to 101, together with the Committee Chairman's letter on pages 76 to 78, will be put to an advisory vote.

2. Information about the Group Remuneration Committee

Purpose of the Committee

The Committee determines the remuneration and contractual terms for the Executive Directors and the Executive Committee (detailed on pages 44 to 46). It approves the fee and contractual terms of the Chairman (whose profile is on page 44). In addition, it maintains oversight of remuneration decisions for roles covered by specific remuneration requirements under Solvency II, including Material Risk Takers and key governance function holders.

The decisions the Committee makes are intended to promote the ongoing success of the Group, whilst upholding the interests of shareholders, regulators, customers and other stakeholders. Consequently, it pays close attention to the Group's risk management policies, ensuring that these are considered alongside other relevant information so that its actions are balanced, appropriate and support the Group's strategy.

The Committee operates within an agreed set of terms of reference, which it reviews annually. A copy of these terms can be viewed on the Group's website at: www.rsagroup.com/termsofreference or alternatively a paper copy can be requested in writing from the Group Company Secretary.

Committee members

The Committee comprises a number of independent Non-Executive Directors who are called upon to exercise judgement on the setting and management of executive remuneration. The Committee's members in 2016 were: Hugh Mitchell (Chairman), Kath Cates (from 1 January to 30 June), Enrico Cucchiani, Isabel Hudson (from 1 November), Joseph Streppel, Martin Strobel (from 1 May) and Johanna Waterous. The number of meetings attended by each Director are shown on page 49.

Committee attendees

At the invitation of the Committee, the Chairman, Group Chief Executive and designated representatives from functions within the business attend meetings to advise on Group strategy, risk, performance, and HR policies and practices, and support the Committee's work.

None of these individuals are present if their own remuneration is being discussed.

Committee attendees during 2016 included the Group Chief Operating Officer, Group Chief Legal Officer & Company Secretary, Group Reward Director and Head of Executive Compensation. Additional input was provided by the Group Chief Risk Officer.

Committee advisers

PricewaterhouseCoopers (PwC) was appointed by the Committee as its independent adviser in September 2012. It was selected following a market tender exercise. During 2016, PwC also provided advice and consultancy services across the Group globally on matters including business processes and transformation, IT risk assurance, internal audit, corporate social responsibility, direct and indirect tax, and governance. PwC is a member of the Remuneration Consultants' Group and a signatory to its Code of Conduct. In addition, the Committee has satisfied itself that the advice it receives is objective and independent as the firm has confirmed there are no conflicts of interests arising between it, its advisers and RSA. The fee paid for services to the Committee in the year was £93,700 excluding VAT, based on a fixed fee for a defined scope of work and hourly rates for specific projects.

Committee meetings held in 2016

In 2016, the Committee met on six occasions and the table below summarises the matters it discussed.

| Meeting | Regular items | Additional items |
|----------------------------|--|--|
| February (two meetings) | <ul style="list-style-type: none"> Review of Directors' base salaries effective from 1 April 2016 Testing of the performance conditions underpinning the Annual Bonus Plan 2015 and the LTIP cycle 2013-15; approval of the level of Directors' awards Approval of 2016 incentive performance conditions Approval of the terms of the long-term incentive grant 2016 and Directors' associated conditional share awards Review of Executive Directors' personal goals for 2016 Review of the Directors' Remuneration Report 2015 | <ul style="list-style-type: none"> Sharesave and Sharebuild participation update |
| May | <ul style="list-style-type: none"> Review of the 2016 long-term incentive grant and an update on dilution levels Approval for a supplementary grant of conditional long-term incentive awards in November 2016 for non-Board employees | <ul style="list-style-type: none"> Corporate governance and Solvency II update |
| August | <ul style="list-style-type: none"> Review of Remuneration Policy and incentive structure for 2017 onwards | <ul style="list-style-type: none"> None |
| September | <ul style="list-style-type: none"> Review of incentive performance measures for 2017 onwards Review of Chairman's fee effective from 1 January 2017 Approval of Solvency II PRA return Approval to operate Sharesave and Sharebuild in 2016 Approval of revised Remuneration Committee terms of reference | <ul style="list-style-type: none"> Corporate governance update |
| December | <ul style="list-style-type: none"> Update on the Annual Bonus Plan 2016 and long-term incentive cycles 2014, 2015 and 2016 Review of the draft Directors' Remuneration Report 2016 Update on the supplementary grant of conditional long-term incentive awards in November 2016 for non-Board employees Review of Committee meeting schedule for 2017 | <ul style="list-style-type: none"> Shareholder engagement update Corporate governance update UK pension scheme update |

Directors' Remuneration Report – continued

3. Total remuneration 2016: 'single figure' tables (audited)

The tables below set out the Directors' total remuneration single figure for the financial year ended 31 December 2016. For comparative purposes, 2015 figures are also provided. The fee structure applicable to Non-Executive Directors is detailed on page 100.

Executive Directors

| (£'000) | Salary | | Taxable benefits ¹ | | Bonus ² | | LTIP | | Pension related benefits | | Other remuneration | | Total | |
|-------------------------------|--------------|--------------|-------------------------------|-----------|--------------------|--------------|-------------------|-------------------|--------------------------|------------|--------------------|-------------------|--------------|--------------|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 ³ | 2015 ⁴ | 2016 ⁵ | 2015 | 2016 | 2015 ⁶ | 2016 | 2015 |
| Scott Egan ⁷ | 525 | 131 | 23 | 6 | 722 | – | – | – | 79 | 13 | – | 1,605 | 1,349 | 1,755 |
| Stephen Hester ⁸ | 964 | 950 | 69 | 71 | 1,550 | 1,163 | 1,453 | – | 289 | 285 | – | – | 4,325 | 2,469 |
| Richard Houghton ⁹ | – | 174 | – | 7 | – | – | – | – | – | 23 | – | – | – | 204 |
| Total | 1,489 | 1,255 | 92 | 84 | 2,272 | 1,163 | 1,453 | – | 368 | 321 | – | 1,605 | 5,674 | 4,428 |

Non-Executive Directors

| (£'000) | Fees | | Taxable benefits ¹ | | Total | |
|------------------------------|--------------|------------|-------------------------------|-----------|--------------|------------|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| Alastair Barbour | 95 | 95 | 17 | 21 | 112 | 116 |
| Kath Cates | 92 | 90 | 1 | 1 | 93 | 91 |
| Enrico Cucchiani | 67 | 70 | 8 | 6 | 75 | 76 |
| Isabel Hudson ¹⁰ | 28 | – | – | – | 28 | – |
| Hugh Mitchell | 90 | 90 | 6 | – | 96 | 90 |
| Martin Scicluna | 400 | 400 | – | 9 | 400 | 409 |
| Joseph Streppel | 83 | 83 | 3 | 3 | 86 | 86 |
| Martin Strobel ¹¹ | 50 | – | 3 | – | 53 | – |
| Johanna Waterous | 95 | 95 | – | – | 95 | 95 |
| Total | 1,000 | 923 | 38 | 40 | 1,038 | 963 |

Notes:

1. Taxable benefits: This includes reimbursement in respect of travel and accommodation. Stephen Hester received a car allowance and the use of a car and driver service which totalled £44,614 (2015: £46,024). Scott Egan received a car allowance of £15,000, and each of the Executive Directors were provided with medical benefits and life cover. Alastair Barbour received benefits of £17,057 (2015: £20,936) for taxable travel where relief under HMRC rules is not available.
2. Bonus: This comprises awards in respect of performance measures relating to the financial year shown, in accordance with the plan described on pages 90 to 92. Half of the bonus shown is awarded in Deferred Bonus Shares which vest three years from the date of grant, and are subject to malus adjustment under the Group's Malus and Clawback Policy detailed on page 94.
3. LTIP 2016: Estimated value of Performance Shares and accrued dividend equivalents that are due to vest on 19 May 2017. Estimate is given on the basis that the performance conditions have been satisfied as explained on pages 92 to 93, using an average share price over the last quarter of 2016 of £5.5118.
4. LTIP 2015: Performance-based awards granted under the 2013-15 LTIP cycle lapsed in full on 3 April 2016. Neither Scott Egan or Stephen Hester had awards in this cycle.
5. Pension 2016: Scott Egan was a member of the RSA Pension Scheme until March 2016 and received an employer pension contribution of 15% of salary. He received a taxable cash allowance of 15% of base salary from April 2016 onwards. Stephen Hester received a taxable cash allowance of 30% of base salary. The aggregate value paid by the Company into the RSA Pension Scheme (a defined contribution plan) for the Executive Directors in 2016 was £19,688 (2015: £13,125). No Executive Director has a prospective entitlement to a defined benefit pension in respect of their service with RSA.
6. Other remuneration 2015: The figure for Scott Egan includes compensatory cash and share-based awards made as part of his appointment to replace cash awards forfeited on leaving his previous employer, detailed on page 73 of the 2015 Annual Report and Accounts.
7. Scott Egan was appointed as a Director effective 1 October 2015 on an annual salary of £525,000. The salary value shown in the table for 2015 is the pro-rated amount based on his appointment date.
8. Stephen Hester received an annual base salary of £950,000 from 1 January to 31 March 2016. This increased by 2% to £969,000 effective 1 April 2016, as detailed on page 80 of the 2015 Annual Report and Accounts.
9. Richard Houghton resigned from the Board effective 7 May 2015 and his employment ended effective 10 July 2015.
10. Isabel Hudson was appointed as a Non-Executive Director effective 1 August 2016.
11. Martin Strobel was appointed as a Non-Executive Director effective 1 May 2016.

4. Components of variable remuneration

Annual Bonus Plan 2016 (audited)

For the 2016 financial year, the Executive Directors' Annual Bonus Plan consisted of financial and business targets aligned to the Group's operational plans. These included: Group underlying Return on Tangible Equity (ROTE), Group underlying Profit before Tax (PBT), Group Combined Operating Ratio (COR), a Business Review Scorecard and role-specific personal objectives. Overall, these targets required demanding business improvements from the prior year.

The normal maximum bonus opportunity was 160% of salary, of which half of any award is deferred into RSA shares for three years. Bonus awards are subject to malus and clawback provisions, as detailed on page 94.

In determining 2016 bonus awards under this Plan, the Committee considered how goals had been met, ensuring that performance also took account of key risk factors.

Financial performance (40% weighting – achieved 40%)

As shown in the table below, RSA's financial performance for each metric was excellent, leading to an outcome under this element of 40%. Record underwriting and combined operating ratio results and a 42% increase in underlying EPS highlight the significance of the 2016 performance in tough market conditions.

Business Review performance (30% weighting – achieved 30%)

The Business Review Scorecard is designed to capture progress against underlying improvements targeted by RSA's plans. Achievement is measured against a range of objective measures, whilst being assessed using judgement in the round. It will vary from the financial metrics' outcome if these are considered over or under representative of the underlying actions of management and their results.

The Committee assessed the 2016 performance taking into account capital, risk and disposal achievements together with the progress delivering performance improvement targets.

Achievement under the Scorecard was assessed to have been exceptional across the areas targeted. In performance terms, and despite soft market conditions, underwriting profit rose sharply to all time record levels for RSA. Attritional loss ratio improved 1.5% points vs 2015 and 0.9% points vs Plan. Controllable cost savings reached £292m, and Group Controllable Expenses were £17m better than Plan. Cost ratios also improved vs prior year.

From a strategic perspective, the 'focus' strategy is already paying off in terms of performance. The final disposals to implement the strategy were successfully closed (Russia & Latin America), raising to £1.2bn total disposal proceeds, well above expectations. Solvency II has bedded in well and the Group's capital position strengthened vs last year and vs published targets despite intense market volatility. Debt buyback was successfully completed. UK pension risk reduction was also executed well. Additionally, reflected in the year end accounts is the pending sale of UK legacy liabilities announced in February 2017 which is of major benefit to the Company.

Taking the above into account, the Committee noted exceptional progress vs prior year and plans, and assessed there being a close relationship between the headline financial outcomes for the year and the underlying measures of performance and management activity. As a result, an award of 30% out of a maximum score of 30% in this category was made. In light of Mr Egan's more recent appointment in Q4 2015, giving less time to influence the 2016 results, the Committee applied a scale back to Mr Egan's award, as shown in the table below.

| Bonus 2016 performance measures | | 2015 Result | 2016 Target ¹ | Actual | Weighting (% of maximum) | Scott Egan (% of maximum) | Stephen Hester (% of maximum) |
|---------------------------------|--|-------------|--|---------------|--------------------------|---------------------------|-------------------------------|
| Group underlying ROTE | | 9.7% | Threshold 10.2% Target 11.3% Maximum 12.4% | 14.2% | 20% | 20% | 20% |
| Group underlying PBT | | £417m | Threshold £394m Target £438m Maximum £482m | £556m | 10% | 10% | 10% |
| Group COR | | 96.9% | Threshold 96.4% Target 95.4% Maximum 94.4% | 94.2% | 10% | 10% | 10% |
| Business Review Scorecard | – Capital metrics: | | | | | | |
| | <i>Solvency II coverage ratio</i> | N/A | ≥130% | 158% | 30% | 23% ⁴ | 30% |
| | <i>TNAV/NWP</i> | 42% | ≥35% | 45% | | | |
| | <i>S&P credit rating</i> | A stable | ≥A– stable | A stable | | | |
| | – Group controllable expense ratio: ² | 25.6% | 23.4% | 23.3% | | | |
| | – Group controllable expenses: ² | £1,767m | £1,532m | £1,515m | | | |
| | – Attritional loss ratio: ³ | 50.8% | 50.2% | 49.3% | | | |
| – Strategic plan initiatives: | | | See narrative | See narrative | | | |
| Personal Scorecard | | | | See narrative | 30% | 23% | 30% |
| Total (% of maximum) | | | | | 100% | 86% | 100% |
| Total (% of annual base salary) | | | | | | 137.6% | 160.0% |
| Bonus receivable ⁵ | | | | | | £722,400 | £1,550,400 |

Notes:

- During the year, targets for the financial metrics were reviewed with the thresholds being made tougher. For reference, the original thresholds set at the beginning of the year for the measures were: Group underlying ROTE 9.1%, Group underlying PBT £350m, Group COR 98.4%.
- 2015 results are adjusted for the timing of business disposals.
- Defined on a Core Group basis excluding Claims Handling Expenses (which are part of the expense measure).
- Modified down from 30% to 23% in light of Mr Egan's tenure in role, giving less time to influence the 2016 results.
- Half of the bonus is awarded in Deferred Bonus Shares which vest three years from the grant date, and are subject to malus adjustment as on page 94.

Directors' Remuneration Report – continued

Personal element

This element focuses on personal performance vs the priorities set by the Board for the Executive Directors in 2016. The Committee noted strong achievement in respect of these areas, as shown in the following tables:

Scott Egan, Group Chief Financial Officer (30% weighting – achieved 23%)

| Overview | Progress |
|---|---|
| Scott's objectives covered business planning, benchmarking and functional improvements, delivering financials and capital plans, and risk and stakeholder engagement targets. | <ul style="list-style-type: none"> – Financial and capital results as set out above. – Completed disposals, pension risk reduction and debt buyback, and led delivery of the UK legacy sale. – Functional improvements and transformation programme rated green. – In his first full year as CFO, Scott has grown substantially, becoming increasingly influential to results and exceeding expectations. |

Stephen Hester, Group Chief Executive (30% weighting – achieved 30%)

| Overview | Progress |
|---|---|
| Stephen's objectives focused on strategy, financial performance, risk management, stakeholder relations and culture/team strengthening. | <ul style="list-style-type: none"> – Stephen has been a driving force in RSA's 2014–16 improvements. All primary objectives for 2016 were met or exceeded as detailed elsewhere in this Annual Report. – In relation to the intangible achievements of RSA under Stephen's leadership, there is particular appreciation of the team building and culture change driven by him that is transforming RSA's performance capabilities and ambitions vs prior years. |

As a result, Mr Hester was awarded a total bonus of 100% of the maximum, and Mr Egan 86% of the maximum.

Long-term incentive awards vesting from 2014–16 cycle (audited)

Conditional long-term incentive awards were granted in 2014. In 2017, these Performance Shares will partially vest, based on the achievement of the performance conditions, as shown below:

| Performance measures 2014–16 | Threshold target: 25% vesting | Maximum target: 100% vesting | Actual | Weighting | Vesting (% of maximum) |
|--|---|---|---------------|-------------|------------------------|
| Relative TSR ^{1,2} | RSA's TSR is equal to the unweighted index of comparators | RSA's TSR outperforms the unweighted index of comparators by at least 7% per annum (22.5% compound over three years) or exceed the TSR of the highest performing company in the index | Below index | 33.33% | 0% |
| Group underlying ROTE ³ | 11% | 16% | 11.2% | 33.33% | 9.33% |
| Business Review Scorecard ⁴ | See narrative | See narrative | See narrative | 33.33% | 33.33% |
| Total | | | | 100% | 42.7% |

Notes:

1. Provisional result: Relative TSR in the 2014–16 cycle is measured over a period which began four weeks prior to the grant date in 2014 and will end on 31 March 2017; this was to ensure the performance period did not begin during a time when shareholders were not in possession of the full information on RSA's performance and strategy. Therefore, the vesting outcome on the TSR measure will be finalised following 31 March 2017. The provisional vesting outcome shown is based on the position as at 21 February 2017 when RSA TSR was 26% and the index of comparators was 44%. If there is any difference between the provisional outcome and the final outcome, it will be shown in the Directors' Remuneration Report for 2017.
2. Relative TSR index of comparators includes: Admiral, Allianz, Aviva, Chubb (formerly ACE), Direct Line, Gjensidige Forsikring, Hiscox, Intact, Mapfre, QBE, Topdanmark, Tryg and Zurich. Amlin and Catlin had originally been included in the index, however they were delisted during the performance period and so the Committee determined to exclude them from the calculation. A straight-line calculation is applied to determine the portion of awards that vest for performance between the threshold and maximum targets.
3. Group underlying ROTE is calculated on a three-year average basis. A straight-line calculation was applied to determine the portion of awards that vest for performance between the threshold and maximum targets.
4. The Scorecard outcome has been determined by the Committee on a provisional basis only. The final outcome will be confirmed shortly after the Annual Results are published. If there is any difference from the provisional outcome, it will be shown in the Directors' Remuneration Report for 2017.

Business Review Scorecard

The LTIP Business Review Scorecard vesting outcome was determined by the Committee assessing the Company's progress since the turnaround plan was actioned in 2014 and focusing on the cumulative result over three years of the action plan measures, particularly relating to strategy implementation, capital recovery and earnings improvement. A related assessment has been carried out annually as part of Annual Bonus setting with Group Chief Executive awards of 25/30, 27/30 and 30/30 respectively, as evidence of successful delivery became successively clearer. Metrics considered by the Committee are set out in the following table.

During the 2014–16 period, the Committee assessed the Scorecard performance as outstanding. As is normal in turnaround situations, it has not been until 2016 that financial results and share price movement have more fully reflected the effort and impact of the turnaround actions that commenced in 2014. As a result, the overall expected vesting level of the 2014–16 LTIP grant is just 42.7%. Nevertheless, the actions taken during the period are having exceptional impact on the company's performance which the Committee is recognising in its assessment of the Business Review element of the LTIP Scorecard.

In challenging market conditions, underwriting performance went from loss making to record levels. Attritional loss ratio improved by an unprecedented 4.1% points. The cost savings target set in 2014 was substantially exceeded, and targets revised upwards three times. Disposal proceeds substantially exceeded expectations, as did capital improvement across all measures.

| Strategic priority | Key performance indicators | Target | Actual | | |
|----------------------|---|--|----------|-------|-------|
| Capital | | | 2014 | 2015 | 2016 |
| | IGD coverage ratio ¹ | ≥175% | 224% | 216% | – |
| | ECA coverage ratio ¹ | ≥115% | 131% | 140% | – |
| | Solvency II coverage ratio ¹ | ≥130% | – | 143% | 158% |
| | TNAV:NWP ² | ≥35% | 39% | 42% | 45% |
| | | | 2014–16 | | |
| | S&P credit rating | ≥A– stable | A stable | | |
| Business performance | | | 2014–16 | | |
| | Cumulative earnings ³ | £907m | £1,122m | | |
| | TNAV growth per share ⁴ | 103.4p | 146.2p | | |
| | Controllable cost savings ² | >£180m by 2016 | £292m | | |
| | Disposal proceeds ² | £1,024m | £1,239m | | |
| | | | 2014 | 2015 | 2016 |
| | Attritional loss ratio ^{2,5} | Improvement on prior year (2013: 53.4%) | 51.9% | 50.8% | 49.3% |

Notes:

1. Solvency II coverage ratio was introduced as a measure of capital strength to reflect the new Solvency II regime implemented from 1 January 2016, replacing IGD and ECA, as noted in the 2015 Annual Report and Accounts on page 67.
2. These indicators were not separately listed in the Scorecard Key Performance Indicators but were key underlying targets and reviewed by the Committee as additional context on the transformation.
3. Defined in common with the underlying ROTE measure of earnings adjusted for disposal gains and restructuring charges which were also key management activities. The Committee assessed all other items falling outside of this definition to determine if they should adjust the Committee's view of progress upwards or downwards (namely non-cash, non-capital accounting items). Comparison is versus original 2014–16 Plans incorporating the planned costs and benefits of the additional cost programmes announced subsequently.
4. TNAV growth per share assessed consistent with the methodology in note 3. Market volatility (FX, Bonds, Pensions) was separately considered, though the target was exceeded with or without this adjustment.
5. Defined on a Core Group basis excluding Claims Handling Expenses (which are captured in the expense measure).

Vesting overview

| Director | Granted number of shares | Vesting number of shares | Estimated value (including dividend equivalents) ¹ |
|----------------|--------------------------|--------------------------|--|
| Stephen Hester | 585,431 | 249,784 | £1,453,258 |

Notes:

1. Estimate includes vesting Performance Shares valued at £1,376,760 and accrued dividend equivalent shares valued at £76,498 which will be added to the awards that vest. Valued using an average share price over the last quarter of 2016 of £5.5118.
2. Scott Egan was appointed in 2015, and does not have awards in this cycle.

Directors' Remuneration Report – continued

Long-term incentive awards granted in 2016 (audited)

Conditional long-term incentive awards were made to the Group Chief Executive and Group Chief Financial Officer on 4 March 2016. These Performance Share awards will vest in 2019, subject to the satisfaction of the plan's performance conditions based on Group underlying ROTE, relative Total Shareholder Return and a Business Review Scorecard. The Scorecard measures a range of indicators on an underlying basis, and includes: growth in Tangible Net Asset Value per Share (TNAV), cumulative earnings, controllable expenses, attritional loss ratio and a range of capital strength metrics including the ratio of TNAV:NWP and Solvency II coverage ratio.

The targets for the performance measures are shown in the following table. Achievement against the Business Review Scorecard will be evaluated using a performance framework whereby each metric will be reviewed against its target, and judgement in the round used to determine the level of vesting, taking into account underlying business performance indicators and any material risk items. The specific targets cannot be disclosed prospectively for commercial reasons, including price sensitivity. A performance narrative will be given to summarise the level of vesting on the Business Review Scorecard once the performance conditions have been tested.

| Performance measures 2016–18 | Weighting | Threshold target: 25% vesting | Maximum target: 100% vesting |
|------------------------------------|-----------|---|--|
| Relative TSR ¹ | ⅓ | RSA's TSR is equal to the unweighted index of comparators | RSA's TSR outperforms the unweighted index of comparators by at least 7% per annum (22.5% compound over three years) or exceeds the TSR of the highest performing company in the index |
| Group underlying ROTE ² | ⅓ | 11% | 16% |
| Business Review Scorecard | ⅓ | Commercially sensitive | Commercially sensitive |

Notes:

1. Relative TSR index of comparators includes: Admiral, Allianz, Aviva, Chubb, Direct Line, Gjensidige Forsikring, Hiscox, Intact, Mapfre, QBE, Topdanmark, Tryg and Zurich. A straight-line calculation is applied to determine the portion of awards that vest for performance between the threshold and maximum targets.
2. Group underlying ROTE will be calculated on a three-year average basis. A straight-line calculation is applied to determine the portion of awards that vest for performance between threshold and on-target, and between on-target and maximum. The average required for on-target vesting (62.5% vesting) is less than the mid-point of the 11–16% range and is considered commercially sensitive because it is set reflecting a growing performance expectation over the three years, and therefore signals the Group's plan for the period. Disclosure will be provided retrospectively following the end of the performance period.

The awards granted are set out in the table below:

| Director | Performance Shares ^{1,2} | | |
|----------------|-----------------------------------|-------------------------------|-------------------------|
| | Basis of award | Number of shares ³ | Face value ⁴ |
| Scott Egan | 200% of salary | 238,030 | £1,050,000 |
| Stephen Hester | 230% of salary | 505,236 | £2,228,700 |

Notes:

1. The performance measures are Group underlying ROTE, Relative TSR and a Business Review Scorecard (⅓ weighting each).
2. The performance period is three years and ends on 31 December 2018.
3. If threshold performance is achieved, 25% of the number of shares shown will vest.
4. The face value of the award is calculated as the maximum number of shares that would vest if all performance measures and targets are met, multiplied by the mid-market closing price of an RSA ordinary share averaged over the five business days preceding the date of grant (4 March 2016), of £4.4112.

Malus and Clawback Policy

The Group operates a Malus and Clawback Policy which is reviewed annually, as set out in the Remuneration Policy on page 82. In summary, for awards issued in 2014 onwards, the Committee has the ability to reduce or forfeit awards that have yet to be paid or vest in the case of shares, to delay the payment or vesting date or to amend another form of award or benefit which has yet to be received (malus adjustment). For cash bonuses awarded for 2015 performance onwards, and long-term incentive awards granted from 2015 onwards, the Committee may also recover sums already paid to Executive Committee members if it considers it appropriate to do so (clawback). This can be applied during a two-year period after receipt (in the case of cash bonuses) or vesting (in the case of long-term incentives).

The circumstances in which malus and clawback may apply are outlined in the table below:

| Malus adjustment | Clawback |
|--|---|
| Material financial misstatement of results for any financial year or the material financial loss/under-performance of a business unit that could have been reasonably risk-managed | Material financial loss of a business unit as a result of circumstances that should reasonably have been risk-managed by the individual |
| Error or material misstatement leading to an overpayment | Material error or financial misstatement of results which has resulted in an overpayment |
| Employee misconduct, including regulatory or other breaches | Gross or serious employee misconduct. |
| Legitimate concerns regarding an employee's conduct, capability or performance | |
| Actions leading to reputational damage | |
| Deterioration in the financial health of the Company leading to severe financial constraint | |
| Any other situation as the Committee may reasonably determine. | |

5. Directors' shareholding (audited)

Executive Directors' shareholding

The table below shows the Executive Directors' shareholding and their unvested scheme interests in the Company's incentive plans. Scott Egan and Stephen Hester joined RSA in October 2015 and February 2014 respectively and continue to build up their shareholdings to the target levels shown below within the targeted five-year period.

| Director | Shares owned outright ¹ | | Unvested scheme interests held at 31 December 2016 | | Required shareholding level | | | |
|----------------|------------------------------------|---------------------------------|---|---|--|------------------------|--|---|
| | Shares held at 1 January 2016 | Shares held at 31 December 2016 | Share awards subject to performance conditions ² | Share awards not subject to performance conditions ³ | Shares counting towards shareholding at 31 December 2016 | Valuation ⁴ | Shareholding level to be reached (% of salary) | Shareholding level at 31 December 2016 (% of salary) ⁵ |
| Scott Egan | – | 29,956 | 238,030 | – | 29,956 | £175,542 | 200% ⁶ | 33% |
| Stephen Hester | 21,500 | 121,500 | 1,759,869 | 242,047 | 121,500 | £711,990 | 300% | 73% |

Notes:

- Interests of Directors in Ordinary Shares of £1.00 each of the Company, including those of closely associated persons. As at 22 February 2017, the interests in Ordinary Shares of Scott Egan and Stephen Hester have not changed since 31 December 2016.
- Includes Performance Shares as detailed on page 96.
- Includes Deferred Bonus Shares as detailed on page 96.
- The valuation is against the mid-market closing price of an RSA ordinary share as at 31 December 2016 of £5.86 per share.
- The gross annual base salary as at 31 December 2016.
- Applies with effect from 5 May 2017. The level was previously 150% of salary.
- Full details of all Directors' shareholdings and options to subscribe for shares are recorded in the Group's Register of Directors' Interests which is open to inspection by shareholders at the AGM and at the Company's registered office during standard business hours. The Directors had no share options that vested and remained unexercised, or were exercised in the year.

Non-Executive Directors' shareholding

| Director | Shares held at 1 January 2016 ¹ | Shares held at 31 December 2016 ¹ |
|-----------------------------|--|--|
| Alastair Barbour | 12,039 | 12,039 |
| Kath Cates | 4,124 | 4,124 |
| Enrico Cucchiani | – | – |
| Isabel Hudson ² | 114 | 3,832 |
| Hugh Mitchell | 8,552 | 8,552 |
| Martin Scicluna | 14,303 | 14,303 |
| Joseph Streppel | 4,125 | 4,125 |
| Martin Strobel ³ | – | 12,000 |
| Johanna Waterous | 12,419 | 18,069 |

Notes:

- Interests of Directors in Ordinary Shares of £1.00 each of the Company, including those of closely associated persons. As at 22 February 2017, the interests in Ordinary Shares of the current Non-Executive Directors have not changed since 31 December 2016.
- Isabel Hudson was appointed as a Non-Executive Director effective 1 August 2016. The table above shows her shareholding as at that date and not 1 January 2016.
- Martin Strobel was appointed as a Non-Executive Director effective 1 May 2016. The table above shows his shareholding as at that date and not 1 January 2016.
- Full details of all Directors' shareholdings are recorded in the Group's Register of Directors' Interests which is open to inspection by shareholders at the AGM and at the Company's registered office during standard business hours.

Directors' Remuneration Report – continued

Scheme interests held by Executive Directors

Details of Executive Directors' existing awards in the Company's share plans for the financial year are set out in the following table. The interests shown were granted under the long-term incentive plan approved by shareholders at the 2014 AGM, the Performance Share Plan (PSP).

| | Share awards held at 1 January 2016 | Share awards granted during the year ¹ | Share awards vested during the year | Share awards lapsed during the year | Share awards held at 31 December 2016 | Grant share price | Vesting date |
|---|-------------------------------------|---|-------------------------------------|-------------------------------------|---------------------------------------|-------------------|--------------|
| Scott Egan | | | | | | | |
| Restricted Shares ² | – | 56,673 | 56,673 | – | – | £4.4112 | 4 March 2016 |
| Performance Shares 2016–18 ³ | – | 238,030 | – | – | 238,030 | £4.4112 | 4 March 2019 |
| Total | – | 294,703 | 56,673 | – | 238,030 | | |
| Stephen Hester | | | | | | | |
| Performance Shares 2014–16 ³ | 585,431 | – | – | – | 585,431 | £4.8682 | 19 May 2017 |
| Performance Shares 2015–17 ³ | 669,202 | – | – | – | 669,202 | £4.2588 | 7 April 2018 |
| Performance Shares 2016–18 ³ | – | 505,236 | – | – | 505,236 | £4.4112 | 4 March 2019 |
| Deferred Bonus Shares ⁴ | 110,247 | – | – | – | 110,247 | £4.2588 | 7 April 2018 |
| Deferred Bonus Shares ⁴ | – | 131,800 | – | – | 131,800 | £4.4112 | 4 March 2019 |
| Total | 1,364,880 | 637,036 | – | – | 2,001,916 | | |

Notes:

1. The Company granted conditional awards over Ordinary Shares under the PSP at nil cost. The number of shares was calculated based on the mid-market closing price averaged over the five business days preceding the grant date of 4 March 2016, of £4.4112.
2. Restricted Shares were granted to Scott Egan as part of his appointment as a compensatory award in respect of awards forfeited on leaving his previous employer, as detailed on page 73 of the 2015 Annual Report and Accounts. A portion of the shares were sold to cover statutory deductions during the year, the rest were retained in line with the shareholding requirements.
3. Performance Shares granted in 2014, 2015 and 2016 have performance conditions of Group underlying ROTE, Relative TSR and a Business Review Scorecard (1/3 weighting each). The dates by which performance conditions are to be met is as follows: 2014 awards by 31 December 2016 (except the Relative TSR condition, the performance period for which began four weeks prior to the grant date and will end on 31 March 2017), 2015 awards by 31 December 2017 and 2016 awards by 31 December 2018.
4. Deferred Bonus Shares vest three years from the date of grant, and are subject to malus adjustment as detailed on page 94.
5. No other Directors of the Company held long-term incentive scheme interests during the year.

6. Payments to Directors for loss of office (audited)

There were no payments to Directors for loss of office in 2016.

7. Payments to former Directors (audited)

No payments were made to former Directors in 2016.

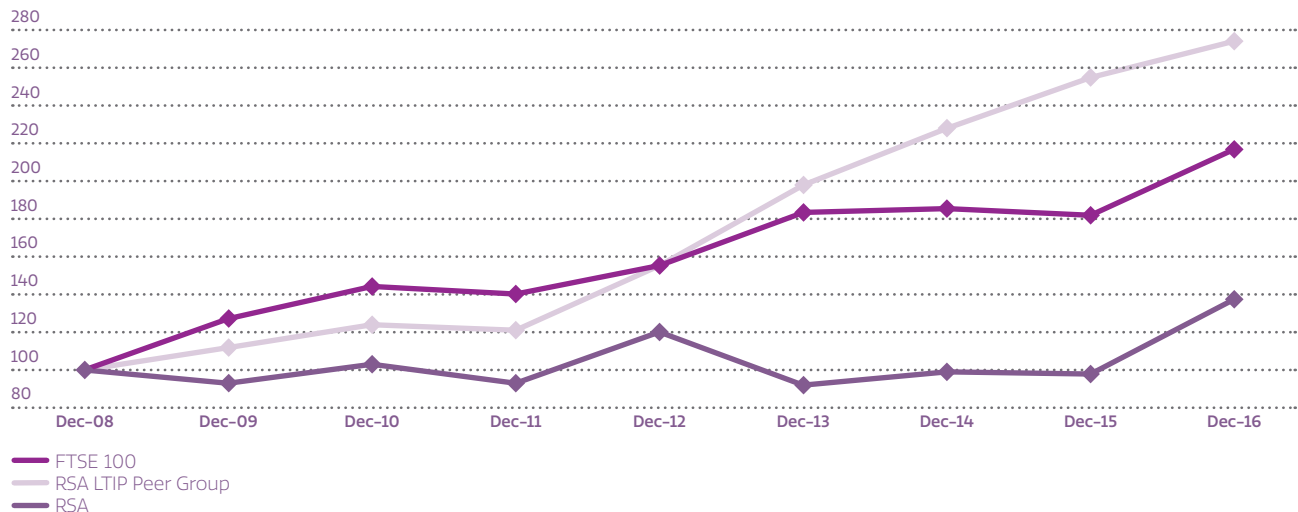
8. Historical TSR and executive remuneration

The graph shows the TSR of the Group with reference to the FTSE 100 Index and the Relative TSR peer group used as an LTIP performance measure, the constituents of which are noted on page 92.

The FTSE 100 Index is included as it comprises the 100 most highly capitalised companies in the UK market, of which RSA was a member in 2016.

RSA's TSR performance relative to the indices is shown over the eight years from 31 December 2008 to 31 December 2016. The graph reflects the change in value of Ordinary Shares in a company over time, as represented by a hypothetical £100 holding in the shares. Any distribution of dividends is included. Data was provided by Datastream.

Value of hypothetical £100 holding



The table below shows the total remuneration for the incumbents appointed as the most senior Executive Director over the past eight years. The annual bonus award rates include both cash and deferred shares components.

| | 2009 | 2010 | 2011 | | 2012 | 2013 | | 2014 | | 2015 | 2016 |
|---|------------|------------|------------|-----------|-----------|-----------|------------------------------|------------------------------|-----------------------------|-----------------------------|-----------------------------|
| Director | Andy Haste | Andy Haste | Andy Haste | Simon Lee | Simon Lee | Simon Lee | Martin Scicluna ¹ | Martin Scicluna ¹ | Stephen Hester ² | Stephen Hester ² | Stephen Hester ³ |
| Single figure of total remuneration (£'000) | 4,451 | 4,024 | 2,488 | 311 | 2,164 | 1,011 | 21 | 39 | 2,118 | 2,469 | 4,325 |
| Annual bonus award rates (% of maximum) | 89% | 73% | 58% | 59% | 50% | 0% | n/a | n/a | 68% | 77% | 100% |
| LTIP vesting rates (% of maximum) | 100% | 66% | 31% | 34% | 34% | 0% | n/a | n/a | n/a | n/a | 43% |

Notes:

1. Martin Scicluna was appointed Executive Chairman effective 13 December 2013 until 4 February 2014.
2. Stephen Hester was appointed Group Chief Executive effective 5 February 2014 and did not have any long-term incentive awards in the 2012-14 and 2013-15 cycles.
3. Details of the 2016 figures are given on pages 90 to 93.

Directors' Remuneration Report – continued

9. Percentage change in remuneration

The table below sets out the percentage change in salary, benefits and bonus for the individual undertaking the most senior Executive Director role in the Company compared with UK employees on average between 2015 and 2016. The UK population was selected for this comparison because pay changes within RSA vary significantly, according to local market factors. The Group Chief Executive's role has a Group-wide remit, but is located in the UK.

| | Salary and Fees | Taxable benefits | Bonus |
|--------------------------------|-----------------|------------------|-------|
| All employees | 2% | 2% | 34% |
| Most senior Executive Director | 2% | -3% | 33% |

10. Relative importance of spend on pay

The table below shows the all-employee pay spend and returns to shareholders by way of dividends for 2016. Figures from 2015 are provided for comparison. The employee pay data covers the Group's employees globally, and therefore includes the impact of exchange rate changes. Levels of inflation vary across the different countries in which the Group operates and, therefore, salary changes will be reflective of local market conditions.

| (£m) | 2015 | 2016 | % difference from prior year |
|--|------|------|------------------------------|
| Total Spend on Employee Pay ¹ | 948 | 804 | -15% |
| Total Distributions to Shareholders ² | 65 | 131 | 102% |

Notes:

1. Includes wages and salaries, social security costs, pension costs and share-based payments as shown in the notes to the Financial Statements on page 137.
2. Includes the figures as shown in the notes to the Financial Statements on page 140.

11. Implementation of Remuneration Policy in 2017

This section outlines how the Committee intends to implement the Directors' Remuneration Policy during 2017.

Base salary, benefits and pension

The Committee reviewed the Executive Director salary levels, taking into account the average reviews applied elsewhere in the Group, including those for employees subject to collective bargaining agreements, and UK inflation figures. It referenced a range of information including market data from two benchmarking peer groups of listed international insurers and FTSE companies of a broadly comparable market capitalisation to RSA, excluding banks and heavy industries.

This is the first time Scott Egan's salary has been reviewed since his appointment in 2015.

The table below shows the salaries that will apply from 1 April 2017. The level of increase is in line with those for other UK-based employees this year:

| Director | Annual base salary effective 1 April 2016 | Annual base salary effective 1 April 2017 | % change |
|----------------|---|---|----------|
| Scott Egan | £525,000 | £538,125 | 2.5% |
| Stephen Hester | £969,000 | £993,225 | 2.5% |

In respect of benefits and pension, the Policy will continue to be implemented the same way as it was at the end of 2016.

How will incentives be aligned to the business strategy in 2017?

The table below shows how the business strategy, and the key performance indicators which underpin it, are reflected in the Annual Bonus Plan and long-term incentive performance measures for Executive Directors in 2017:

| Strategic priorities | Annual Bonus Plan 2017 | Long-term incentive cycle 2017-19 |
|---------------------------|--|-----------------------------------|
| • Shareholder Value | Group underlying ROTE | Relative TSR |
| • Profitability | Group underlying PBT Group COR | Group underlying ROTE |
| • Risk and Resilience | Business Scorecard: Risk and Resilience: Regulatory capital ratios, credit rating, capital actions, risk management; | |
| • Underlying Performance | Underlying Performance: Attritional loss ratio, total controllable costs/cost ratios, key business improvement projects; | |
| • Business Sustainability | Business Sustainability: Customer franchise and other relevant actions related to the Company's long-term success including People and Corporate Social Responsibility | |

Annual Bonus Plan 2017

As noted in the Committee Chairman's letter on pages 76 to 78, the Annual Bonus Plan is aligned with the core priorities for focus in 2017. The Executive Directors will be expected to deliver against stretching targets, which are geared towards making continued performance improvement. They are targeted against the performance of the entire Group, taking into account their contribution thereto.

The Business Scorecard component focuses on key areas of management activity essential to the success of the Company including Risk and Resilience, Underlying Performance and Business Sustainability (including Customer franchise). The Personal Scorecard consists of 'SMART' objectives bespoke to each Director, with a focus on both 'what' is achieved and 'how' goals are delivered.

Half of the total bonus will be awarded in cash where clawback can apply, the balance is deferred into shares for a three-year period where malus adjustment can apply.

The Committee will assess performance for 2017 once the financial year has ended, taking into account material risk factors. All of the bonus targets are considered to be commercially sensitive because they signal the Group's forward plan for the year, and therefore they are not provided in this document. Disclosure will be provided in the 2017 Directors' Remuneration Report, to the extent that the targets do not remain commercially sensitive.

The table below sets out the structure of the Executive Directors' bonus plan for 2017:

| Bonus performance measures | Weighting (% of bonus) | Maximum opportunity (% of salary) |
|---|---------------------------|--------------------------------------|
| Group underlying Return on Tangible Equity (ROTE) | 20% | 32% |
| Group underlying Profit before Tax (PBT) | 10% | 16% |
| Group COR | 10% | 16% |
| Business Scorecard | 30% | 48% |
| Personal Scorecard | 30% | 48% |
| Total | 100% | 160% |

Long-term incentive 2017-19

The plan directly supports the building of shareholder value by targeting Group underlying Return on Tangible Equity (ROTE), relative Total Shareholder Return (TSR) and a Business Scorecard.

For the 2017 grant, performance measures will be assessed against a performance period of 1 January 2017 to 31 December 2019, taking into account underlying business performance and material risk factors.

To maintain an appropriate degree of stretch in the targets, the three-year average required for an on-target level of vesting on the Group underlying ROTE element is positioned requiring improved underlying performance vs 2016 record results. The performance range has been increased to 12-18%, compared to 11-16% for the 2016-18 cycle.

The Business Scorecard measures a range of indicators on an underlying basis, and includes: regulatory capital ratios, credit rating, capital actions, risk management, attritional loss ratio, total controllable costs/cost ratios, key business improvement projects, customer franchise and other relevant actions related to the Company's long-term success.

In contrast to the Business Scorecard in the Annual Bonus, which will capture calendar year actions and outcomes relative to RSA's business plan, the long-term incentive Scorecard will capture progress over three years vs the Company's strategy and three-year Operating Plans.

The Business Scorecard will be evaluated using a performance framework whereby each metric will be reviewed against its target, together with any other aspects connected to the business performance and judgement in the round used by the Committee to determine the level of vesting. The specific targets cannot be disclosed prospectively for commercial reasons, including price sensitivity. A performance narrative will be given to summarise the level of vesting on the Scorecard once the performance conditions have been tested.

Directors' Remuneration Report – continued

The Committee has approved in principle that Stephen Hester's Performance Share opportunity in the 2017-19 LTIP grant will be 230% of salary at maximum vesting, which is the usual level of award for the Group Chief Executive; and that Scott Egan's opportunity will be 200% of salary at maximum vesting. Executive Directors must retain all vested shares arising from this incentive plan for two years post-vesting (except those sold to cover statutory deductions), and they are subject to the Group's Clawback Policy. The table below summarises the LTIP's structure.

| Performance measures 2017-19 | Weighting | Threshold target: 25% vesting | Maximum target: 100% vesting |
|------------------------------------|-----------|---|--|
| Relative TSR ¹ | 1/3 | RSA's TSR is equal to the unweighted index of comparators | RSA's TSR outperforms the unweighted index of comparators by at least 7% per annum (22.5% compound over three years) or exceeds the TSR of the highest performing company in the index |
| Group underlying ROTE ² | 1/3 | 12% | 18% |
| Business Scorecard | 1/3 | Commercially sensitive | Commercially sensitive |

Notes:

1. The TSR index of comparators for this cycle includes: Admiral, Allianz, Aviva, Chubb, Direct Line, Gjensidige Forsikring, Hiscox, Intact, Mapfre, QBE, Topdanmark, Tryg and Zurich. A straight-line calculation is applied to determine the portion of awards that vest for performance between the threshold and maximum targets.
2. Group underlying ROTE will be calculated on a three-year average basis. A straight-line calculation is applied to determine the portion of awards that vest for performance between threshold and on-target, and between on-target and maximum. The average required for on-target vesting (62.5% vesting) is positioned requiring demanding increases in underlying performance vs 2016 and is considered commercially sensitive because it is set in line with, and therefore signals, the Group's forward plan for the period. Disclosure will be provided retrospectively following the end of the performance period.

Non-Executive Directors' fees

The Committee reviewed the Chairman's fee in accordance with the Remuneration Policy, and did so referencing a range of information including market data on fees taken from the same peer groups used to benchmark the Executive Directors' salaries, UK inflation figures and the average reviews applied elsewhere in the Group. The fee, which has remained unchanged since Mr Scicluna's appointment in January 2013, will rise by 5% from £400,000 to £420,000 with effect from 1 January 2017.

Under the Company's Articles of Association, the Non-Executive Directors' remuneration is determined by the Board, within limits set by shareholders. The Chairman and Board (minus the Non-Executive Directors) discharges its accountability for setting and managing Non-Executive Directors' remuneration; it will do this when their contractual terms or fee structure are under consideration, which is typically once a year, as noted on page 87.

The current Non-Executive Director fee structure has been in place since July 2013. The Company reviewed the Non-Executive Directors' fees during 2016 in accordance with the Remuneration Policy and the fees effective from 1 January 2017 are shown in the following table.

| Fee structure | From 1 July 2013 | From 1 January 2017 |
|--|------------------|---------------------|
| Base fee | £60,000 | £62,500 |
| Additional fee for chairing committees: | | |
| Group Audit Committee | £20,000 | £20,000 |
| Group Remuneration Committee | £20,000 | £20,000 |
| Group Investment Committee | £12,500 | £12,500 |
| Board Risk Committee | £20,000 | £20,000 |
| Additional fee for Senior Independent Director | £20,000 | £20,000 |
| Additional committee fee ¹ | £5,000 | £5,000 |

Note:

1. A fee of £5,000 applies for each committee a Non-Executive Director is a member of other than as Committee Chairman.

12. Statement of voting at General Meeting

The following voting was recorded at the AGM on 6 May 2016 regarding the resolution to approve the Annual Report on Remuneration:

| Resolution | Votes for | Votes against | Total votes cast | Votes withheld ¹ |
|---|-------------|---------------|------------------|-----------------------------|
| To approve the Directors' Remuneration Report | | | | |
| Number of votes | 684,660,846 | 41,745,807 | 726,406,653 | 2,358,792 |
| % of votes cast | 94.25% | 5.75% | 100% | – |

The most recent resolution to approve the Directors' Remuneration Policy was at the AGM on 9 May 2014, where the following voting was recorded:

| Resolution (2014 AGM) | Votes for | Votes against | Total votes cast | Votes withheld ¹ |
|---|---------------|---------------|------------------|-----------------------------|
| To approve the Directors' Remuneration Policy | | | | |
| Number of votes ² | 3,309,027,861 | 106,612,562 | 3,415,640,423 | 100,893,815 |
| % of votes cast | 96.88% | 3.12% | 100% | – |

Notes:

1. Votes withheld are not included in the calculation as a vote withheld is not a vote in law.
2. Voting took place prior to the subdivision and 5:1 consolidation of Ordinary Shares which became effective on 12 May 2014.

13. Dilution

RSA monitors its dilution levels on a regular basis to ensure that they remain within the headroom limits set by the Investment Association (IA). As at 31 December 2016, the dilution levels were as follows:

| Limit | RSA dilution % |
|--|----------------|
| 10% over 10 years for all share schemes | 3.76% |
| 5% over 10 years for discretionary schemes, including long-term incentives | 2.48% |

14. External directorships

Stephen Hester received fees of £47,292 during the year in respect of his non-executive role at Centrica plc, where he is Senior Independent Director. As permitted under the Remuneration Policy, he retained these fees.

Scott Egan does not hold outside directorships of FTSE 100 (or any other listed) companies but would be allowed to have one such appointment, subject to the approval of the Group Nomination and Governance Committee.

15. Directors' contracts

The Executive Directors' service agreements became effective on the following dates:

| Executive Director | Effective date |
|--------------------|-----------------|
| Scott Egan | 1 October 2015 |
| Stephen Hester | 5 February 2014 |

The table below shows when the Non-Executive Directors' appointments became effective and when their terms will expire:

| Non-Executive Director | Date of initial appointment | Expiry date of current term |
|------------------------|-----------------------------|-----------------------------|
| Alastair Barbour | 10 October 2011 | 10 October 2017 |
| Kath Cates | 1 September 2013 | 1 September 2019 |
| Enrico Cucchiani | 1 December 2014 | 1 December 2017 |
| Isabel Hudson | 1 August 2016 | 1 August 2019 |
| Hugh Mitchell | 26 September 2012 | 26 September 2018 |
| Martin Scicluna | 1 January 2013 | 1 January 2019 |
| Joseph Streppel | 3 October 2011 | 3 October 2017 |
| Martin Strobel | 1 May 2016 | 1 May 2019 |
| Johanna Waterous | 20 May 2008 | 20 May 2017 |



Hugh S Mitchell

Non-Executive Director and Chairman of Group Remuneration Committee
22 February 2017

Financial statements

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Directors' responsibilities

The Directors are responsible for preparing the Annual Report and Accounts and the Group and Parent Company financial statements in accordance with applicable laws and regulations. Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law they are required to prepare Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and applicable law and have also chosen to prepare the Parent Company financial statements on the same basis. Under company law the Directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and Parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Group and Parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Parent Company and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulations. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and Parent Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report, Directors' and Corporate Governance Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement

We confirm to the best of our knowledge:

- The financial statements on pages 109 to 113, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and Parent Company; and
- The Strategic Report on pages 4 to 41, includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties the Group faces.

Signed by order of the Board



Stephen Hester
Group Chief Executive
22 February 2017



Scott Egan
Group Chief Financial Officer
22 February 2017



Independent auditor's report

to the members of RSA Insurance Group plc only

Opinions and conclusions arising from our audit

1. Our opinion on the financial statements is unmodified

We have audited the financial statements of RSA Insurance Group plc ("RSA" or "the Group") for the year ended 31 December 2016 set out on pages 109 to 185.

In our opinion:

- The financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2016 and of the Group's profit for the year then ended;
- The Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- The Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- The financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Overview

| | |
|---------------------------------------|---|
| Materiality: | £35m (2015: £35m) |
| Group financial statements as a whole | 0.6% (2015: 0.6%) of Net Earned Premium £6,340m (2015: £6,160m) |

| | |
|-----------------|--|
| Coverage | 97% (2015: 93%) of Net Earned Premium |
|-----------------|--|

Risks of material misstatement vs 2015

| | | |
|------------------------|--|----|
| Recurring risks | Insurance liabilities | ◀▶ |
| | IT systems and controls | ▲ |
| | Pensions and post-retirement obligations | ◀▶ |
| | Deferred tax assets | ◀▶ |

2. Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements the risks of material misstatement that had the greatest effect on our audit, in decreasing order of audit significance, were as follows.

| | The Risk | Our Response |
|--|---|--|
| <p>Insurance liabilities (2016: £12,676 million gross, £10,424 million net; 2015: £12,191 million gross, £10,203 million net)</p> <p><i>Refer to page 71 (Group Audit Committee Report), page 115 (accounting policy) and pages 159 to 164 (financial disclosures)</i></p> | <p>Subjective valuation Insurance liabilities represent the single largest liability for the Group. Valuation of these liabilities is highly judgmental because it requires a number of assumptions to be made with high estimation uncertainty such as loss ratios, estimates of the frequency and severity of claims and, where appropriate, the discount rates for longer tail classes of business by territory and line of business. The determination and application of the methodology and performance of the calculations are also complex.</p> <p>A margin is added to the actuarial best estimate of insurance liabilities to make allowance for specific risks identified in assessment of the best estimate. The appropriate margin to recognise is a subjective judgement and estimate taken by the directors, based on the perceived uncertainty and potential for volatility in the underlying claims.</p> <p>Certain lines of business have greater inherent uncertainty, for example those where claims emerge more slowly over time, or where there is greater variability in claim settlement amounts. This includes Abuse, Asbestos and Deafness classes; UK Professional and Financial Risk Classes; the Danish Workers Compensation class; the Swedish Personal Accident classes; the Canadian General Liability class; and classes of business affected by emerging industry issues such as the impact of Periodic Payment Orders (which are akin to annuities with longevity and inflation risk) on UK motor business.</p> <p>Completeness and accuracy of data The valuation of insurance liabilities depends on complete and accurate data about the volume, amount and pattern of current and historical claims since they are often used to form expectations about future claims. If the data used in calculating insurance liabilities, or for forming judgements over key assumptions, is not complete and accurate then material impacts on the valuation of insurance liabilities may arise.</p> | <p>With the assistance of our actuarial specialists, we performed the following procedures:</p> <ul style="list-style-type: none"> • Sector experience and Benchmarking: Comparison of assumptions, reserving methodologies and estimates of losses to expectations based on the Group's historical experience, current trends and benchmarking to our own industry knowledge including information relating to forthcoming legislation that may affect claims settlement speed or amount. • Sensitivity analysis: Review of sensitivity analysis over key judgements and assumptions, such as the discount rates for longer tail classes of business and Periodic Payment Order projections. • Independent re-performance: Independent re-projection of the reserve balances for certain classes of business. The determination of which classes to reproject was based on risk assessment and consideration of the evidence available from other alternative data analysis procedures. • Control design and observation: Evaluation of the governance around the overall Group reserving process, including the scrutiny applied by the Local, Regional and Group Reserving committees, as well as Group level actuarial reviews. We assessed qualifications and experience of those responsible and examined the output of the reviews to assess the scope and depth of these processes. Our evaluation of the methodologies and key assumptions for the most significant and subjective classes of business enabled us to assess the quality of challenge applied through the Group's reserving process. • Margin evaluation: Evaluation of the appropriateness of the Reserve Committee's recommended margin to be applied to the actuarial best estimate. We reviewed the Director's approach to, and analysis performed, in setting the margin. In particular we considered the allowance for uncertainties inherent in the data and assumptions in developing the actuarial best estimate through inquiry with the Directors. <p>In addition to the above the audit team performed procedures to assess the completeness and accuracy of data:</p> <ul style="list-style-type: none"> • Control observation and re-performance: Evaluation and testing of key controls designed to ensure the integrity of the data used in the actuarial reserving process (including both current and prior year case reserve data). The controls included reconciliations between data in the actuarial reserving systems and data in the policy administration systems. We tested controls through inspecting or re-performing the Group's reconciliations. <p>In addition, we tested the operation of controls over the valuation of individual claims reserves, such as large loss review controls, internal peer reviews and claims approvals. We assessed whether such controls were performed in line with the Group's policies and with reference to underlying claims data.</p> <ul style="list-style-type: none"> • Tests of detail: Re-performance of reconciliations between the claims data recorded in the policy administration systems and the data used in the actuarial reserving calculations to ensure the integrity of the data used in the actuarial reserving process. We also compared samples of claims case reserves to appropriate documentation, such as reports from loss adjusters in order to test the controls over the valuation of individual claims reserves. We used data analysis to focus our procedures on significant or anomalous claims. |

| | The Risk | Our Response |
|---|--|---|
| IT systems and control environment Refer to page 72 (Group Audit Committee Report). | Processing errors Many financial reporting controls depend on the correct functioning of operational and financial IT systems. If these systems or controls fail, a significant risk of error in reported financial information can arise from the failure to transfer data appropriately between systems or inappropriate changes being made to financial data or systems. This is an area of significant risk in our audit due to the complexity of the IT infrastructure, particularly in the UK and Scandinavia, where there are legacy systems which require increased manual inputs, relative to more automated processes. This risk is heightened in the current year given the Group is undertaking IT transformation activities, including system implementations and transitions, leading to changes to processes and increasing the risk that controls do not continue to operate effectively. | With the assistance of our own IT audit specialists, our procedures included: <ul style="list-style-type: none"> • Controls design and observation: Testing general IT controls around system access, change management and computer operations within specific applications pertinent to the financial statements by assessing if appropriate policies are in place and adhered to by inspecting supporting evidence. Where general IT controls are not operating effectively, we addressed the increased risk of financial statement misstatement by extending the scope of our work. This included assessing the operation of controls over changes or transactions being recorded in the systems and testing manual compensating controls, such as reconciliations between systems and other information sources, through re-performance or inspection. • Extended scope: Where general IT controls and compensating manual controls did not operate to mitigate a risk, we performed additional substantive testing, such as using extended sample sizes and performing data analysis routines over impacted accounts. |
| | Pensions and post-retirement obligations (2016: £8,893 million; 2015: £7,126 million) Refer to page 72 (Group Audit Committee Report), page 118 (accounting policy) and pages 164 to 168 (financial disclosures). | Subjective valuation Small changes in the assumptions and estimates used can have significant effect on the valuation of the Group's pension obligation and therefore the amount of the pension and post-retirement obligations and the Group's financial position. With the assistance of our own pension actuarial specialists, our procedures included: <ul style="list-style-type: none"> • Benchmarking assumptions: Comparing the key assumptions such as discount rate, inflation rate and life expectancy against externally derived data. • Assessing valuer's credentials: Evaluating the Group's external valuer's competence, objectivity, capability and scope of work. • Assessing transparency: Considering the adequacy of the Group's disclosures in respect of the sensitivity of the defined pension obligation to these assumptions. |
| | Deferred tax assets (2016: £216 million; 2015: £123 million) Refer to page 72 (Group Audit Committee Report), page 117 (accounting policy) and pages 155 to 156 (financial disclosures). | Forecast-based valuation The Group has significant unrecognised deferred tax assets in respect of tax losses. There is inherent uncertainty involved in forecasting future taxable profits, which determines the extent to which deferred tax assets are or are not recognised. The recoverability of the recognised deferred tax asset is dependent on the future profitability of the UK business in particular. Our procedures included: <ul style="list-style-type: none"> • Control design and observation: Evaluating the internal review and challenge process the Group undertakes during the development of the operational plan and by the Group Risk Function during the approval process, and the extent to which the Group considered alternative outcomes. • Historical comparisons and our sector experience: Comparing the expected growth rates to the Group's approved operating plan and assessing the accuracy of that forecasting process in the past. We considered whether projected margins are achievable with reference to the business's recent performance and operating plans, as well as our own industry knowledge. • Sensitivity testing: Sensitivity testing of taxable profits to assumptions such as the Combined Operating Ratio. • Own tax expertise: With the support of our own tax specialists and their knowledge of tax legislation, we also assessed the extent to which projected profits were taxable, in particular the Group's assumptions about how accumulated tax losses and other associated tax attributes can be utilized within the Group against UK taxable profits. • Assessing transparency: Assessing adequacy of the Group's disclosures in respect of the assumptions supporting the deferred tax asset valuation and recognition. |

3. Our application of materiality and an overview of the scope of our audit

The materiality for the Group financial statements as a whole was set at £35m (2015: £35m) determined with reference to a benchmark of Net Earned Premiums, of which it represents 0.6% (2015: 0.6%). We continue to believe that the benchmark of net earned premiums is a fair reflection of revenue from the Group's operations as it is not subject to the volatility arising from multi-year insurance contracts that net written premiums would be.

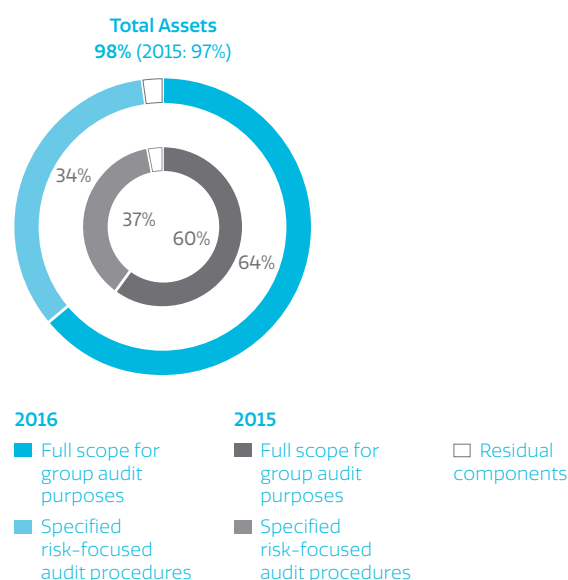
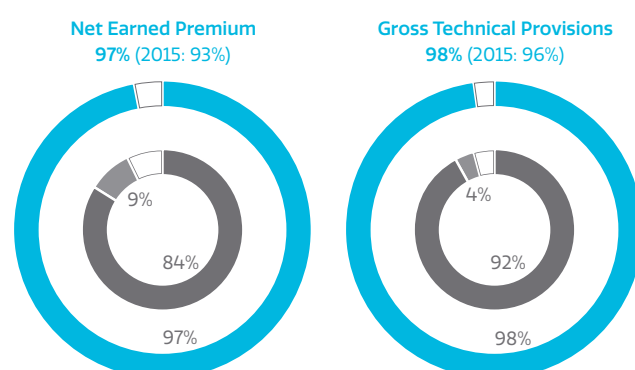
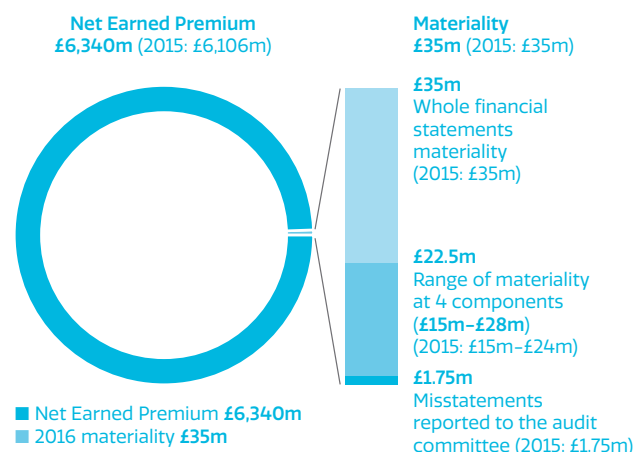
We reported to the Audit Committee any corrected or uncorrected misstatements exceeding £1.75m (2015: £1.75m), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Audits for Group reporting purposes were performed by component auditors for four (2015: four) of the Group's eight (2015: sixteen) reporting components, being those located within the UK, Ireland, Canada and Scandinavia. Within the Scandinavian reporting components, audits were performed by component auditors in Denmark, Sweden and Norway. The Group's central functions were not individually significant enough to require an audit for Group reporting purposes, but did present specific individual risks that needed to be addressed. As such, specified risk-focused procedures were performed on investments, treasury and reinsurance, which included agreeing financial information to supporting documentation.

The components within the scope of our work accounted for the percentages illustrated opposite. For the remaining components we performed analysis at an aggregated Group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The Group audit team instructed component auditors as to the significant areas to be covered, including the relevant risks detailed above and the information to be reported back. The Group audit team approved the component materialities, which ranged from £15m to £28m (2015: £15m to £24m), having regard to the mix of size and risk profile of the Group across the components. All (2015: all) of the audits of reporting components were performed by the component auditors.

The Group audit team visited five (2015: five) component locations, being those in the UK, Ireland, Canada, Denmark and Sweden (2015: same) to assess the audit risk and planned audit approach. Telephone conference meetings were also held with these component auditors and others that were not physically visited. At these visits and meetings, the findings reported to the Group audit team were discussed in more detail and the Group audit team reviewed key elements of the component auditors' work papers. Any further work required by the Group audit team was then performed by the component auditor.



4. Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

In our opinion:

- The part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- The information given in the Strategic Report and the Directors' Report for the financial year is consistent with the financial statements.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and from reading the Strategic Report and the Directors' Report:

- We have not identified material misstatement in those reports; and
- In our opinion, those reports have been prepared in accordance with Companies Act 2006.

5. We have nothing to report on the disclosures of principal risks

Based on the knowledge we acquired during our audit, we have nothing material to add or draw attention to in relation to:

- The Directors' Viability Statement on page 63, concerning the principal risks, their management, and, based on that, the directors' assessment and expectations of the Group's continuing in operation over the three years to 2019; or
- The disclosures in note 1 of the financial statements concerning the use of the going concern basis of accounting.

6. We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- We have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; or
- The Group Audit Committee Report does not appropriately address matters communicated by us to the audit committee.

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- Adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- The parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- Certain disclosures of directors' remuneration specified by law are not made; or
- We have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- The directors' statements, set out on page 63, in relation to going concern and longer-term viability; and
- The part of the Corporate Governance in the Directors' and Corporate Governance Report relating to the Company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope and responsibilities

As explained more fully in the Directors' Responsibilities Statement set out on page 103, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate. This report is made solely to the company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014a, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

Stuart Crisp (Senior Statutory Auditor) for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants
15 Canada Square
London
E14 5GL

22 February 2017

Consolidated Income Statement for the year ended 31 December 2016

| | Notes | 2016 £m | 2015 £m |
|--|--------|--------------|--------------|
| Income | | | |
| Gross written premiums | | 7,220 | 6,858 |
| Less: reinsurance premiums | | (981) | (906) |
| Net written premiums | 8 | 6,239 | 5,952 |
| Change in the gross provision for unearned premiums | | 109 | (97) |
| Less: change in provision for unearned reinsurance premiums | | (8) | 305 |
| Change in provision for unearned premiums | | 101 | 208 |
| Net earned premiums | | 6,340 | 6,160 |
| Net investment return | 9 | 347 | 381 |
| Other operating income | 11 | 170 | 142 |
| Total income | | 6,857 | 6,683 |
| Expenses | | | |
| Gross claims incurred | | (4,826) | (4,496) |
| Less: claims recoveries from reinsurers | | 707 | 367 |
| Net claims | 10 | (4,119) | (4,129) |
| Underwriting and policy acquisition costs | | (1,977) | (1,986) |
| Unwind of discount | | (59) | (52) |
| Other operating expenses | 12 | (229) | (308) |
| | | (6,384) | (6,475) |
| Finance costs | 13 | (138) | (106) |
| Remeasurement of disposal groups and gains on disposals of businesses | 6(iii) | (234) | 3 |
| Net share of profit after tax of associates | | - | 1 |
| Profit before tax | 8 | 101 | 106 |
| Income tax expense | 17 | (54) | (18) |
| Profit after tax from continuing operations | | 47 | 88 |
| (Loss)/profit from discontinued operations | 6(i) | (27) | 156 |
| Profit for the year | | 20 | 244 |
| Attributable to: | | | |
| Equity holders of the Parent Company | | 27 | 235 |
| Non-controlling interests | | (7) | 9 |
| | | 20 | 244 |
| Earnings per share on profit/(loss) attributable to the ordinary shareholders of the Parent Company | | | |
| Basic | | | |
| From continuing operations | 19 | 4.4p | 6.9p |
| From discontinued operations | 19 | (2.6)p | 15.4p |
| | | 1.8p | 22.3p |
| Diluted | | | |
| From continuing operations | 19 | 4.4p | 6.9p |
| From discontinued operations | 19 | (2.6)p | 15.3p |
| | | 1.8p | 22.2p |
| Ordinary dividends paid and proposed for the year | | | |
| Interim dividend paid | 20 | 5.0p | 3.5p |
| Final dividend proposed | 20 | 11.0p | 7.0p |

The attached notes on pages 114 to 179 form an integral part of these consolidated financial statements.

Consolidated Statement of Comprehensive Income for the year ended 31 December 2016

| | Notes | 2016 £m | 2015 £m |
|--|-------|------------|--------------|
| Profit for the year | | 20 | 244 |
| Items from continuing operations that may be reclassified to the income statement: | | | |
| Exchange gains/(losses) net of tax on translation of foreign operations | | 228 | (120) |
| Fair value gains/(losses) on available for sale financial assets net of tax | | 151 | (211) |
| | | 379 | (331) |
| Items from continuing operations that will not be reclassified to the income statement: | | | |
| Pension – remeasurement of net defined benefit asset/liability net of tax | 21 | (316) | 65 |
| Movement in property revaluation surplus net of tax | | 1 | 3 |
| | | (315) | 68 |
| Other comprehensive income/(expense) for the year from continuing operations | | 64 | (263) |
| Other comprehensive income/(expense) for the year from discontinued operations | 6(i) | 120 | (106) |
| Total other comprehensive income/(expense) for the year | 21 | 184 | (369) |
| Total comprehensive income/(expense) for the year from continuing operations | | 111 | (175) |
| Total comprehensive income for the year from discontinued operations | 6(i) | 93 | 50 |
| Total comprehensive income/(expense) for the year | | 204 | (125) |
| Attributable to: | | | |
| Equity holders of the Parent Company | | | |
| from continuing operations | | 98 | (189) |
| from discontinued operations | | 94 | 51 |
| | | 192 | (138) |
| Non-controlling interests | | | |
| from continuing operations | | 13 | 14 |
| from discontinued operations | | (1) | (1) |
| | | 12 | 13 |
| | | 204 | (125) |

The attached notes on pages 114 to 179 form an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity for the year ended 31 December 2016

| | Ordinary share capital £m | Ordinary share premium £m | Own shares £m | Preference shares £m | Re-valuation reserves £m | Capital redemption reserve £m | Foreign currency translation reserve £m | Retained earnings £m | Shareholders' equity £m | Non-controlling interests £m | Total equity £m |
|---|------------------------------|------------------------------|------------------|-------------------------|-----------------------------|----------------------------------|--|-------------------------|----------------------------|---------------------------------|--------------------|
| Balance at 1 January 2015 | 1,015 | 1,075 | (1) | 125 | 527 | 389 | (46) | 741 | 3,825 | 108 | 3,933 |
| Total comprehensive income | | | | | | | | | | | |
| Profit for the year | - | - | - | - | - | - | - | 235 | 235 | 9 | 244 |
| Other comprehensive (expense)/income (note 21) | - | - | - | - | (234) | - | (204) | 65 | (373) | 4 | (369) |
| | - | - | - | - | (234) | - | (204) | 300 | (138) | 13 | (125) |
| Transactions with owners of the Group | | | | | | | | | | | |
| Contribution and distribution | | | | | | | | | | | |
| Dividends (note 20) | - | - | - | - | - | - | - | (65) | (65) | (3) | (68) |
| Shares issued for cash (note 32) | 1 | 2 | - | - | - | - | - | - | 3 | - | 3 |
| Share based payments (note 18/32) | 1 | - | - | - | - | - | - | 13 | 14 | - | 14 |
| Other reserve transfer | - | - | - | - | - | - | 29 | (29) | - | - | - |
| | 2 | 2 | - | - | - | - | 29 | (81) | (48) | (3) | (51) |
| Changes in shareholders' interests in subsidiaries | - | - | - | - | - | - | - | 3 | 3 | 11 | 14 |
| Total transactions with owners of the Group | 2 | 2 | - | - | - | - | 29 | (78) | (45) | 8 | (37) |
| Balance at 1 January 2016 | 1,017 | 1,077 | (1) | 125 | 293 | 389 | (221) | 963 | 3,642 | 129 | 3,771 |
| Total comprehensive income | | | | | | | | | | | |
| Profit for the year | - | - | - | - | - | - | - | 27 | 27 | (7) | 20 |
| Other comprehensive income/(expense) (note 21) | - | - | - | - | 181 | - | 299 | (315) | 165 | 19 | 184 |
| | - | - | - | - | 181 | - | 299 | (288) | 192 | 12 | 204 |
| Transactions with owners of the Group | | | | | | | | | | | |
| Contribution and distribution | | | | | | | | | | | |
| Dividends (note 20) | - | - | - | - | - | - | - | (131) | (131) | (3) | (134) |
| Shares issued for cash (note 32) | 2 | 3 | - | - | - | - | - | - | 5 | - | 5 |
| Share based payments (note 18/32) | 1 | - | - | - | - | - | - | 15 | 16 | - | 16 |
| Other reserve transfer ¹ | - | - | - | - | 28 | - | - | (28) | - | - | - |
| | 3 | 3 | - | - | 28 | - | - | (144) | (110) | (3) | (113) |
| Changes in shareholders' interests in subsidiaries | - | - | - | - | (6) | - | - | (3) | (9) | (6) | (15) |
| Total transactions with owners of the Group | 3 | 3 | - | - | 22 | - | - | (147) | (119) | (9) | (128) |
| Balance at 31 December 2016 | 1,020 | 1,080 | (1) | 125 | 496 | 389 | 78 | 528 | 3,715 | 132 | 3,847 |

Note:

1. During the year a reclassification was made between retained earnings and the revaluation reserve of £28m primarily as a result of the changes to the UK tax treatment of unrealised investment gains of available for sale securities. Further details on the revaluation reserve can be found in note 21.

The attached notes on pages 114 to 179 form an integral part of these consolidated financial statements.

Consolidated Statement of Financial Position as at 31 December 2016

| | Notes | 2016 £m | 2015 £m |
|---|-------|---------------|---------------|
| Assets | | | |
| Goodwill and other intangible assets | 22 | 728 | 616 |
| Property and equipment | 23 | 109 | 109 |
| Investment property | 24 | 333 | 365 |
| Investments in associates | | 12 | 13 |
| Financial assets | 25 | 12,325 | 11,797 |
| Total investments | | 12,670 | 12,175 |
| Reinsurers' share of insurance contract liabilities | 28 | 2,252 | 1,988 |
| Insurance and reinsurance debtors | 30 | 2,823 | 2,653 |
| Deferred tax assets | 29 | 270 | 163 |
| Current tax assets | 29 | 65 | 51 |
| Other debtors and other assets | 30 | 430 | 693 |
| Other assets | | 765 | 907 |
| Cash and cash equivalents | 31 | 985 | 816 |
| | | 20,332 | 19,264 |
| Assets of operations classified as held for sale | 6(ii) | 807 | 1,347 |
| Total assets | | 21,139 | 20,611 |
| Equity and liabilities | | | |
| Equity | | | |
| Shareholders' equity | | 3,715 | 3,642 |
| Non-controlling interests | | 132 | 129 |
| Total equity | | 3,847 | 3,771 |
| Liabilities | | | |
| Loan capital | 34 | 1,068 | 1,254 |
| Insurance contract liabilities | 36 | 12,676 | 12,191 |
| Insurance and reinsurance liabilities | 36 | 954 | 945 |
| Borrowings | 35 | 251 | 11 |
| Deferred tax liabilities | 29 | 54 | 40 |
| Current tax liabilities | 29 | 32 | 31 |
| Provisions | 38 | 420 | 261 |
| Other liabilities | 39 | 1,087 | 1,017 |
| Provisions and other liabilities | | 1,593 | 1,349 |
| | | 16,542 | 15,750 |
| Liabilities of operations classified as held for sale | 6(ii) | 750 | 1,090 |
| Total liabilities | | 17,292 | 16,840 |
| Total equity and liabilities | | 21,139 | 20,611 |

The attached notes on pages 114 to 179 form an integral part of these consolidated financial statements.

The financial statements were approved on 22 February 2017 by the Board of Directors and are signed on its behalf by:



Scott Egan
Group Chief Financial Officer

Consolidated Statement of Cashflows for the year ended 31 December 2016

| | Note | 2016 £m | Re-presented ¹ 2015 £m |
|--|------|--------------|---|
| Cashflows from operating activities | | | |
| Net profit for the year before tax from continuing operations | | 101 | 106 |
| Adjustments for non cash movements in net profit for the year | | | |
| Depreciation | | 20 | 21 |
| Amortisation and impairment of intangible assets | | 83 | 80 |
| Amortisation of available for sale assets | | 70 | 64 |
| Fair value gains/(losses) on disposal of financial assets | | 15 | (37) |
| Impairment on available for sale financial assets | | (8) | 7 |
| Share of profit of associates | | – | (1) |
| Loss/(profit) on disposal of subsidiaries | | 234 | (3) |
| Foreign exchange (loss)/gain | | (87) | 41 |
| Other non-cash movements ¹ | | 17 | 49 |
| Changes in operating assets/liabilities | | | |
| Loss and loss adjustment expenses | | (308) | (77) |
| Unearned premiums | | (76) | (179) |
| Movement in working capital ¹ | | (69) | 299 |
| Reclassification of investment income and interest paid | | (212) | (232) |
| Tax paid | | (88) | (108) |
| Dividend income | | 28 | 25 |
| Interest and other investment income | | 328 | 322 |
| Pension deficit funding | | (65) | (65) |
| Net cashflows from operating activities – continuing operations | | (17) | 312 |
| Net cashflows from operating activities – discontinued operations | | (18) | 11 |
| Cashflows from investing activities | | | |
| Proceeds from sales or maturities of: | | | |
| Financial assets | | 3,747 | 3,931 |
| Investment property | | 28 | 3 |
| Property and equipment | | 10 | 1 |
| Investment in subsidiaries (net of cash disposed of) | | – | 14 |
| Purchase of: | | | |
| Financial assets | | (3,589) | (4,118) |
| Property and equipment | | (25) | (14) |
| Intangible assets | | (139) | (48) |
| Net cashflows from investing activities – continuing operations | | 32 | (231) |
| Net cashflows from investing activities – discontinued operations | | 333 | 219 |
| Cashflows from financing activities | | | |
| Proceeds from issue of share capital | | 5 | 3 |
| Dividends paid to ordinary shareholders | | (122) | (56) |
| Dividends paid to preference shareholders | | (9) | (9) |
| Dividends paid to non-controlling interests | | (3) | (3) |
| Redemption of debt instruments | | (200) | (299) |
| Issue of debt instruments | | 242 | – |
| Interest paid | | (150) | (107) |
| Net cashflows from financing activities – continuing operations | | (237) | (471) |
| Net increase/(decrease) in cash and cash equivalents | | 93 | (160) |
| Cash and cash equivalents at the beginning of the year | | 902 | 1,135 |
| Effect of changes in foreign exchange on cash and cash equivalents | | 92 | (73) |
| Cash and cash equivalents at the end of the year | 31 | 1,087 | 902 |

Note:

1. Following a review of other non-cash movements and foreign exchange adjustments, specific balances have been further analysed and classified as movements in working capital for 2016 and 2015. These adjustments have no impact on the overall reported cashflow from operating activities in either year, or any other notes to the financial statements.

The attached notes on pages 114 to 179 form an integral part of these consolidated financial statements.

Basis of Preparation and Significant Accounting Policies

RSA Insurance Group Plc (the 'Company') is a public limited company incorporated and domiciled in England and Wales. The Company through its subsidiaries and associates (together the 'Group' or 'RSA') provides personal and commercial insurance products to its global customer base, principally in the UK, Ireland, Middle East (together 'UK & International'), Scandinavia and Canada.

1) Basis of preparation

The consolidated financial statements have been prepared on a going concern basis and in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union (EU). The consolidated financial statements are prepared on a historical cost basis. Where other bases are applied these are identified in the relevant accounting policy.

In line with industry practice, the Group's statement of financial position is not presented using current and non-current classifications, but broadly in increasing order of liquidity.

The assets and liabilities considered as non-current include: investments in associates, deferred tax assets, property and equipment, intangible assets, goodwill, deferred tax liabilities, outstanding debt including loan capital and elements of financial investments, insurance contract liabilities and reinsurers' share of insurance contract liabilities.

The assets and liabilities considered as current include cash and cash equivalents, and insurance and reinsurance debtors.

The remaining balances are of a mixed nature. The current and non-current portions of such balances are set out in the respective notes or in the Risk and Capital Management note (note 5).

Except where otherwise stated, all figures included in the consolidated financial statements are presented in millions of pounds Sterling (£m).

Accounting policies that are significant to understanding the performance, financial position and cashflows of the Group are set out in note 4 with other policies presented in Appendix A. The notes are grouped together by their nature. Estimation techniques and assumptions are presented in the relevant note in order to provide context to the figures presented. The most significant estimates and assumptions are those used in determining Insurance contract liabilities (note 36), Deferred tax (note 29) and Defined benefit pension scheme liabilities (note 37). With the exception of the re-presentation of the Segmental information (note 8), all of the information previously disclosed continues to be presented, where material, on a basis consistent with prior year.

2) Adoption of new and revised standards

There are a small number of narrow scope amendments arising from annual improvements to standards that are applicable to the Group for the first time in 2016, none of which have had a significant impact on the consolidated financial statements.

3) Recently issued accounting pronouncements

IFRS 9 'Financial Instruments' and IFRS 17 'Insurance Contracts'

The IASB currently expects to publish IFRS 17 'Insurance Contracts' during the first half of 2017 and that the latest adoption date for the new standard will be 2021.

This timescale is anticipated to be consistent with the latest date of adoption of IFRS 9 'Financial Instruments' as permitted by the amendment to IFRS 4 'Insurance Contracts'. The amendment (which has still to be adopted by the EU) provides the option to defer the normal adoption date of 2018 for up to three years.

The Group plans to take advantage of the deferral approach available under IFRS 4, thereby adopting the standard from 1 January 2021.

IFRS 15 'Revenue Recognition'

IFRS 15 'Revenue Recognition' becomes effective from 1 January 2018. Revenue arising from insurance contracts and from financial instruments is outside the scope of IFRS 15. The impact on the recognition of revenue from other services delivered to customers by the Group is expected to be insignificant.

IFRS 16 'Leases'

In January 2016, the IASB issued IFRS 16 'Leases' to replace the existing standard IAS 17, which will be effective from 1 January 2019 but with earlier adoption permitted.

The main change under IFRS 16 is that it requires the recognition of the lease obligations, together with an asset representing the right to the use of the leased asset during the term of the lease. Under IAS 17, for leases qualifying as operating leases, the lease obligations are not recognised in the statement of financial position.

The Group is currently in the process of assessing the impact of IFRS 16 on the financial statements and the undiscounted value of the Group's operating lease obligations are disclosed in note 40.

Other pronouncements

There are a number of amendments to IFRS that have been issued by the IASB that become mandatory during 2017 or in a subsequent accounting period. The Group has evaluated these changes and none are expected to have a significant impact on the consolidated financial statements.

4) Significant accounting policies

The significant accounting policies used in the preparation of these consolidated financial statements, as set out below, have been applied consistently to all periods presented in these consolidated financial statements, unless otherwise stated.

The Group has not made any significant changes to its accounting policies during 2016 but has refined its policy on accounting for disposals of a business.

Premium income

Premium written is recognised in the period in which the Group is legally bound through a contract to provide insurance cover. It represents the full amount of premiums receivable under the contract, including estimates where the amounts are not known at the date they are written. These are deferred as a provision for unearned premiums until recognised as revenue principally computed on a monthly or daily pro-rata basis. Net premiums earned are stated net of amounts passed ('ceded') to reinsurers. Premiums are shown before deduction of commission and exclude any sales based taxes or duties.

Gross claims incurred and insurance contract liabilities

Gross claims incurred represent the cost of agreeing and settling insurance claims on insurance contracts underwritten by the Group. Provisions for losses and loss adjustment expenses are recognised at the estimated ultimate cost, net of expected salvage and subrogation recoveries when a claim is incurred.

The provisions for losses and loss adjustment expenses, and related reinsurance recoveries, are discounted where there is a long period from incident to claims settlement or when nominal interest rates are high and where there exists a suitable claims payment pattern from which to calculate the discount. In defining those claims with a long period from incident to claims settlement, an average period of settlement of six years or more has been used as a guide. The discount rate used is based upon an investment return expected to be earned by financial assets which are appropriate in value and duration to match the provisions for insurance contract liabilities being discounted during the period expected before the final settlement of such claims.

Differences between the estimated cost and subsequent settlement of claims or re-estimated costs are recognised in the consolidated income statement in the year in which they are settled or in which the insurance contract liabilities are re-estimated.

Acquisition costs comprise the direct and indirect costs of obtaining and processing new insurance business. These costs are recognised as deferred acquisition costs (DAC) and are deducted from the provision for unearned premium. DAC is amortised on the same basis as the related unearned premiums are earned.

At the end of each reporting period tests are performed to ensure the adequacy of the Group's insurance contract liabilities by considering the cashflows associated with the provision for unearned premium net of related DAC. In performing these tests, best estimates of future contractual cashflows, including loss adjustment and administrative expenses as well as investment income on financial assets backing such liabilities are used. Any deficiency is charged to the consolidated income statement immediately by establishing a provision for liability adequacy known as the unexpired risk provision. The unexpired risk provision is assessed in aggregate for business classes which are managed together and where there are no restraints on the ability to use assets held in relation to such business to meet any of the associated liabilities.

Further information on net claims can be found in note 10, and insurance contract liabilities in note 36.

Reinsurance

Written premiums ceded to a reinsurer are recognised in the period in which the reinsurance contract is entered into and include estimates where the amounts are not finalised at the end of the reporting period. The ceded written premiums are recognised in the consolidated income statement over the period of the reinsurance contract, based on the expected earning pattern in relation to the underlying insurance contract(s).

Reinsurers' share of insurance contract liabilities within the consolidated statement of financial position includes the reinsurers' share of provisions for losses and loss adjustment expenses and unearned premiums. The Group reports third party reinsurance balances on the consolidated balance sheets on a gross basis to present the exposure to credit risk related to third party reinsurance. The amount recoverable is reduced when there is an event arising after the initial recognition that provides objective evidence that the Group may not receive all amounts due under the reinsurance contract.

Annuities purchased by the Group to provide for payments under structured settlement arrangements are accounted for as reinsurance ceded and a corresponding reinsurers' share of insurance contract liabilities in cases where the Group remains liable for the settlement in the event of default by the annuity provider. Any gain or loss arising on the purchase of an annuity is recognised in the consolidated income statement at the date of purchase.

Further information can be found in note 28.

Levies

Levies payable are treated as costs of underwriting business and are deducted from the associated unearned premium reserve (UPR). This treatment is consistent with the Group's policy for deferred acquisition costs (DAC).

Basis of Preparation and Significant Accounting Policies – continued

Financial Instruments

Classification and measurement of financial assets and financial liabilities

The Group initially recognises financial instruments at their fair value on the date at which they are purchased.

At initial measurement, the Group classifies its financial assets and financial liabilities in one of the following categories:

- Designated at fair value through profit and loss ('FVTPL');
- Held for trading;
- Available for sale ('AFS');
- Cash and cash equivalents;
- Loans and receivables;
- Financial liabilities; or
- Derivatives designated as hedging instruments.

Transaction costs that are directly attributable to the acquisition of financial assets and financial liabilities that are FVTPL are added to their fair value in their initial measurement.

Further information can be found in note 25, note 26 and note 27.

The table below summarises the classification and treatment of the Group's financial assets and financial liabilities.

| Category | Financial Instrument | Description | Subsequent Measurement | Recognition of change in fair value |
|---|---|--|---|--|
| Designated Fair Value Through Profit & Loss (FVTPL) on initial recognition | Debt securities, equity securities | Where the investment return is managed on the basis of the total return on investment (including unrealised investment gains) | Fair value using prices at the end of the period | Income statement – net investment gains/(losses) |
| Held for trading | Derivative assets/(liabilities) not designated as hedging instruments | Acquired or incurred principally for the purpose of selling or repurchasing in the near term | Carried at fair value Derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative | Income statement – net investment gains/(losses) |
| Available for sale (AFS) | Debt securities, equity securities. | Where the investment return on equity or debt securities is managed on the basis of the periodic cashflows arising from the investment | Fair value using prices at the end of the period | Other comprehensive income – unrealised gains/(losses) Income statement – net investment gains/(losses) when realised or impaired |
| Cash and cash equivalents | Cash and cash equivalents | Consist of cash and highly liquid investments that are readily convertible into a known amount of cash, are subject to insignificant risk of changes in value and have a maturity date of 90 days or less from the date of acquisition | Carrying amounts at amortised cost | |
| Loans and receivables | Loans, reinsurance deposits, other deposits and financial assets arising from non-investment activities | Financial assets with fixed or determinable payments not quoted in an active market | Amortised cost using the effective interest method | Income statement – net investment gains/(losses) when realised or impaired |
| Financial liabilities | Other borrowings | Financial liabilities with fixed or determinable payments | Amortised cost using the effective interest method | Income statement – net investment gains/(losses) when settled. |
| | Loan capital | Financial liabilities with fixed or determinable payments and maturity date | Amortised cost using the effective interest method | Income statement – net investment gains/(losses) when settled |

| Category | Financial Instrument | Description | Subsequent Measurement | Recognition of change in fair value |
|--|--|---|---|--|
| Derivatives designated as hedging instruments | Derivative assets/ (liabilities) designated as hedging instruments | Hedge of a net investment in a foreign operation or hedge of future cashflows or hedge of fair value of fixed interest securities | Carried at fair value Derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative | Hedge of future cashflows – effective portion is initially recognised in OCI; subsequently recognised in the income statement when the hedged cashflows affect profit or loss Hedge of a net investment in foreign operations – effective portion is recognised in OCI, ineffective portion is immediately recognised in the income statement Hedge of fair value – recognised in the income statement. The change in fair value of the hedged investments attributable to the hedged risk is transferred from the revaluation reserve to the income statement |

Investment Income

Dividends on equity investments are recognised as investment income in the consolidated income statement on the date at which the investment is priced 'ex dividend'. Interest income is recognised in the consolidated income statement using the effective interest rate method.

Unrealised gains and losses on AFS investments are recognised in other comprehensive income, except for impairment losses and foreign exchange gains and losses on monetary items which are recognised in the consolidated income statement. On derecognition of an investment classified as available for sale, the cumulative gain or loss previously recognised in other comprehensive income is recognised in the consolidated income statement. Further information can be found in note 9.

Impairment of financial instruments

The Group determines, at each reporting date, whether there is evidence that the value of a financial asset or a group of financial assets, other than those measured as FVTPL are impaired. A financial asset is impaired if there is objective evidence that indicates that an event has occurred after the initial recognition of the asset that may have resulted in a loss of value as a result of having a negative effect on the estimated future cashflows generated by that asset which can be estimated reliably.

An impairment loss in respect of debt instruments is calculated as the difference between its carrying amount and the present value of the estimated future cashflows discounted at the original effective interest rate of the instrument. Interest on the impaired asset continues to be recognised using the effective interest rate method.

For equity securities whose fair values are readily determined and where there is objective evidence that such an asset is impaired by a 'significant' or 'prolonged' decline in the fair value below cost, the net loss previously charged to other comprehensive income is reclassified to the consolidated income statement.

If the fair value of a previously impaired debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed and the reversal recognised in the consolidated income statement. Impairment losses on equity investments are not reversed. Further information can be found in note 9.

Current and deferred tax

Current and deferred tax are recognised in the consolidated income statement, except to the extent that the tax arises from a transaction or event recognised either in other comprehensive income or directly in equity.

Taxation is based on profits and income for the year as determined in accordance with the relevant tax legislation, together with adjustments for prior years.

Basis of Preparation and Significant Accounting Policies – continued

Deferred tax is provided in full using the liability method on temporary differences arising between the tax bases of assets and liabilities and the carrying amounts in the consolidated financial statements. However, if the deferred tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting, nor taxable profit or loss, it is not accounted for. Deferred tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the end of the reporting period and are expected to apply when the related deferred tax asset is realised or the related deferred tax liability is settled.

Deferred tax in respect of the unremitted earnings of overseas subsidiaries and principal associated undertakings is recognised as an expense in the year in which the profits arise, except where the remittance of earnings can be controlled and it is probable that remittance will not take place in the foreseeable future, in which case the tax charge is recognised on the dividends received.

Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which unused tax losses and temporary differences can be utilised.

Post-retirement benefits and obligations

The Group operates both defined contribution and defined benefit schemes.

A defined contribution scheme is a pension scheme under which the Group pays fixed contributions and has no further payment obligations once the contributions have been paid. Contributions to defined contribution pension schemes are charged in the consolidated income statement in the period in which the underlying employment services are provided to the Group.

A defined benefit scheme refers to any other pension scheme; specifically, the Group's defined benefit schemes define an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary.

The value of the net defined benefit liability/asset recognised in the consolidated statement of financial position for each individual post-retirement scheme is calculated as the difference between the present value of the defined benefit obligations of the scheme and the fair value of the scheme assets out of which the obligations are to be settled.

For those schemes in a net liability (deficit) position, the net liability is recognised in the consolidated statement of financial position in provisions. For those schemes in a net asset (surplus) position, the asset is recognised in the consolidated statement of financial position in other debtors and other assets only to the extent that the Group can realise an economic benefit, in the form of a refund or a reduction in future contributions, at some point during the life of the scheme or when the scheme liabilities are settled.

The amounts charged (or credited where relevant) in the consolidated income statement relating to post-retirement defined benefit schemes are as follows:

- The current service cost: this is the present value of additional benefits payable for employees' services provided during the reporting period;
- The past service costs and gains or losses on settlement: these are changes to the obligations already established for past service costs that have arisen from an amendment to the terms of the scheme or a curtailment of the benefits payable by the scheme. These are recognised at the earlier of when the terms of the scheme are amended or the curtailment occurs or, where applicable, when the Group recognises related restructuring costs or termination benefits;
- Net interest on the net defined benefit liability/(asset): this is determined by applying the discount rate applied to the defined benefit obligation for the period to the net defined benefit liability/(asset), and results in a net interest (expense)/income;
- The administration costs of operating the pension schemes.

Remeasurements of the net defined benefit liability/asset recognised in other comprehensive income comprises actuarial gains and losses as a result of changes in assumptions and experience adjustments in the calculation of the defined benefit obligation, and return on scheme assets excluding interest. The most significant of these is the selection of the discount rate used to calculate the defined benefit obligation, details of which are set out in note 37.

Goodwill, other intangible assets, and internally developed computer software

Goodwill

Goodwill is the difference between the cost of a business acquisition and the net fair value of the identifiable assets, liabilities and contingent liabilities acquired. Goodwill is initially capitalised in the consolidated statement of financial position at cost and is subsequently recognised at cost less accumulated impairment losses. The cost of the acquisition is the amount of cash paid and the fair value of other purchase consideration.

Other intangible assets

Other intangible assets are valued at cost less accumulated amortisation, and less any accumulated impairment losses.

Other intangible assets comprise renewal rights, customer lists, brands, computer software and other acquired identifiable non-monetary assets without physical form. The useful economic lives are generally between one and five years and are estimated considering relevant metrics such as customer retention rates, contract length, and forecast period to technological obsolescence. The asset is amortised on a straight-line basis across this period.

Internally developed computer software

The Group capitalises internal and external computer software development costs where the software is separately identifiable; the Group has control over the software; and where it can be demonstrated that they provide future economic benefits for the Group through facilitating revenue or improved processes. The costs capitalised includes administrative and other general overhead expenditure when they can be directly attributed to the software development and preparing it for use. The useful economic life of externally acquired and internally generated software is normally estimated to be between three and seven years.

Further information on goodwill and other intangibles can be found in note 22.

Impairment of goodwill, other intangible assets and internally developed computer software

Goodwill is subject to an impairment test on an annual basis. Other intangible assets, which includes internally generated software, are reviewed for indications of impairment on an annual basis and are subject to an impairment test only if there is an indication of impairment.

Goodwill, other intangible assets and internally developed computer software are allocated to cash generating units (CGUs) for the purpose of impairment testing. When testing for impairment, the recoverable amount of a CGU is determined based on value in use calculations. Further information on how the value in use is calculated can be found in note 22.

Where the carrying amount is more than the recoverable amount, impairment of goodwill or intangible assets is recognised in the consolidated income statement. Impairment losses previously recognised on other intangible assets may be reversed in subsequent periods provided that the revised carrying amount does not exceed the value that would have been determined (net of amortisation) had no impairment loss been recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Assets and liabilities held for sale

Assets and liabilities are classified as held for sale if it is considered highly probable that the carrying amount of the assets and directly associated liabilities will be recovered principally through a sale, rather than through continuing operations. This includes the expectation that the sale will be completed within 12 months of the classification date as held for sale, subject to extension in certain circumstances.

Assets and liabilities held for sale are each presented as a single line in the statement of financial position, at the lower of the carrying amount and fair value less costs to sell.

Where the asset or liability comprises a separate business operation (e.g. a subsidiary, an associate or a branch), the assets (including any goodwill allocated to the business) and the directly associated liabilities of the business are considered together as one disposal group. In the period when assets are recognised as held for sale on the face of the consolidated statement of financial position for the first time, the comparative prior period is not re-presented.

Further information can be found in note 6(ii).

Discontinued operations

A discontinued operation is a component of the Group that has either been disposed of, or is classified as held for sale, and represents a separate major line of business or geographical area of operation.

The profit from discontinued operations is shown separately on the face of the income statement as a single amount. It comprises the profit or loss after tax from discontinued operations together with the gain or loss after tax recognised on completed sales or the gain or loss after tax on the discontinued operations arising from revaluing the carrying value of a held for sale operation to its fair value less costs to sell. Further information can be found in note 6(i).

In the period in which an operation is first classified as discontinued, the consolidated income statement, statement of other comprehensive income, statement of cashflows, earnings per share and diluted earnings per share for the comparative prior period is re-presented to present those operations as discontinued.

In circumstances where the Group is entering into an arrangement to make a legal transfer of a book of business which includes an interim economic transfer of risk to the intended acquirer prior to obtaining court approval for the transfer, the accounting gain or loss arising from the reinsurance is considered as being incremental to the disposal and is consequently presented as a gain or loss arising from the disposal of the business.

Reorganisation costs

Reorganisation costs represent external and clearly identifiable internal costs that are necessarily incurred and directly attributable to the Group's restructuring programme. The aim of the restructuring programme is to both reduce operating costs and improve profitability. Employee termination costs are only recognised when they are part of a restructuring programme that has been communicated to those affected or when a detailed plan of redundancies is announced.

Provisions for onerous contracts are recognised when action is taken by the Group as part of a restructuring programme that reduces any remaining benefit expected under a contract to below its remaining unavoidable costs.

Further information can be found in note 7.

Risk and Capital Management

5) Risk and Capital Management

Insurance Risk

The Group is exposed to risks arising from insurance contracts as set out below:

- A) Underwriting risk
- B) Reinsurance risk
- C) Reserving risk

A) Underwriting risk

Underwriting risk refers to the risk that underwritten business is less profitable than planned due to insufficient pricing.

The majority of underwriting risk to which the Group is exposed is of a short-term nature, and generally does not exceed 12 months. The Group's underwriting strategy aims to ensure that the underwritten risks are well diversified in terms of the type, amount of risk, and geography in order to ensure that the Group is not exposed to a concentration of risk which would result in a volatile insurance result.

Underwriting limits are in place to enforce appropriate risk selection criteria and pricing with all of the Group's underwriters having specific licences that set clear parameters for the business they can underwrite, based on their expertise.

The Group has developed enhanced methods of recording exposures and concentrations of risk and has a centrally managed forum looking at Group underwriting issues, reviewing and agreeing underwriting direction and setting policy and directives where appropriate. The Group has a quarterly portfolio management process across all its business units where key risk indicators are tracked to monitor emerging trends, opportunities and risks. This provides greater control of exposures in high risk areas as well as enabling a prompt response to claims from policyholders should there be a catastrophic event such as an earthquake.

Pricing for the Group's products is generally based upon historical claims frequencies and claims severity averages, adjusted for inflation and modelled catastrophes, trended forward to recognise anticipated changes in claims patterns after making allowance for other costs incurred by the Group, conditions in the insurance market and a profit loading that adequately covers the cost of capital.

B) Reinsurance risk

Reinsurance risk refers to the risk of loss to the Group from the failure to enforce payment under the contracts from one or more of its reinsurers.

Decisions on how much insurance risk to pass on to other insurers through the use of reinsurance is another key strategy employed in managing the Group's exposure to insurance risk. The Group Board determines a maximum and the Group Corporate Centre determines a minimum level of risk to be retained by the Group as a whole and, therefore, the amount of central reinsurance cover purchased. This is then distributed across the Group in accordance with deemed risk appetite. Local operations may also purchase additional reinsurance within agreed local reinsurance appetite parameters.

Reinsurance arrangements in place include proportional, excess of loss, stop loss, catastrophe and adverse development coverage. These arrangements ensure that the Group should not suffer total net insurance losses beyond the Group's risk appetite in any one year.

The Group remains primarily liable as the direct insurer on all risks reinsured, although the reinsurer is liable to the Group to the extent of the insurance risk it has contractually accepted responsibility for.

C) Reserving risk

Reserving risk refers to the risk that the Group's estimates of future claims will be insufficient.

The Group establishes a provision for losses and loss adjustment expenses for the anticipated costs of all losses that have already occurred but have not yet been paid. Such estimates are made for losses already reported to the Group as well as for the losses that have already occurred but are not yet reported losses together with a provision for the future costs of handling and settling the outstanding claims.

There is a risk to the Group from the inherent uncertainty in estimating provisions at the end of the reporting period for the eventual outcome of outstanding notified claims as well as estimating the number and value of claims that are still to be notified. In particular, the estimation of the provisions for the ultimate costs of claims for asbestos and environmental pollution is subject to a range of uncertainties that is generally greater than those encountered for other classes of business due to the slow emergence and longer settlement period for these claims.

The Group seeks to reduce its reserving risk through the use of experienced regional actuaries who estimate the actuarial indication of the required reserves based on claims experience, business volume, anticipated change in the claims environment and claims cost. This information is used by local reserving committees to recommend to the Group Reserving Committee the appropriate level of reserves for each region – which will include adding a margin onto the actuarial indication as a provision for unforeseen developments such as future claims patterns differing from historical experience, future legislative changes and the emergence of latent exposures such as asbestosis. The Group Reserving Committee review these local submissions and recommend the final level of reserves to be held by the Group. The Group has a Group Reserving Committee which is chaired by

the Group Chief Financial Officer and includes the Group Chief Executive, Group Underwriting Director, Group Chief Actuary and Group Chief Risk Officer. A similar committee has been established in each of the Group's major operating segments. The Group Reserving Committee monitors the decisions and judgements made by the business units as to the level of reserves to be held. It then recommends to the Group Board via the Group Audit Committee for the final decision on the level of reserves to be included within the consolidated financial statements. In forming its collective judgement, the Committee considers the following information:

- The actuarial indication of ultimate losses together with an assessment of risks and possible favourable or adverse developments that may not have been fully reflected in calculating these indications. At the end of 2016, these risks and developments include: the possibility of future legislative change having retrospective effect on open claims; changes in claims settlement procedures potentially leading to future claims payment patterns differing from historical experience; the possibility of new types of claim, such as disease claims, emerging from business written several years ago; general uncertainty in the claims environment; the emergence of latent exposures such as asbestos; the outcome of litigation on claims received; failure to recover reinsurance and unanticipated changes in claims inflation;
- The views of internal peer reviewers of the reserves and of other parties including actuaries, legal counsel, risk directors, underwriters and claims managers;
- The outcome from independent assurance reviews performed by the Group actuarial function to assess the reasonableness of regional actuarial indication estimates;
- How previous actuarial indications have developed.

Financial risk

Financial risk refers to the risk of financial loss predominantly arising from investment transactions entered into by the Group, and also to a lesser extent arising from insurance contracts, and includes the following risks:

- Credit risk;
- Market risk including price, interest rate and currency rate risks;
- Liquidity risk.

The Group undertakes a number of strategies to manage these risks including the use of derivative financial instruments for the purpose of reducing its exposure to adverse fluctuations in interest rates, foreign exchange rates and long term inflation. The Group does not use derivatives to leverage its exposure to markets and does not hold or issue derivative financial instruments for speculative purposes. The policy on use of derivatives is approved by the Board Risk Committee ('BRC').

Credit risk

Credit risk is the risk of loss resulting from the failure of a counterparty to honour its financial or contractual obligations to the Group. The Group's credit risk exposure is largely concentrated in its fixed income investment portfolio and to a lesser extent, its premium receivables, and reinsurance assets.

Credit risk is managed at both a Group level and at a local level. Local operations are responsible for assessing and monitoring the creditworthiness of their counterparties (e.g. brokers and policyholders). Local credit committees are responsible for ensuring these exposures are within the risk appetite of the local operations. Exposure monitoring and reporting is embedded throughout the organisation with aggregate credit positions reported and monitored at Group level.

The Group's credit risk strategy appetite and credit risk policy are developed by the BRC and are reviewed and approved by the Board on an annual basis. This is done through the setting of Group policies, procedures and limits.

In defining its appetite for credit risk the Group looks at exposures at both an aggregate and business unit level distinguishing between credit risks incurred as a result of offsetting insurance risks or operating in the insurance market (e.g. reinsurance credit risks and risks to receiving premiums due from policyholders and intermediaries) and credit risks incurred for the purposes of generating a return (e.g. invested assets credit risk).

Limits are set at both a portfolio and counterparty level based on likelihood of default, derived from the rating of the counterparty, to ensure that the Group's overall credit profile and specific concentrations are managed and controlled within risk appetite.

The Group's investment management strategy primarily focuses on debt instruments of high credit quality issuers and seeks to limit the overall credit exposure with respect to any one issuer by ensuring limits have been based upon credit quality. Restrictions are placed on each of the Group's investment managers as to the level of exposure to various rating categories including unrated securities.

The Group is also exposed to credit risk from the use of reinsurance in the event that a reinsurer fails to settle its liability to the Group.

The Group Reinsurance Credit Committee oversees the management of credit risk arising from the reinsurer failing to settle its liability to the Group. Group standards are set such that reinsurers that have a financial strength rating of less than 'A-' with Standard & Poor's, or a comparable rating, are removed from the Group's authorised list of approved reinsurers unless the Group's internal review discovers exceptional circumstances in favour of the reinsurer. Collateral is taken, where appropriate, to mitigate exposures to acceptable levels. At 31 December 2016 the extent of collateral held by the Group against reinsurers' share of insurance contract liabilities was **£159m** (2015: £69m). The UK Legacy reinsurance announced on 7 February 2017 will involve additional extensive collateral arrangements.

Risk and Capital Management – continued

The Group's use of reinsurance is sufficiently diversified that it is not concentrated on a single reinsurer, or any single reinsurance contract. The Group regularly monitors its aggregate exposures by reinsurer group against predetermined reinsurer Group limits, in accordance with the methodology agreed by the BRC. The Group's largest reinsurance exposures to active reinsurance groups are Munich Re, Lloyd's, and Berkshire Hathaway Inc. At 31 December 2016 the reinsurance asset recoverable from these groups does not exceed **2.4%** (2015: 2.8%) of the Group's total financial assets. Stress tests are performed by reinsurer counterparty and the limits are set such that in a catastrophic event, the exposure to a single reinsurer is estimated not to exceed **6.1%** (2015: 7.1%) of the Group's total financial assets.

The credit profile of the Group's assets exposed to credit risk is shown below. The credit rating bands are provided by independent rating agencies. The table below sets out the Group's aggregated credit risk exposure for its financial and insurance assets as at 2016 and 2015.

As at 31 December 2016

Credit rating relating to financial assets that are neither past due nor impaired

| | AAA £m | AA £m | A £m | BBB £m | <BBB £m | Not rated £m | Value including held for sale £m | Less: Amounts classified as held for sale £m | Total of financial assets that are neither past due nor impaired £m |
|---|-----------|----------|---------|-----------|------------|-----------------|--|---|---|
| Debt securities | 5,216 | 3,327 | 2,733 | 875 | 108 | 62 | 12,321 | 776 | 11,545 |
| Loans and receivables | 67 | – | 1 | – | 4 | 16 | 88 | – | 88 |
| Reinsurers' share of insurance contract liabilities | – | 605 | 1,577 | 90 | 20 | 51 | 2,343 | 96 | 2,247 |
| Insurance and reinsurance debtors ¹ | 129 | 30 | 834 | 96 | 103 | 1,518 | 2,710 | 15 | 2,695 |
| Derivative assets | – | 2 | 8 | 37 | – | 9 | 56 | – | 56 |
| Other debtors | – | – | – | – | – | 127 | 127 | 1 | 126 |
| Cash and cash equivalents | 402 | 202 | 442 | 27 | – | 16 | 1,089 | 104 | 985 |

Note:

1. The insurance and reinsurance debtors classified as not rated comprise personal policyholders and small corporate customers that do not have individual credit ratings. The overall credit risk to the Group is deemed to be low as the cover could be cancelled if payment were not received on a timely basis.

As at 31 December 2015

Credit rating relating to financial assets that are neither past due nor impaired

| | AAA £m | AA £m | A £m | BBB £m | <BBB £m | Not rated £m | Value including held for sale £m | Less: Amounts classified as held for sale £m | Total of financial assets that are neither past due nor impaired £m |
|---|-----------|----------|---------|-----------|------------|-----------------|--|---|---|
| Debt securities | 5,737 | 1,612 | 2,818 | 1,166 | 82 | 73 | 11,488 | 376 | 11,112 |
| Loans and receivables | 50 | – | 1 | – | 4 | 45 | 100 | – | 100 |
| Reinsurers' share of insurance contract liabilities | – | 368 | 1,626 | 91 | 23 | 113 | 2,221 | 237 | 1,984 |
| Insurance and reinsurance debtors ¹ | 106 | 22 | 715 | 148 | 93 | 1,864 | 2,948 | 469 | 2,479 |
| Derivative assets | 4 | 5 | – | 21 | – | 8 | 38 | – | 38 |
| Other debtors | – | – | – | – | – | 258 | 258 | 9 | 249 |
| Cash and cash equivalents | 304 | 116 | 346 | 57 | 14 | 76 | 913 | 97 | 816 |

Note:

1. The insurance and reinsurance debtors classified as not rated comprise personal policyholders and small corporate customers that do not have individual credit ratings. The overall credit risk to the Group is deemed to be low as the cover could be cancelled if payment were not received on a timely basis.

With the exception of government debt securities, the largest single aggregate credit exposure does not exceed 3% of the Group's total financial assets.

Ageing of financial assets that are past due but not impaired

The following table provides information regarding the carrying value of financial assets that have been impaired and the ageing of financial assets that are past due but not impaired as at 31 December 2016, excluding those assets that have been classified as held for sale.

As at 31 December 2016

| | Financial assets that are past due but not impaired | | | | | | Carrying value in the statement of financial position £m | Impairment losses charged/ (reversed) to the income statement £m |
|---|---|--------------------------|---------------------------|------------------------------|-----------------------------|--|---|---|
| | Neither past due nor impaired £m | Up to three months £m | Three to six months £m | Six months to one year £m | Greater than one year £m | Financial assets that have been impaired £m | | |
| Debt securities | 11,545 | – | – | – | – | – | 11,545 | – |
| Loans and receivables | 88 | – | – | – | – | – | 88 | (10) |
| Reinsurers' share of insurance contract liabilities | 2,247 | – | – | – | – | 5 | 2,252 | – |
| Insurance and reinsurance debtors | 2,695 | 79 | 22 | 17 | 7 | 3 | 2,823 | 1 |
| Derivative assets | 56 | – | – | – | – | – | 56 | – |
| Other debtors | 126 | – | – | – | 3 | – | 129 | – |
| Cash and cash equivalents | 985 | – | – | – | – | – | 985 | – |

As at 31 December 2015

| | Financial assets that are past due but not impaired | | | | | | Carrying value in the statement of financial position £m | Impairment losses charged to the income statement £m |
|---|---|--------------------------|---------------------------|------------------------------|-----------------------------|--|---|---|
| | Neither past due nor impaired £m | Up to three months £m | Three to six months £m | Six months to one year £m | Greater than one year £m | Financial assets that have been impaired £m | | |
| Debt securities | 11,112 | – | – | – | – | – | 11,112 | 3 |
| Loans and receivables | 100 | – | – | – | – | – | 100 | 2 |
| Reinsurers' share of insurance contract liabilities | 1,984 | – | – | – | – | 4 | 1,988 | 1 |
| Insurance and reinsurance debtors | 2,479 | 121 | 18 | 18 | 17 | – | 2,653 | 4 |
| Derivative assets | 38 | – | – | – | – | – | 38 | – |
| Other debtors | 249 | 1 | – | – | 3 | – | 253 | – |
| Cash and cash equivalents | 816 | – | – | – | – | – | 816 | – |

Market risk

Market risk is the risk of adverse financial impact resulting, directly or indirectly from fluctuations from equity and property prices, interest rates and foreign currency exchange rates. Market risk arises in our operations due to fluctuations in both the value of liabilities and in the value of investments held. At Group level, it also arises in relation to the overall portfolio of international businesses. Market risk is subject to the Board Risk Committee risk management framework, which is subject to review and approval by the Board.

Market risk can be further broken down into three key components:

i. Price risk

The Group classifies its investment portfolio in debt securities and equity securities in accordance with the accounting definitions under IFRS.

At 31 December 2016 the Group held investments classified as equity securities of **£692m** (2015: £585m). These include interests in structured entities (as disclosed in note 27) and other investments where the price risk arises from interest rate risk rather than from equity market price risk. The Group considers that within equity securities, investments with a fair value of **£170m** (2015: £159m) may be more affected by equity index market price risk than by interest rate risk. On this basis a 15% fall in the value of equity index prices would result in the recognition of losses of **£26m** (2015: £24m) in other comprehensive income.

In addition the Group holds investments in properties and in group occupied properties which are subject to property price risk. A decrease of 15% in property prices would result in the recognition of losses of **£50m** (2015: £55m) in the income statement and **£5m** (2015: £6m) in other comprehensive income.

Risk and Capital Management – continued

This analysis assumes that there is no correlation between interest rate and property market rate risks. It also assumes that all other assets and liabilities remain unchanged and that no management action is taken. This analysis does not represent management's view of future market change, but reflects management's view of key sensitivities.

This analysis is presented gross of the corresponding tax credits/(charges).

ii. Interest rate risk

Interest rate risk arises primarily from the Group's investments in long-term debt and fixed income securities and their movement relative to the value placed on insurance liabilities. This impacts both the fair value and amount of variable returns on existing assets as well as the cost of acquiring new fixed maturity investments.

Given the composition of the Group's investments as at 31 December 2016, the table below illustrates the impact to the income statement and other comprehensive income of hypothetical 100bps change in interest rates on long-term debt and fixed income securities that are subject to interest rate risk.

Changes in the income statement and other comprehensive income:

| | Increase in income statement | | Decrease in other comprehensive income | |
|---|------------------------------|------------|--|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| Increase in interest rate markets: | | | | |
| Impact on fixed income securities and cash of an increase in interest rates of 100bps | 20 | 25 | (452) | (435) |

The Group manages interest rate risk by holding investment assets (predominantly fixed income) that generate cashflows which broadly match the duration of expected claim settlements and other associated costs.

The sensitivity of the fixed interest securities of the Group has been modelled by reference to a reasonable approximation of the average interest rate sensitivity of the investments held within each of the portfolios. The effect of movement in interest rates is reflected as a one time rise of 100bps on 1 January 2017 and 1 January 2016 on the following year's income statement and other comprehensive income.

iii. Currency risk

The Group incurs exposure to currency risk in two ways:

- Operational currency risk – by holding investments and other assets and by underwriting and incurring liabilities in currencies other than the currency of the primary environment in which the business units operate the Group is exposed to fluctuations in foreign exchange rates that can impact both its profitability and the reported value of such assets and liabilities;
- Structural currency risk – by investing in overseas subsidiaries the Group is exposed to the risk that fluctuations in foreign exchange rates impact the reported profitability of foreign operations to the Group, and the value of its net investment in foreign operations.

Operational currency risk is principally managed within the Group's individual operations by broadly matching assets and liabilities by currency and liquidity. Operational currency risk is not significant.

Structural currency risk is managed at a Group level through currency forward contracts and foreign exchange options within predetermined limits set by the Group Investment Committee. In managing structural currency risk the needs of the Group's subsidiaries to maintain net assets in local currencies to satisfy local regulatory solvency and internal risk based capital requirements are taken into account. These assets should prove adequate to support local insurance activities irrespective of exchange rate movements but may affect the value of the consolidated shareholders' equity expressed in Sterling.

At 31 December 2016, the Group's total shareholders' equity deployed by currency was:

| | Pounds Sterling £m | Danish Krone/ Euro £m | Canadian Dollar £m | Swedish Krona £m | Other £m | Total £m |
|---|-----------------------|-----------------------------|-----------------------|---------------------|-------------|--------------|
| Shareholders' equity at 31 December 2016 | 2,516 | 284 | 477 | 236 | 202 | 3,715 |
| Shareholders' equity at 31 December 2015 | 2,158 | 377 | 492 | 132 | 483 | 3,642 |

Shareholders' equity is stated after taking account of the effect of currency forward contracts and foreign exchange options. The analysis aggregates the Danish Krone exposure and the Euro exposure as the Danish Krone continues to be pegged closely to the Euro. The Group considers this aggregate exposure when reviewing its hedging strategy.

The table below illustrates the impact of a hypothetical 10% change in Danish Krone/Euro, Canadian Dollar or Swedish Krona exchange rates on shareholders' equity when retranslating into Sterling:

| | 10% strengthening in Pounds Sterling against Danish Krone/Euro £m | 10% weakening in Pounds Sterling against Danish Krone/Euro £m | 10% strengthening in Pounds Sterling against Canadian Dollar £m | 10% weakening in Pounds Sterling against Canadian Dollar £m | 10% strengthening in Pounds Sterling against Swedish Krona £m | 10% weakening in Pounds Sterling against Swedish Krona £m |
|---|---|---|--|--|--|--|
| Movement in shareholders' equity at 31 December 2016 | (25) | 31 | (43) | 53 | (21) | 26 |
| Movement in Shareholders' equity at 31 December 2015 | (34) | 42 | (45) | 55 | (12) | 15 |

Changes arising from the retranslation of foreign subsidiaries' net asset positions from their primary currencies into Sterling are taken through the foreign currency translation reserve and so consequently these movements in exchange rates have no impact on profit.

Liquidity risk

Liquidity risk refers to the risk of loss to the Group as a result of assets not being available in a form that can immediately be converted into cash, and therefore the consequence of not being able to pay its obligations when due. To help mitigate this risk, the BRC sets limits on assets held by the Group designed to match the maturities of its assets to that of its liabilities.

A large proportion of investments is maintained in short-term (less than one year) highly liquid securities, which are used to manage the Group's operational requirements based on actuarial assessment and allowing for contingencies.

The following table summarises the contractual repricing or maturity dates, whichever is earlier. Provision for unearned premium and provision for losses and loss adjustment expenses are also presented and are analysed by remaining estimated duration until settlement.

As at 31 December 2016

| | Less than one year £m | One to two years £m | Two to three years £m | Three to four years £m | Four to five years £m | Five to ten years £m | Greater than ten years £m | Total £m | Carrying value in the statement of financial position £m |
|--|--------------------------------|------------------------------|--------------------------------|---------------------------------|--------------------------------|----------------------------|------------------------------------|---------------|---|
| Subordinated guaranteed US\$ bonds | – | – | – | – | – | – | 7 | 7 | 6 |
| Perpetual guaranteed subordinated capital securities | 375 | – | – | – | – | – | – | 375 | 369 |
| Guaranteed subordinated notes due 2045 | – | – | – | – | – | 400 | – | 400 | 395 |
| Guaranteed subordinated step-up notes due 2039 | – | – | 300 | – | – | – | – | 300 | 298 |
| Provision for unearned premium | 3,007 | 246 | 88 | 6 | 4 | 2 | – | 3,353 | 3,311 |
| Provisions for losses and loss adjustment expenses | 3,583 | 1,728 | 1,150 | 805 | 556 | 1,300 | 1,887 | 11,009 | 9,365 |
| Direct insurance creditors | 108 | – | – | – | – | – | – | 108 | 108 |
| Reinsurance creditors | 559 | 201 | 86 | – | – | – | – | 846 | 846 |
| Borrowings | 251 | – | – | – | – | – | – | 251 | 251 |
| Deposits received from reinsurers | 67 | – | – | – | – | – | – | 67 | 67 |
| Derivative liabilities | 28 | 1 | 49 | – | 19 | 35 | 35 | 167 | 167 |
| Total | 7,978 | 2,176 | 1,673 | 811 | 579 | 1,737 | 1,929 | 16,883 | 15,183 |
| Interest on perpetual bonds and notes | 63 | 49 | 32 | 21 | 21 | 81 | 2 | 269 | |

Risk and Capital Management – continued

As at 31 December 2015

| | Less than one year £m | One to two years £m | Two to three years £m | Three to four years £m | Four to five years £m | Five to ten years £m | Greater than ten years £m | Total £m | Carrying value in the statement of financial position £m |
|--|-----------------------------|------------------------------|--------------------------------|---------------------------------|-----------------------------|----------------------------|------------------------------------|---------------|---|
| Subordinated guaranteed US\$ bonds | – | – | – | – | – | – | 6 | 6 | 5 |
| Perpetual guaranteed subordinated capital securities | – | 375 | – | – | – | – | – | 375 | 359 |
| Guaranteed subordinated notes due 2045 | – | – | – | – | – | 400 | – | 400 | 394 |
| Guaranteed subordinated step-up notes due 2039 | – | – | – | 500 | – | – | – | 500 | 496 |
| Provision for unearned premium | 2,778 | 232 | 81 | 10 | 3 | 3 | – | 3,107 | 3,107 |
| Provisions for losses and loss adjustment expenses | 3,256 | 1,576 | 1,069 | 747 | 536 | 1,242 | 2,120 | 10,546 | 9,084 |
| Direct insurance creditors | 115 | – | – | – | – | – | – | 115 | 115 |
| Reinsurance creditors | 569 | 183 | 78 | – | – | – | – | 830 | 830 |
| Borrowings | 11 | – | – | – | – | – | – | 11 | 11 |
| Deposits received from reinsurers | 14 | – | – | – | – | – | – | 14 | 14 |
| Derivative liabilities | 50 | 1 | 1 | 18 | – | 19 | – | 89 | 89 |
| Total | 6,793 | 2,367 | 1,229 | 1,275 | 539 | 1,664 | 2,126 | 15,993 | 14,504 |
| Interest on perpetual bonds and notes | 93 | 81 | 68 | 39 | 21 | 101 | 2 | 405 | |

The maturity analysis above is presented on an undiscounted basis. The carrying values in the statement of financial position are discounted where appropriate in accordance with Group accounting policy.

The capital and interest payable on the bonds and notes have been included until the dates on which the Group has the option to call the instruments and the interest rates are reset. For further information on terms of the bonds and notes, see note 34.

Capital Management

It is a key regulatory requirement that the Group maintains sufficient capital to support its exposure to risk. Accordingly, the Group's capital management strategy is closely linked to its monitoring and management of risk. The Group's capital objectives consist of striking the right balance between the need to support claims liabilities and ensure the confidence of policyholders, exposure to other risks, support competitive pricing strategies, meet regulatory capital requirements, and providing adequate returns for its shareholders.

The Group's overall capital position is primarily comprised of shareholders' equity and subordinated loan capital and aims to maximise shareholder value, while maintaining financial strength and maintaining adequate regulatory capital. In addition the Group also aims to hold sufficient capital so as to maintain its single 'A' credit rating.

The Group operates in many countries, and its regulated entities hold appropriate levels of capital to satisfy applicable local regulations. Compliance with local regulatory requirements is embedded within the BRC mandate, for the protection of the Group's policyholders and the continuation of the Group's ability to underwrite.

Regulatory solvency position during 2016

The Group's Solvency II Internal Model was approved by the PRA in December 2015 and forms the basis of the primary Solvency II solvency capital ratio (SCR) measure.

The Internal Model is used to support, inform and improve the Group's decision making across the Group. It is used to determine the Group's optimum capital structure, its investment and hedging strategy, its reinsurance programme and to determine the pricing and target returns for each portfolio.

At 31 December 2016, the estimated SCR and corresponding eligible own funds were as follows:

| | Unaudited 2016 £bn | Unaudited 2015 £bn |
|----------------------|--------------------------|--------------------------|
| Eligible Own Funds | 2.9 | 2.9 |
| SCR | 1.8 | 2.0 |
| Coverage (unrounded) | 158% | 143% |

The disposal of **£834m** of undiscounted UK legacy insurance liabilities net of reinsurance was announced on 7 February 2017. The transaction takes the form of an initial reinsurance agreement, to be effective at 31 December 2016 and which substantially effects economic transfer, to be followed by a subsequent legal transfer of the business. This disposal will add a further 17–20 coverage points to RSA's Solvency II SCR coverage.

The first solvency and financial condition report as required by Solvency II for the year ended 31 December 2016 will be publicly available in May 2017.

The impact on the Solvency II coverage ratio of a range of sensitivities is set out below:

| | Unaudited 2016 Including pensions | Unaudited 2016 Excluding pensions |
|--|--|--|
| Solvency II sensitivities¹ (change in coverage ratio): | | |
| Interest rates: +1% non-parallel ² shift | +6% | 0% |
| Interest rates: -1% non-parallel ² shift | -7% | -2% |
| Equities: -15% | -8% | -1% |
| Foreign exchange: GBP +10% vs all currencies | -4% | -4% |
| Cat loss of £75m net | -4% | -4% |
| Credit spreads: +0.25% parallel shift | +9% | -4% |
| Credit spreads: -0.25% parallel shift | -13% | +4% |

Notes:

1. Sensitivities exclude second order impacts from the application of Tier 1 eligibility rules.
2. RSA has updated its approach to interest rate sensitivities, from a parallel shift in the yield curve to a non-parallel shift. This is to reflect that the long end of the yield curve is typically more stable than the short end.

The above sensitivities have been considered in isolation. Should sensitivities impact in combination there may be some natural offsets between them.

Own Risk and Solvency Assessment (ORSA)

The Solvency II directive introduced a requirement for undertakings to conduct an ORSA.

The Group defines its ORSA as a series of inter-related activities by which it establishes:

- The quantity and quality of the risks which it seeks to assume;
- The level of capital required to support those risks;
- The actions it will take to achieve and maintain the desired levels of risk and capital.

The assessment considers both the current position and the positions that may arise during the planning horizon of the Group (typically the next three years). It looks at both the expected outcome and the outcome arising when the plan assumptions do not materialise as expected.

The assessments of how much risk to assume and how much capital to hold are inextricably linked. In some situations, it may be desirable to increase the amount of risk assumed or retained in order to make the most efficient use of capital available or else to return excess capital to capital providers. In other situations, where the risks assumed give rise to a capital requirement that is greater than the capital immediately available to support those risks, it will be necessary either to reduce the risk assumed or to obtain additional capital.

The assessment of risk and solvency needs is in principle carried out continuously. In practice, the assessment consists of a range of specific activities and decisions carried out at different times of the year as part of an annual cycle, supplemented as necessary by ad hoc assessments of the impact of external events and developments and of internal business proposals.

Papers are presented to the Board throughout the year dealing with individual elements that make up the ORSA. The information contained in those papers and the associated decisions taken are summarised in an annual ORSA report, which is submitted to the Group's regulators as part of the normal supervisory process.

The ORSA is approved by the BRC.

Significant Transactions and Events

6(i) Discontinued operations and disposals

The Group classified the following operations as discontinued because they have been sold and represent a separate geographical area of operation.

| Operation | Date of disposal | Acquirer |
|------------------|------------------|---|
| Hong Kong | 31 March 2015 | Allied World Assurance Company |
| Singapore | 31 March 2015 | Allied World Assurance Company |
| Labuan | 12 May 2015 | Allied World Assurance Company |
| China | 14 May 2015 | Swiss Re Corporate Solutions |
| Indian associate | 29 July 2015 | Sundaram Finance Ltd |
| Italy | 31 December 2015 | ITAS Mutua |
| Russia | 29 January 2016 | Joint Stock Insurance Company Blagostoyanie |
| Brazil | 29 February 2016 | Suramericana S.A. |
| Colombia | 31 March 2016 | Suramericana S.A. |
| Chile | 30 April 2016 | Suramericana S.A. |
| Argentina | 30 April 2016 | Suramericana S.A. |
| Mexico | 31 May 2016 | Suramericana S.A. |
| Uruguay | 30 June 2016 | Suramericana S.A. |

The revenue, expenses and related income tax expense in 2016 and 2015 relating to these discontinued operations is set out below.

The total loss on the sale of discontinued operations disposed of during the year after tax was **£29m** (2015: profit of £170m).

Discontinued income statement

for the year ended 31 December 2016

| | Notes | 2016 £m | 2015 £m |
|---|-------|--------------|--------------|
| Income | | | |
| Gross written premiums | | 256 | 1,365 |
| Less: reinsurance premiums | | (87) | (492) |
| Net written premiums | 8 | 169 | 873 |
| Change in the gross provision for unearned premiums | | 38 | 32 |
| Less: change in provision for unearned reinsurance premiums | | (19) | (53) |
| Change in provision for unearned premiums | | 19 | (21) |
| Net earned premiums | | 188 | 852 |
| Net investment return | 9 | 16 | 60 |
| Total income | | 204 | 912 |
| Expenses | | | |
| Gross claims incurred | | (304) | (672) |
| Less: claims recoveries from reinsurers | | 208 | 222 |
| Net claims | 10 | (96) | (450) |
| Underwriting and policy acquisition costs | | (89) | (366) |
| Unwind of discount | | (5) | (15) |
| Other operating expenses | 12 | (7) | (45) |
| | | (197) | (876) |
| (Loss)/gain on disposal | | (29) | 170 |
| (Loss)/profit before tax | | (22) | 206 |
| Income tax expense | 17 | (5) | (50) |
| (Loss)/profit after tax | | (27) | 156 |

Discontinued statement of comprehensive income
for the year ended 31 December 2016

| | 2016 £m | 2015 £m |
|---|-------------|------------|
| (Loss)/profit for the year from discontinued operations | (27) | 156 |
| Items from discontinuing operations that may be reclassified to the income statement: | | |
| Exchange losses/(gains) recycled on disposal of discontinued operations net of tax | 111 | (39) |
| Exchange gains/(losses) net of tax | 3 | (53) |
| Exchange losses on non-controlling interests net of tax | – | (3) |
| | 114 | (95) |
| Fair value losses/(gains) recycled on disposal of discontinued operations net of tax | 1 | (6) |
| Fair value gains/(losses) on available for sale financial assets net of tax | 3 | (9) |
| | 4 | (15) |
| Items from discontinuing operations that will not be reclassified to the income statement: | | |
| Movement in property revaluation, net of tax | 2 | 4 |
| Other comprehensive income/(expense) for the year from discontinued operations | 120 | (106) |
| Total comprehensive income for the year from discontinued operations | 93 | 50 |

6(ii) Held for Sale disposal groups

The assets (including any goodwill allocated to the business) and the liabilities of the businesses held for sale are shown below.

As at 31 December 2016

| | UK Legacy £m | Oman £m | UK Other £m | Total £m |
|---|-----------------|------------|----------------|--------------|
| Assets classified as held for sale: | | | | |
| Property and equipment | – | – | 4 | 4 |
| Investments | 689 | 87 | – | 776 |
| Reinsurers' share of insurance contract liabilities | 90 | 6 | – | 96 |
| Insurance and reinsurance debtors | – | 15 | – | 15 |
| Other debtors and other assets | 9 | 6 | 1 | 16 |
| Cash and cash equivalents | 101 | 3 | – | 104 |
| Total assets of disposal groups | 889 | 117 | 5 | 1,011 |
| Remeasurement of disposal groups to fair value less costs to sell | (204) | – | – | (204) |
| Assets of operations classified as held for sale | 685 | 117 | 5 | 807 |
| Liabilities directly associated with assets classified as held for sale: | | | | |
| Insurance contract liabilities | 685 | 50 | – | 735 |
| Insurance and reinsurance liabilities | – | 5 | – | 5 |
| Provisions and other liabilities | – | 10 | – | 10 |
| Liabilities of operations classified as held for sale | 685 | 65 | – | 750 |
| Net assets of operations classified as held for sale | – | 52 | 5 | 57 |

Significant Transactions and Events – continued

As at 31 December 2015

| | Latin America £m | Russia £m | Total £m |
|---|---------------------|--------------|--------------|
| Assets classified as held for sale: | | | |
| Goodwill and intangibles | 63 | – | 63 |
| Property and equipment | 21 | – | 21 |
| Investments | 380 | – | 380 |
| Reinsurers' share of insurance contract liabilities | 237 | – | 237 |
| Insurance and reinsurance debtors | 468 | 1 | 469 |
| Other debtors and other assets | 77 | 3 | 80 |
| Cash and cash equivalents | 77 | 20 | 97 |
| Assets of operations classified as held for sale | 1,323 | 24 | 1,347 |
| Liabilities directly associated with assets classified as held for sale: | | | |
| Insurance contract liabilities | 699 | 12 | 711 |
| Insurance and reinsurance liabilities | 175 | – | 175 |
| Provisions and other liabilities | 200 | 4 | 204 |
| Liabilities of operations classified as held for sale | 1,074 | 16 | 1,090 |
| Net assets of operations classified as held for sale | 249 | 8 | 257 |

Discontinued operations disposed of during the year

Year ended 31 December 2016

| | Latin America £m | Russia £m | Total £m |
|---|---------------------|--------------|-------------|
| Consideration received | 434 | 5 | 439 |
| Less: transaction costs | (20) | (1) | (21) |
| Net proceeds from sales | 414 | 4 | 418 |
| Carrying value of net assets disposed of | (321) | (3) | (324) |
| Gains on sale before recycling of items from other comprehensive income | 93 | 1 | 94 |
| Recycle of items from other comprehensive income on disposals: | | | |
| Foreign currency translation reserve | (99) | (11) | (110) |
| Unrealised gains on available for sale investments | (1) | – | (1) |
| Profits on sales of discontinued operations before tax | (7) | (10) | (17) |
| Tax on disposal | (12) | – | (12) |
| Profits on sales of discontinued operations after tax | (19) | (10) | (29) |

Discontinued operations disposed of during the year

Year ended 31 December 2015

| | Hong Kong, Singapore and Labuan £m | China £m | India (associate) £m | Italy £m | Total £m |
|--|---|-------------|----------------------------|-------------|-------------|
| Consideration received | 123 | 69 | 46 | 18 | 256 |
| Less: transaction costs | (13) | (2) | – | (5) | (20) |
| Net proceeds from sales | 110 | 67 | 46 | 13 | 236 |
| Carrying value of net assets disposed of | (35) | (47) | (18) | – | (100) |
| Gains on sale before recycling of items from other comprehensive income | 75 | 20 | 28 | 13 | 136 |
| Recycle of items from other comprehensive income on disposals: | | | | | |
| Foreign currency translation reserve | 27 | 8 | (4) | 8 | 39 |
| Unrealised gains on available for sale investments | 1 | – | (3) | 10 | 8 |
| Related tax | – | – | – | (2) | (2) |
| Profits on sales of discontinued operations before tax | 103 | 28 | 21 | 29 | 181 |
| Tax on disposal | – | (2) | (4) | (5) | (11) |
| Profits on sales of discontinued operations after tax | 103 | 26 | 17 | 24 | 170 |

6(iii) (Loss)/gains on disposal of businesses not classified as discontinued

In 2016, the assets and liabilities of the Oman and UK Legacy business are classified as held for sale. Upon classification as held for sale, the net assets are measured at the lower of carrying amount and fair value less costs to sell. This valuation adjustment results in a **£234m** loss which is recognised in the continuing income statement.

Further information on the classification of the UK Legacy business as held for sale can be found in note 43.

In 2015, the £3m of gains on disposal of businesses not classified as discontinued include £2m relating to the disposal of the Engineering Inspection & Consultancy division in both UK & Ireland to Infexion Private Equity Partners on 1 November 2015.

7) Reorganisation costs

In 2016, the reorganisation costs of **£160m** (note 8 and note 12) are directly associated with continuing operations (2015: £183m). The amounts are directly attributable to redundancy **£49m** (2015: £59m) and other restructuring activity of **£111m** (2015: £124m). Restructuring costs in 2016 relate to amounts incurred across the Group for activities such as process re-engineering, office footprint consolidation, reducing spans of control, and renegotiation of supplier contracts. These include the transition to a new IT infrastructure provider, Wipro, in the UK, Ireland and Scandinavia.

Notes to the Income Statement, Other Comprehensive Income and Dividends

8) Segmental information

The Group's operating segments comprise Scandinavia, Canada, UK & International, Central functions and non-core, which is consistent with how the Group is managed.

The primary operating segments are based on geography and are all engaged in providing personal and commercial general insurance services. Central functions include the Group's internal reinsurance function and Group Corporate Centre.

Core businesses

The Group's principal core businesses are Scandinavia, Canada, and UK & International. These represent separate operating segments, and the major geographical areas in which the Group continues to operate through established businesses in mature markets.

Each operating segment is managed by a member of the Group Executive Committee who is directly accountable to the Group Chief Executive and Board of Directors, who together form the central decision making function in respect of the operating activities of the Group. The UK is the Group's country of domicile and one of its principle markets.

Amounts attributable to Central Functions are also included within the core business results.

During 2016, following a reorganisation change, the Middle East was combined with the UK and Ireland regions to form the 'UK & International' segment. Previously the Middle East operations were reported under non-core. The 2015 segmental results have been re-presented accordingly.

Non-core segment

The Group's non-core segment is comprised of the Group's UK legacy business, which is managed as part of the UK operations. The UK Legacy business is not presented as a discontinued operation as it is not a separate geographical area nor a major line of business.

When businesses become classified as discontinued (see note 6) their results on a segmental basis are re-presented from non-core and into discontinued operations, and the comparatives are re-presented on the same basis. During 2016, no further operations were classified as discontinued and as such, the 2015 comparatives do not require re-presentation.

Assessing segment performance

The Group uses the following key measures to assess the performance of its operating segments:

- Net written premiums;
- Underwriting result;
- Combined operating ratio ('COR');
- Operating result.

Net written premiums is the key measure of revenue used in internal reporting.

Underwriting result, COR and operating result are the key internal measures of profitability of the operating segments. The COR reflects the ratio of claims costs and expenses (including commission) to earned premiums, expressed as a percentage.

Transfers or transactions between segments are entered into under normal commercial terms and conditions that would also be available to unrelated third parties.

Year ended 31 December 2016

| | Core | | | | | | | Continuing operations per income statement £m | Add discontinued operations £m | Total Group £m |
|--|--------------------|--------------|--------------------------------|---------------|-------------------|-------------------------|----------------|--|-----------------------------------|-------------------|
| | UK & International | | | | | | | | | |
| | Scandinavia £m | Canada £m | UK (excluding Legacy) £m | Ireland £m | Middle East £m | Central Functions £m | Non-core £m | | | |
| Net written premiums | 1,721 | 1,443 | 2,588 | 306 | 187 | 36 | (42) | 6,239 | 169 | 6,408 |
| Underwriting result | 239 | 74 | 123 | (49) | 14 | (9) | (16) | 376 | 4 | 380 |
| Investment result | 72 | 66 | 136 | 7 | 6 | – | 2 | 289 | 9 | 298 |
| Central costs and other activities | – | – | – | – | – | (23) | – | (23) | – | (23) |
| Operating result (management basis) | 311 | 140 | 259 | (42) | 20 | (32) | (14) | 642 | 13 | 655 |
| Realised gains | | | | | | | | 28 | 2 | 30 |
| Unrealised gains, impairments and foreign exchange | | | | | | | | (4) | – | (4) |
| Interest costs | | | | | | | | (138) | – | (138) |
| Amortisation of intangible assets | | | | | | | | (16) | – | (16) |
| Pension net interest and administration costs | | | | | | | | (4) | – | (4) |
| Solvency II costs | | | | | | | | (7) | – | (7) |
| Reorganisation costs | | | | | | | | (160) | (8) | (168) |
| Economic assumption changes | | | | | | | | (6) | – | (6) |
| Losses on disposals of businesses | | | | | | | | (234) | (17) | (251) |
| Profit/(loss) before tax | | | | | | | | 101 | (10) | 91 |
| Tax on continuing operations | | | | | | | | (54) | (5) | (59) |
| Tax on disposals of discontinued operations | | | | | | | | – | (12) | (12) |
| Profit/(loss) after tax | | | | | | | | 47 | (27) | 20 |
| Combined operating ratio (%) | 86.2 | 94.9 | 95.4 | 116.2 | 92.8 | | | | | 94.2 |

Notes to the Income Statement, Other Comprehensive Income and Dividends – continued

Year ended 31 December 2015 (re-presented)

| | Core UK & International | | | | | | | Continuing operations per income statement £m | Add discontinued operations £m | Total Group £m |
|--|----------------------------|--------------|-----------------------------------|---------------|----------------------|----------------------------|----------------|---|---|----------------------|
| | Scandinavia £m | Canada £m | UK (excluding Legacy) £m | Ireland £m | Middle East £m | Central Functions £m | Non-core £m | | | |
| Net written premiums | 1,606 | 1,360 | 2,606 | 261 | 181 | (111) | 49 | 5,952 | 873 | 6,825 |
| Underwriting result | 94 | 116 | 12 | (35) | 8 | 50 | (60) | 185 | 35 | 220 |
| Investment result | 69 | 66 | 135 | 9 | 3 | – | 1 | 283 | 39 | 322 |
| Central costs and other activities | – | – | – | – | – | (18) | 1 | (17) | (2) | (19) |
| Operating result (management basis) | 163 | 182 | 147 | (26) | 11 | 32 | (58) | 451 | 72 | 523 |
| Realised gains | | | | | | | | 21 | 4 | 25 |
| Unrealised gains, impairments and foreign exchange | | | | | | | | (9) | 4 | (5) |
| Interest costs | | | | | | | | (106) | – | (106) |
| Amortisation of intangible assets | | | | | | | | (25) | (2) | (27) |
| Pension net interest and administration costs | | | | | | | | (8) | – | (8) |
| Solvency II costs | | | | | | | | (26) | – | (26) |
| Reorganisation costs | | | | | | | | (183) | – | (183) |
| Impairment of goodwill and intangible assets | | | | | | | | (9) | (42) | (51) |
| Non-recurring charges | | | | | | | | (3) | – | (3) |
| Gains on disposals of businesses | | | | | | | | 3 | 181 | 184 |
| Profit before tax | | | | | | | | 106 | 217 | 323 |
| Tax on continuing operations | | | | | | | | (18) | (50) | (68) |
| Tax on disposals of discontinued operations | | | | | | | | – | (11) | (11) |
| Profit after tax | | | | | | | | 88 | 156 | 244 |
| Combined operating ratio (%) | 94.0 | 91.7 | 99.5 | 113.4 | 95.4 | | | | | 96.9 |

9) Net investment return

A summary of the gross investment income, net realised and net unrealised gains/(losses) included in the income statement is given below:

| | Investment income | | Net realised gains/(losses) | | Net unrealised (losses)/gains | | Impairments | | Total investment return | |
|-------------------------------------|-------------------|------------|-----------------------------|------------|-------------------------------|------------|-------------|------------|-------------------------|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m | 2016 £m | 2015 £m | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| Investment property | 23 | 22 | – | 2 | (4) | 25 | – | – | 19 | 49 |
| Equity securities | | | | | | | | | | |
| Available for sale | 24 | 20 | 12 | 21 | – | – | (2) | (2) | 34 | 39 |
| At FVTPL | 4 | 5 | 2 | – | – | (7) | – | – | 6 | (2) |
| Debt securities | | | | | | | | | | |
| Available for sale | 289 | 289 | 14 | 4 | – | – | – | (3) | 303 | 290 |
| At FVTPL | – | – | – | – | (9) | (1) | – | – | (9) | (1) |
| Other loans and receivables: | | | | | | | | | | |
| Loans secured by mortgages | 2 | 1 | – | – | – | – | – | – | 2 | 1 |
| Other loans | – | – | – | (6) | – | – | 10 | (2) | 10 | (8) |
| Short term investments | 1 | 2 | – | – | – | – | – | – | 1 | 2 |
| Group occupied property | – | – | – | – | – | (2) | – | – | – | (2) |
| Deposits, cash and cash equivalents | 7 | 5 | – | – | – | 1 | – | – | 7 | 6 |
| Derivatives | 5 | 3 | – | – | (31) | 4 | – | – | (26) | 7 |
| Continuing operations | 355 | 347 | 28 | 21 | (44) | 20 | 8 | (7) | 347 | 381 |
| Discontinued operations | 14 | 56 | 2 | 4 | – | – | – | – | 16 | 60 |
| Total net investment return | 369 | 403 | 30 | 25 | (44) | 20 | 8 | (7) | 363 | 441 |

Direct operating expenses (including repairs and maintenance) arising from investment properties were not material in 2016 or 2015.

Unrealised gains and losses recognised in other comprehensive income for available for sale assets are as follows:

| | Net unrealised gains/(losses) | | Net realised (gains)/losses transferred to income statement | | Impairments transferred to income statement | | Net movement recognised in other comprehensive income | |
|------------------------------------|-------------------------------|-------------------------|---|-------------------------|---|-------------------------|---|-------------------------|
| | 2016 £m | Re-presented 2015 £m | 2016 £m | Re-presented 2015 £m | 2016 £m | Re-presented 2015 £m | 2016 £m | Re-presented 2015 £m |
| Equity securities | 21 | (23) | (13) | (20) | 2 | 5 | 10 | (38) |
| Debt securities | 169 | (180) | (11) | (4) | – | – | 158 | (184) |
| Other | 10 | (8) | – | 6 | (10) | 2 | – | – |
| Total continuing operations | 200 | (211) | (24) | (18) | (8) | 7 | 168 | (222) |
| Discontinued operations | 5 | (8) | (1) | (8) | – | – | 4 | (16) |
| Total | 205 | (219) | (25) | (26) | (8) | 7 | 172 | (238) |

10) Net claims

| | 2016 £m | 2015 £m |
|---|--------------|--------------|
| Gross claims paid | 4,840 | 4,574 |
| Gross changes in provision for losses and loss adjustment expenses | (14) | (78) |
| Reinsurance recoveries on claims paid | (353) | (307) |
| Reinsurers' share of changes in provision for losses and loss adjustment expenses | (354) | (60) |
| Continuing operations | 4,119 | 4,129 |
| Discontinued operations | 96 | 450 |
| Total net claims | 4,215 | 4,579 |

Notes to the Income Statement, Other Comprehensive Income and Dividends – continued

11) Other operating income

| | 2016 £m | Re-presented ¹ 2015 £m |
|-------------------------------------|------------|---|
| Engineering inspection fees | – | 36 |
| Administration fees income | 39 | 30 |
| Instalment policy fee income | 17 | 10 |
| Introductory commissions | 27 | 23 |
| Service income | 14 | 14 |
| Other fees | 41 | 29 |
| Foreign exchange gain | 32 | – |
| Continuing operations | 170 | 142 |
| Discontinued operations | – | – |
| Total other operating income | 170 | 142 |

Note:

1. Other operating income has been further analysed in 2016 into the categories noted above. The 2015 comparatives have been re-presented on the same basis.

12) Other operating expenses

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Administration and other expenses | 30 | 17 |
| Investment expenses and charges | 12 | 14 |
| Amortisation of intangible assets | 16 | 25 |
| Pension administration expenses | 4 | 8 |
| Solvency II costs | 7 | 26 |
| Reorganisation costs (see note 7) | 160 | 183 |
| Impairment of goodwill and other intangible assets (see note 22) | – | 9 |
| Foreign exchange losses | – | 23 |
| Non-recurring charges ¹ | – | 3 |
| Continuing operations | 229 | 308 |
| Discontinued operations | 7 | 45 |
| Total other operating expenses | 236 | 353 |

Note:

1. In 2015, the £3m non-recurring charges represent costs incurred in relation to the Zurich Insurance Group bid for RSA.

13) Finance costs

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Interest expense on loan capital | 97 | 104 |
| Premium on debt buy back ¹ | 39 | 2 |
| Other loan interest | 2 | – |
| Total finance costs relating to continuing operations | 138 | 106 |

Note:

1. On 7 July 2016, the Group bought back £200m of its holding of 9.375% Lower Tier 2 guaranteed subordinated step-up notes on which a premium was paid of £39m for early redemption.

14) Employee expenses

Staff costs for all employees comprise:

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Wages and salaries | 621 | 739 |
| Social security costs | 85 | 102 |
| Pension costs | 82 | 93 |
| Share based payments to directors and employees | 16 | 14 |
| Total staff costs | 804 | 948 |
| Staff costs relating to continuing operations | 780 | 848 |
| Staff costs relating to discontinued operations | 24 | 100 |

The average number of employees during the year are as follows:

| | 2016 Number | Re-presented ¹ 2015 Number |
|--|----------------|---|
| Scandinavia | 3,214 | 3,382 |
| Canada | 3,318 | 3,599 |
| UK & International ¹ | 7,142 | 8,452 |
| Average number of employees during the year relating to continuing operations | 13,674 | 15,433 |
| Average number of employees during the year relating to discontinued operations | 754 | 2,954 |
| Total average number of employees during the year | 14,428 | 18,387 |

Note:

1. During the 2016 year, the Middle East region (previously non-core) has been included as part of UK & International. To ensure consistency in presentation, the average number of employees for UK & International for 2015 has been re-presented. UK & International includes staff employed in central functions.

Further information on pension obligations of the Group can be found in note 37. Further information on employee share schemes can be found in note 18.

15) Related party transactions

The following transactions were carried out with key management:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Salaries and other short term employee benefits | 7 | 9 |
| Bonus awards | 5 | 5 |
| Pension benefits | 1 | 1 |
| Share based awards | 4 | 2 |
| Total | 17 | 17 |

Key management personnel comprise members of the Group Executive Committee, executive directors, and non-executive directors.

Included in salaries and other short term employee benefits and bonus awards is **£5,239,000** (2015: £5,378,000) paid in respect of directors. These amounts exclude the value of share options granted to directors and gains made on the exercise of such options, Group contributions paid in respect of pension schemes and cash or other assets received or receivable under long term incentive schemes. The total value of the directors' remuneration (including values for these excluded items) and other details are disclosed in the remuneration report.

A number of the directors, other key managers, their close families and entities under their control have general insurance policies with subsidiary companies of the Group. Such policies are available at discounted rates to all employees including executive directors.

Notes to the Income Statement, Other Comprehensive Income and Dividends – continued

16) Auditor's remuneration

| | 2016 | | 2015 | |
|--|------------------|--------------------|------------------|--------------------|
| | Continuing £m | Discontinued £m | Continuing £m | Discontinued £m |
| Fees payable to the auditor for audit of the Company's annual accounts | 0.7 | – | 0.9 | – |
| Fees payable to the auditor and its associates for other services: | | | | |
| The audit of the Company's subsidiaries, pursuant to legislation | 3.9 | – | 3.3 | 0.9 |
| Audit related assurance services | 1.7 | – | 0.8 | – |
| Other services | 0.1 | – | 0.1 | – |
| | 6.4 | – | 5.1 | 0.9 |

Included in the Audit related assurance work for 2016 is **£1.4m** of assurance work in respect of Solvency II reporting, including preparation for the new regulatory regime. The remainder of **£0.3m** (2015: £0.8m), together with 'Other services' of **£0.1m** (2015: £0.1m), is ancillary non-audit work representing in aggregate **9%** (2015: 17%) of the Group IFRS audit fee of **£4.6m** (2015: £5.1m).

17) Income tax

The tax amounts charged/(credited) in the income statement are as follows:

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Current tax | 90 | 85 |
| Deferred tax | (36) | (67) |
| Total taxation attributable to continuing operations | 54 | 18 |
| Tax on disposal of discontinued operations | 12 | 11 |
| Tax on profits of discontinued operations | 5 | 50 |
| Taxation attributable to the Group | 71 | 79 |

Reconciliation of the income tax expense

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Profit before tax | 101 | 106 |
| Tax at the UK rate of 20% (2015: 20.2%) | 20 | 21 |
| Tax effect of: | | |
| Income/gains not taxable | (3) | (8) |
| Expenses not deductible for tax purposes | 7 | 7 |
| Impairment and amortisation of goodwill | 6 | 1 |
| Movement in deferred tax assets not recognised | (17) | (26) |
| Increase/(release) of tax provided in respect of prior periods | 2 | (4) |
| Different tax rates of subsidiaries operating in other jurisdictions | 17 | 8 |
| Withholding tax on dividends from subsidiaries | 5 | 5 |
| Effect of change in tax rates | 16 | 15 |
| Other | 1 | (1) |
| Total income tax expense attributable to continuing operations | 54 | 18 |
| Total income tax expense attributable to discontinued operations | 17 | 61 |
| Income tax expense | 71 | 79 |

The current tax and deferred income tax credited/(charged) to each component of other comprehensive income is as follows:

| | Current Tax | | Deferred Tax | | Total | |
|---|-------------|------------|--------------|-------------|------------|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| Fair value gains and losses | 5 | 49 | (24) | (33) | (19) | 16 |
| Remeasurement of net defined benefit pension liability | – | – | 64 | (16) | 64 | (16) |
| Total credited/(charged) to other comprehensive income | 5 | 49 | 40 | (49) | 45 | – |

The aggregate current tax and deferred tax relating to items that are charged directly to equity is **£nil** (2015: £nil).

Tax Rates

The table below provides a summary of the current tax and deferred tax rates for the year in respect of the core tax jurisdictions in which the Group operates.

| | 2016 | | 2015 | |
|---------|-------------|--------------|-------------|--------------|
| | Current Tax | Deferred Tax | Current Tax | Deferred Tax |
| UK | 20.0% | 17.0% | 20.2% | 18.0% |
| Canada | 27.5% | 27.5% | 26.8% | 26.8% |
| Denmark | 22.0% | 22.0% | 23.5% | 22.0% |
| Ireland | 12.5% | 12.5% | 12.5% | 12.5% |
| Sweden | 22.0% | 22.0% | 22.0% | 22.0% |

18) Share based payments

The total amount included within staff costs in the consolidated income statement in respect of all share scheme plans in 2016 is **£16m** (2015: £14m).

Analysis of share scheme costs:

| | 2016 £m | 2015 £m |
|-------------------------------|------------|------------|
| Long-Term Incentive Plan 2006 | – | 1 |
| Performance Share Plan 2014 | 14 | 9 |
| SAYE | 1 | 2 |
| Sharebuild | 1 | 2 |
| Total | 16 | 14 |

Analysis of new award costs:

| | 2016 | | 2015 | |
|-----------------------------|-----------------------|---------------------------|-----------------------|---------------------------|
| | Charge for year £m | Total value granted £m | Charge for year £m | Total value granted £m |
| Performance Share Plan 2014 | 6 | 15 | 5 | 13 |
| SAYE | – | 1 | – | 1 |
| Total | 6 | 16 | 5 | 14 |

The balance of the value of the awards will be charged to the consolidated income statement during the remaining vesting periods.

Performance Share Plan 2014

This plan is the Group's current Long-Term Incentive Plan (LTIP). Awards of performance shares to executive directors and other selected executives and senior managers are subject to performance conditions consisting of the Group's underlying return on tangible equity, relative total shareholder return and business review scorecard targets over a three year performance period. All awards vest on the third anniversary of the date of grant to the extent that the performance conditions have been met.

The Remuneration Committee may also make conditional awards of restricted shares to other executives and senior managers, which are not subject to performance conditions.

Additionally, the Remuneration Committee may defer a portion of an individual's gross bonus (limited to 50% of that bonus) into an award over shares referred to for the purpose of the plan as deferred bonus shares, which are also not subject to performance conditions.

If an employee resigns from the Group, then performance shares and restricted shares lapse at date of leaving the Group. Deferred Bonus Shares awards are generally retained by the employee to whom the share was granted if they leave the Group, unless the employee is dismissed for cause.

However, the Remuneration Committee has the discretion to modify the treatment of leavers' share awards that have yet to be released, based on the leaving circumstances, where this is appropriate and in shareholders' interests. Awards retained will vest on the normal vesting date.

Long-Term Incentive Plan 2006

This plan was replaced by the Performance Share Plan 2014. No awards have been granted under this plan since 2013 year end.

Further information can be found in the Directors' Remuneration Report within the Corporate Governance section.

Notes to the Income Statement, Other Comprehensive Income and Dividends – continued

19) Earnings per share

The earnings per ordinary share are calculated by reference to the profit attributable to the ordinary shareholders and the weighted average number of shares in issue during the year. These were **1,018,173,824** for basic EPS and **1,024,448,507** for diluted EPS (excluding those held in Employee Stock Ownership Plan (ESOP) and Share Incentive Plan (SIP) trusts). The number of shares in issue at 31 December 2016 was **1,019,140,938** (excluding those held in ESOP and SIP trusts).

Basic EPS

| | 2016 | | 2015 | |
|---|------------|--------------|------------|--------------|
| | Continuing | Discontinued | Continuing | Discontinued |
| Profit/(loss) attributable to the shareholders of the Parent Company (£m) | 54 | (27) | 79 | 156 |
| Less: cumulative preference dividends (£m) | (9) | – | (9) | – |
| Profit/(loss) for the calculation of earnings per share | 45 | (27) | 70 | 156 |
| Weighted average number of Ordinary Shares in issue (thousands) | 1,018,174 | 1,018,174 | 1,015,489 | 1,015,489 |
| Basic earnings/(loss) per share (p) | 4.4 | (2.6) | 6.9 | 15.4 |

| | 2016 £m | 2015 £m |
|---|--------------|-------------|
| Weighted average number of Ordinary Shares in issue (thousands) | 1,018,174 | 1,015,489 |
| Adjustments for share options and contingently issuable shares (thousands) | 6,275 | 3,791 |
| Total weighted average number of Ordinary Shares for diluted earnings per share (thousands) continuing operations | 1,024,449 | 1,019,280 |
| Diluted earnings per share (p) relating to continuing operations | 4.4 | 6.9 |
| Diluted (loss)/earnings per share (p) relating to discontinued operations | (2.6) | 15.3 |

Note 32 includes further information of the outstanding share options and unvested share awards to Group employees that could potentially dilute basic earnings per share in the future, including those awards omitted from the calculation of diluted earnings per share because they were antidilutive in 2016 and 2015.

20) Dividends paid and proposed

The final dividend to equity holders is recognised as a liability when approved at the Annual General Meeting. The Company and its subsidiaries may be subject to restrictions on the amount of dividends they can pay to shareholders as a result of regulatory requirements. However, based on the information currently available, the Group does not believe that such restrictions materially limit the ability to meet obligations or pay dividends. At the Annual General Meeting (AGM) on 5 May 2017, a final dividend in respect of the year ended 31 December 2016 of **11p** per ordinary share amounting to a total dividend of **£112m** is to be proposed. The proposed dividend will be paid and accounted for in shareholders' equity as an appropriation of retained earnings in the year ending 31 December 2017.

| | 2016 p | 2015 p | 2016 £m | 2015 £m |
|---|-----------|-----------|------------|------------|
| Ordinary dividend: | | | | |
| Final paid in respect of prior year | 7.0 | 2.0 | 71 | 20 |
| Interim paid in respect of current year | 5.0 | 3.5 | 51 | 36 |
| | 12.0 | 5.5 | 122 | 56 |
| Preference dividend | | | 9 | 9 |
| | | | 131 | 65 |

21) Total other comprehensive income

Year ended 31 December 2016

| | Investment valuation reserve £m | Group occupied property reserve £m | Hedging instrument reserve £m | Total re- valuation reserves £m | Foreign currency translation reserve £m | Retained earnings £m | Shareholders' equity £m | Non- controlling interests £m | Total equity £m |
|---|--|--|--|--|---|----------------------------|-------------------------------|--|-----------------------|
| Exchange gains net of tax | 24 | – | – | 24 | 299 | – | 323 | 19 | 342 |
| Fair value gains net of tax | 154 | – | – | 154 | – | 1 | 155 | – | 155 |
| Pension – remeasurement of net defined benefit liability net of tax | – | – | – | – | – | (316) | (316) | – | (316) |
| Movement in property revaluation net of tax | – | 3 | – | 3 | – | – | 3 | – | 3 |
| | – | | | | | | | | |
| Total other comprehensive income for the year | 178 | 3 | – | 181 | 299 | 315 | 165 | 19 | 184 |

Year ended 31 December 2015

| | Investment valuation reserve £m | Group occupied property reserve £m | Hedging instrument reserve £m | Total re- valuation reserves £m | Foreign currency translation reserve £m | Retained earnings £m | Shareholders' equity £m | Non- controlling interests £m | Total equity £m |
|---|--|--|--|--|---|----------------------------|-------------------------------|--|-----------------------|
| Exchange (losses)/gains net of tax | (15) | (1) | – | (16) | (204) | – | (220) | 5 | (215) |
| Fair value losses net of tax | (222) | – | (3) | (225) | – | – | (225) | (1) | (226) |
| Pension – remeasurement of net defined benefit liability net of tax | – | – | – | – | – | 65 | 65 | – | 65 |
| Movement in property revaluation net of tax | – | 7 | – | 7 | – | – | 7 | – | 7 |
| | | | | | | | | | |
| Total other comprehensive (expense)/income for the year | (237) | 6 | (3) | (234) | (204) | 65 | (373) | 4 | (369) |

Notes to the Statement of Financial Position

22) Goodwill and intangible assets

| As at 31 December 2016 | Goodwill £m | Intangible assets arising from acquired claims provisions £m | Externally acquired software £m | Internally generated software £m | Other £m | Total £m |
|---|----------------|---|--|---|-------------|--------------|
| Cost | | | | | | |
| At 1 January 2016 | 514 | 109 | 86 | 614 | 245 | 1,568 |
| Additions and transfers | – | – | 1 | 131 | 9 | 141 |
| Disposals | (144) | – | (6) | (47) | (39) | (236) |
| Exchange adjustment | 70 | 19 | 1 | 55 | 44 | 189 |
| At 31 December 2016 | 440 | 128 | 82 | 753 | 259 | 1,662 |
| Accumulated amortisation | | | | | | |
| At 1 January 2016 | – | 108 | 64 | 355 | 151 | 678 |
| Amortisation charge | – | 1 | 8 | 61 | 18 | 88 |
| Amortisation on disposals | – | – | (5) | (25) | (25) | (55) |
| Exchange adjustment | – | 19 | 1 | 27 | 28 | 75 |
| At 31 December 2016 | – | 128 | 68 | 418 | 172 | 786 |
| Accumulated impairment | | | | | | |
| At 1 January 2016 | 151 | – | – | 55 | 5 | 211 |
| Impairment charge | 30 | – | – | 1 | – | 31 |
| Impairment on disposals | (86) | – | – | (16) | – | (102) |
| Exchange adjustment | – | – | – | 8 | – | 8 |
| At 31 December 2016 | 95 | – | – | 48 | 5 | 148 |
| Carrying amount at 31 December 2016 | 345 | – | 14 | 287 | 82 | 728 |
| Less: Assets classified as held for sale | – | – | – | – | – | – |
| Carrying amount at 31 December 2016 net of held for sale | 345 | – | 14 | 287 | 82 | 728 |

| As at 31 December 2015 | Goodwill £m | Intangible assets arising from acquired claims provisions £m | Externally acquired software £m | Internally generated software £m | Other £m | Total £m |
|---|----------------|---|--|---|-------------|--------------|
| Cost | | | | | | |
| At 1 January 2015 | 545 | 117 | 123 | 592 | 278 | 1,655 |
| Additions and transfers | – | – | 2 | 51 | – | 53 |
| Disposals | – | (1) | (33) | (8) | (7) | (49) |
| Exchange adjustment | (31) | (7) | (6) | (21) | (26) | (91) |
| At 31 December 2015 | 514 | 109 | 86 | 614 | 245 | 1,568 |
| Accumulated amortisation | | | | | | |
| At 1 January 2015 | – | 114 | 77 | 318 | 149 | 658 |
| Amortisation charge | – | 2 | 10 | 56 | 22 | 90 |
| Amortisation on disposals | – | (1) | (20) | (8) | (6) | (35) |
| Exchange adjustment | – | (7) | (3) | (11) | (14) | (35) |
| At 31 December 2015 | – | 108 | 64 | 355 | 151 | 678 |
| Accumulated impairment | | | | | | |
| At 1 January 2015 | 133 | – | 3 | 57 | 4 | 197 |
| Impairment charge | 18 | – | – | 3 | 1 | 22 |
| Impairment on disposals | – | – | (1) | (3) | – | (4) |
| Exchange adjustment | – | – | (2) | (2) | – | (4) |
| At 31 December 2015 | 151 | – | – | 55 | 5 | 211 |
| Carrying amount at 31 December 2015 | 363 | 1 | 22 | 204 | 89 | 679 |
| Less: Assets classified as held for sale | 45 | – | 1 | 7 | 10 | 63 |
| Carrying amount at 31 December 2015 net of held for sale | 318 | 1 | 21 | 197 | 79 | 616 |

Amortisation

Amortisation expense of **£72m** (2015: £63m) has been charged to underwriting and policy acquisition costs with the remainder recognised in other operating expenses.

Impairments

During 2016 the software impairment charge is **£1m** (2015: £3m). In 2016 **£1m** (2015: £1m) of software impairment had been recognised within other operating expenses. In 2016 no software impairment was charged to underwriting and policy acquisition costs (2015: £2m).

When testing for goodwill impairment, the carrying value of the CGU to which goodwill has been allocated is compared to the recoverable amount as determined by a value in use calculation. These calculations use cashflow projections based on operating plans approved by management covering a three year period and using the best estimates of future premiums, operating expenses and taxes using historical trends, general geographical market conditions, industry trends and forecasts and other available information as discussed in more detail in the strategic report section. Cashflows beyond this period are extrapolated using the estimated growth rates which management deem appropriate for the CGU. The cashflow forecasts are adjusted by appropriate discount rates. Where a sales price has been agreed for a CGU, the sales proceeds less costs to sell are considered the best estimate of the value in use.

Where the value in use is less than the current carrying value of the CGU in the Statement of Financial Position, the goodwill is impaired in order to ensure that the CGU carrying value is not greater than its future value to the Group.

Goodwill impairment charges of **£30m** (2015: £18m) have been recognised within other operating expenses, split between continuing operations **£30m** in Oman (2015: Scandinavian Marine £6m) and discontinued operations **£nil** (2015: Argentina £12m).

The Oman Government has issued legislation by royal decree, which requires a proportion of the company to be offered to the public which is currently expected to result in the Group losing control of the business. As a result of the expected loss of control, the business in Oman is classified as held for sale (HFS) measured at fair value less costs to sell resulting in a revaluation impairment of **£30m** of which £20m is attributable to Non Controlling Interest.

Goodwill is allocated to the Group's CGUs, which are contained within the following operating segments as follows:

| | 2016 £m | Re-presented 2015 £m |
|---------------------------|------------|----------------------------|
| Scandinavia | 152 | 131 |
| Canada | 160 | 130 |
| UK and Ireland | 33 | 57 |
| Non-core and discontinued | – | 45 |
| Total Goodwill | 345 | 363 |

Impairment Sensitivity

Following completion of the Group impairment testing, it was identified that the Norwegian and Canadian Commercial goodwill valuation models were sensitive to changes in key assumptions.

The sensitivities are listed below:

| | Norway Potential headroom/ (Impairment) £m | Canadian Commercial Potential (Impairment) £m |
|---|--|---|
| Impairment sensitivity | | |
| 1% decrease in terminal value growth rate | 1 | (55) |
| 1% increase to discount rate | (21) | (69) |

The range of pre-tax discount rates used for goodwill impairment testing, which reflect specific risks relating to the CGU at the date of evaluation and weighted average growth rates used in 2016 for the cash generating units within each operating segment are shown below. The growth rates include improvements in trade performance, where these are forecast in the three year operational plan for the CGU.

| | Pre-tax discount rate | | Weighted average growth rate | |
|--------------|-----------------------|---------|------------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Scandinavia | 9%–10% | 9%–11% | 2%–3% | 2%–3% |
| Canada | 11%–12% | 10%–11% | 2%–4% | 3%–4% |
| UK & Ireland | 9%–11% | 10%–11% | 2% | 2% |

The key assumptions used by the cash generating unit (CGU) Trygg-Hansa, with goodwill of **£115m**, within the Scandinavia region were discount rate of **8%** and growth rate of **2%** and by CGU RSA Commercial, with goodwill of **£82m**, within the Canadian region were discount rate of **9%** and growth rate of **4%**. All other CGUs are not considered significant in comparison to the total value of goodwill.

Notes to the Statement of Financial Position – continued

23) Property and equipment

| | Group occupied property–land and buildings 2016 £m | Other 2016 £m | Total 2016 £m | Group occupied property–land and buildings 2015 £m | Other 2015 £m | Total 2015 £m |
|--|---|---------------------|---------------------|---|---------------------|---------------------|
| Cost/valuation | | | | | | |
| At 1 January | 52 | 272 | 324 | 57 | 307 | 364 |
| Additions | 1 | 26 | 27 | 1 | 19 | 20 |
| Disposal of subsidiaries | (16) | (28) | (44) | – | (13) | (13) |
| Other disposals | – | (24) | (24) | (7) | (15) | (22) |
| Revaluation adjustments credited to Other Comprehensive Income | 3 | – | 3 | 7 | – | 7 |
| Revaluation adjustments charged to Income Statement | – | – | – | (2) | – | (2) |
| Exchange adjustment | (2) | 30 | 28 | (4) | (26) | (30) |
| At 31 December | 38 | 276 | 314 | 52 | 272 | 324 |
| Accumulated depreciation | | | | | | |
| At 1 January | 1 | 191 | 192 | 1 | 211 | 212 |
| Depreciation charge | 2 | 20 | 22 | 1 | 22 | 23 |
| Depreciation on disposals | – | (34) | (34) | – | (23) | (23) |
| Exchange adjustment | 1 | 19 | 20 | (1) | (19) | (20) |
| At 31 December | 4 | 196 | 200 | 1 | 191 | 192 |
| Accumulated impairment | | | | | | |
| At 1 January | – | 2 | 2 | – | – | – |
| Impairment charge | – | – | – | – | 2 | 2 |
| Impairment on disposals | – | (1) | (1) | – | – | – |
| Exchange adjustment | – | – | – | – | – | – |
| At 31 December | – | 1 | 1 | – | 2 | 2 |
| Carrying amount at 31 December | 34 | 79 | 113 | 51 | 79 | 130 |
| Less: Assets classified as held for sale | 4 | – | 4 | 13 | 8 | 21 |
| Carrying amount at 31 December net of held for sale | 30 | 79 | 109 | 38 | 71 | 109 |

Other includes fixtures, fittings and other equipment. Group occupied property was revalued on 31 December 2016 by independent valuers using the basis of valuation as set out in note 26.

Depreciation expenses of **£22m** (2015: £23m) have been charged to underwriting costs and policy acquisition costs.

The carrying amount of group occupied property that would have been recognised had the assets been carried under the cost model including assets held for sale at 31 December 2016 is **£30m** (2015: £38m).

The movement in the Group occupied property reserve is shown below:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| At 1 January | 22 | 20 |
| Revaluation adjustment (note 21) | 3 | 7 |
| Transfers and disposal of subsidiaries | (9) | (4) |
| Exchange adjustment | 1 | (1) |
| Group occupied property reserve at 31 December | 17 | 22 |

24) Investment Property

Investment property, consisting of **£333m** (2015: £365m) freehold and leasehold land and buildings, is held for long term rental yields and is not occupied by the Group.

The movement in the carrying value of investment property is detailed below:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| At 1 January | 369 | 346 |
| Sales | (28) | – |
| Disposal of subsidiaries | (4) | – |
| Fair value (losses)/gains | (4) | 25 |
| Exchange adjustment | – | (2) |
| Investment property at 31 December | 333 | 369 |
| Less: Assets classified as held for sale | – | 4 |
| Investment property at 31 December net of assets held for sale | 333 | 365 |

Investment properties are included in the Group's investment portfolio to provide investment returns over the longer term in accordance with the Group's investment strategy. Investment properties are managed by external managers.

The lease agreements are normally drawn up in line with local practice and the Group has no significant exposure to leases that include contingent rents.

25) Financial assets

The following table analyses the Groups financial assets by classification as at 31 December 2016 and 31 December 2015.

As at 31 December 2016

| | At FVTPL £m | Available for sale £m | Loans and receivables £m | Total £m |
|--|----------------|-----------------------------|--------------------------------|---------------|
| Equity securities | 6 | 686 | – | 692 |
| Debt securities | 19 | 12,302 | – | 12,321 |
| Financial assets measured at fair value | 25 | 12,988 | – | 13,013 |
| Loans and receivables | – | – | 88 | 88 |
| Total financial assets | 25 | 12,988 | 88 | 13,101 |
| Less: Assets classified as held for sale | | | | |
| Debt securities | – | 776 | – | 776 |
| Total financial assets net of held for sale | 25 | 12,212 | 88 | 12,325 |

As at 31 December 2015

| | At FVTPL £m | Available for sale £m | Loans and receivables £m | Total £m |
|--|----------------|-----------------------------|--------------------------------|---------------|
| Equity securities | 38 | 547 | – | 585 |
| Debt securities | 15 | 11,473 | – | 11,488 |
| Financial assets measured at fair value | 53 | 12,020 | – | 12,073 |
| Loans and receivables | – | – | 100 | 100 |
| Total financial assets | 53 | 12,020 | 100 | 12,173 |
| Less: Assets classified as held for sale | | | | |
| Debt securities | – | 376 | – | 376 |
| Total assets classified as held for sale | – | 376 | – | 376 |
| Total financial assets net of held for sale | 53 | 11,644 | 100 | 11,797 |

Notes to the Statement of Financial Position – continued

The following table analyses the cost/amortised cost, gross unrealised gains and losses and fair value of financial assets.

| | 2016 | | | 2015 | |
|--|----------------------------------|---------------------------|---|------------------|------------------|
| | Cost/ amortised cost £m | Unrealised gains £m | Unrealised losses and impairments £m | Fair value £m | Fair value £m |
| Equity securities | 689 | 48 | (45) | 692 | 585 |
| Debt securities | 11,794 | 627 | (100) | 12,321 | 11,488 |
| Financial assets measured at fair value | 12,483 | 675 | (145) | 13,013 | 12,073 |
| Loans and receivables | 88 | – | – | 88 | 100 |
| Total financial assets | 12,571 | 675 | (145) | 13,101 | 12,173 |
| Less: Assets classified as held for sale | | | | | |
| Debt securities | 776 | – | – | 776 | 376 |
| Total financial assets net of held for sale | 11,795 | 675 | (145) | 12,325 | 11,797 |

Collateral

At 31 December 2016, the Group had pledged **£763m** (2015: £376m) of financial assets as collateral for liabilities or contingent liabilities. The nature of the assets pledged as collateral comprises government securities of **£636m** (2015: £314m), cash and cash equivalents of **£114m** (2015: £50m) and debt securities of **£13m** (2015: £12m). The terms and conditions of the collateral pledged are market standard in relation to letter of credit facilities.

At 31 December 2016, the Group has accepted **£101m** (2015: £554m) in collateral. The Group is permitted to sell or repledge collateral held in the event of default by the owner. The fair value of the collateral accepted is **£101m** (2015: £554m). The terms and conditions of the collateral held are market standard. The assets held as collateral are readily convertible into cash.

Derivative financial instruments

The following table presents the fair value and notional amount of derivatives by term to maturity and nature of risk.

As at 31 December 2016

| | Notional Amount | | | | Fair Value | |
|--|---------------------------|----------------------------|-----------------------|-------------|-------------|-----------------|
| | Less than 1 year £m | From 1 to 5 years £m | Over 5 years £m | Total £m | Asset £m | Liability £m |
| Designated as hedging instruments | | | | | | |
| Currency risk (net investment in foreign operation) | 1,271 | – | – | 1,271 | 7 | (20) |
| Cross currency interest swaps (fair value/cashflow) | 17 | 264 | 261 | 542 | 2 | (109) |
| Total | | | | | 9 | (129) |
| At FVTPL | | | | | | |
| Currency risk mitigation | 317 | – | – | 317 | 6 | (2) |
| Inflation risk mitigation | – | – | 332 | 332 | 41 | (36) |
| Total | | | | | 47 | (38) |
| Total derivatives | | | | | 56 | (167) |

Derivative financial instruments

The following table presents the fair value and notional amount of derivatives by term to maturity and nature of risk.

As at 31 December 2015

| | Notional Amount | | | Fair Value | |
|--|------------------------|-------------------------|--------------------|-------------|----------------|
| | Less than 1 year £m | From 1 to 5 years £m | Over 5 years £m | Total £m | |
| Designated as hedging instruments | | | | | |
| Currency risk (net investment in foreign operation) | 1,076 | – | – | 1,076 | 7 (8) |
| Cross currency interest swaps (fair value/cashflow) | – | 160 | 158 | 318 | – (39) |
| Total | | | | | 7 (47) |
| At FVTPL | | | | | |
| Currency risk mitigation | 252 | 39 | – | 291 | – (8) |
| Inflation risk mitigation | – | – | 236 | 236 | 31 (34) |
| Total | | | | | 31 (42) |
| Total derivatives | | | | | 38 (89) |

The use of derivatives can result in accounting mismatches when gains and losses arising on the derivatives are presented in the income statement in accordance with the Group's accounting policies and corresponding losses and gains on the risks being mitigated are not included in the income statement. In such circumstances the Group may apply hedge accounting in accordance with IFRS and the Group accounting policy on hedging.

The Group applies hedge accounting to derivatives acquired to reduce foreign exchange risk in its net investment in certain major overseas subsidiaries. There was no ineffectiveness recognised in the income statement in respect of these hedges during 2016 or 2015.

The Group also applies hedge accounting to specified fixed interest assets in its investment portfolio. During 2014, the Group invested in a portfolio of high investment grade corporate bonds denominated in US dollars to allow it to invest in a more diversified range of issuers. These investments are used to cover the insurance liabilities in the UK business. In order to remove exchange risk from this portfolio of investments the Group also acquired cross currency interest rate swaps to swap the cashflows from the portfolio into cashflows denominated in pounds Sterling. The Group applies fair value hedge accounting when using 'fixed to floating' interest rate swaps and cashflow hedge accounting when using 'fixed to fixed' interest rate swaps. The interest rate swaps exactly offset the timing and amounts expected to be received on the underlying investments. The investments have a remaining term of between two and eight years. There have been no default and no defaults are expected on the hedged investments.

The total gains/losses on cashflow hedge instruments during 2016 was a **£6m gain** (2015: loss of £4m) in the consolidated statement of other comprehensive income, and the amount reclassified to the income statement was **£1m** (2015: £nil). The ineffectiveness recognised in the income statement was **£nil** (2015: £nil).

The total losses on the fair value hedge instruments recognised in the income statement were **£50m** (2015: £19m) and the offsetting gains related to the hedged risk were **£45m** (2015: £18m).

The Group enters into derivative transactions under International Swaps and Derivatives Association (ISDA) master netting arrangements. In general, under such agreements the amounts owed by each counterparty on a single day in respect of all transactions outstanding in the same currency are aggregated into a single net amount that is payable by one counterparty to the other. In certain circumstances, such as a credit default, all outstanding transactions under the agreement are terminated, the termination value is assessed and only a single net amount is payable in settlement of all transactions.

The ISDA agreements do not meet the criteria for offsetting in the statement of financial position. This is because the Group does not have any current legally enforceable right to offset recognised amounts, because the right to offset is enforceable only on the occurrence of future events. The tables below provide information on the impact of the netting arrangements.

In addition, during 2016, the Group took out borrowings from credit institutions under repurchase agreements of **£249m** (note 35). The Group continues to recognise debt securities in the statement of financial position as the Group remains exposed to the risks and rewards of ownership.

Notes to the Statement of Financial Position – continued

As at 31 December 2016

| | Amounts subject to enforceable netting arrangements | | | | | |
|---|---|-------------------------|----------------------------------|--------------------------------|-------------------------------|---------------------|
| | Effect of offsetting in statement of financial position | | | Related items not offset | | |
| | Gross amounts £m | Amounts offset £m | Net amounts reported £m | Financial instruments £m | Financial collateral £m | Net amount £m |
| Derivative financial assets | 56 | – | 56 | (45) | (9) | 2 |
| Reverse repurchase arrangements and other similar secured lending | 249 | – | 249 | (249) | – | – |
| Total assets | 305 | – | 305 | (294) | (9) | 2 |
| Derivative financial liabilities | 167 | – | 167 | (45) | (113) | 9 |
| Repurchase arrangements and other similar secured borrowing | 249 | – | 249 | (249) | – | – |
| Total liabilities | 416 | – | 416 | (294) | (113) | 9 |

As at 31 December 2015

| | Amounts subject to enforceable netting arrangements | | | | | |
|---|---|-------------------------|-------------------------------|--------------------------------|-------------------------------|------------------|
| | Effect of offsetting in statement of financial position | | | Related items not offset | | |
| | Gross amounts £m | Amounts offset £m | Net amounts reported £m | Financial instruments £m | Financial collateral £m | Net amount £m |
| Derivative financial assets | 38 | – | 38 | (34) | – | 4 |
| Reverse repurchase arrangements and other similar secured lending | – | – | – | – | – | – |
| Total assets | 38 | – | 38 | (34) | – | 4 |
| Derivative financial liabilities | 89 | – | 89 | (34) | (46) | 9 |
| Repurchase arrangements and other similar secured borrowing | – | – | – | – | – | – |
| Total liabilities | 89 | – | 89 | (34) | (46) | 9 |

26) Fair value measurement

Fair value is used to value a number of assets within the statement of financial position and represents its market value at the reporting date.

Cash and cash equivalents, loans and receivables

For cash, loans and receivables, commercial paper, other assets, liabilities and accruals, their carrying amounts are considered to be as approximate fair values.

Group occupied property and investment property

Group occupied properties are valued on a vacant possession basis using third party valuers. Investment properties are valued, at least annually, at their highest and best use.

The fair value of property has been determined by external, independent valuers, having appropriate recognised professional qualifications and recent experience in the location and category of the property being valued.

The valuations of buildings with vacant possession are based on the comparative method of valuation with reference to sales of other vacant buildings. Fair value is then determined based on the locational qualities and physical building characteristics (principally condition, size, specification and layout) as appropriate.

Investment properties are valued using discounted cashflow models which take into account the net present value of cashflows to be generated from the properties. The cashflow streams reflect the current rent (the gross rent) payable to lease expiry, at which point it is assumed that each unit will be re-let at its estimated rental value. Allowances have been made for voids and rent free periods where applicable. The appropriate rent to be capitalised is selected on the basis of the location of the building, its quality, tenant credit quality and lease terms amongst other factors.

These cashflows are discounted at an appropriate rate of interest to determine their present value.

In both cases the estimated fair value would increase/(decrease) if:

- The estimated rental value is higher/(lower);
- Void periods were shorter/(longer);
- The occupancy rate were higher/(lower);
- Rent free periods were shorter/(longer);
- The discount rates were lower/(higher).

Derivative financial instruments

Derivative financial instruments are financial contracts whose fair value is determined on a market basis by reference to underlying interest rate, foreign exchange rate, equity or commodity instrument or indices.

Loan capital

The fair value measurement of the Group's loan capital instruments, with the exception of the subordinated guaranteed US\$ bonds, are based on pricing obtained from a range of financial intermediaries who base their valuations on recent transactions of the Group's loan capital instruments and other observable market inputs such as applicable risk free rate and appropriate credit risk spreads.

The fair value measurement of the subordinated guaranteed US\$ bonds is also obtained from an indicative valuation based on the applicable risk free rate and appropriate credit risk spread.

Fair value hierarchy

Fair value for all assets and liabilities which are either measured or disclosed is determined based on available information and categorised according to a three-level fair value hierarchy as detailed below.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from data other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3 fair value measurements are those derived from valuation techniques that include significant inputs for the asset or liability valuation that are not based on observable market data (unobservable inputs).

A financial instrument is regarded as quoted in an active market (level 1) if quoted prices for that financial instrument are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

The Group uses prices received from external providers who calculate these prices from quotes available at the reporting date for the particular investment being valued. For investments that are actively traded the Group determines whether the prices meet the criteria for classification as a level 1 valuation. The price provided is classified as a level 1 valuation when it represents the price at which the investment traded at the reporting date taking into account the frequency and volume of trading of the individual investment together with the spread of prices that are quoted at the reporting date for such trades. Typically investments in frequently traded government debt would meet the criteria for classification in the level 1 category. Where the prices provided do not meet the criteria for classification in the level 1 category, the prices are classified in the level 2 category.

In limited circumstances, the Group does not receive pricing information from an external provider for its financial investments. In such circumstances the Group calculates fair value based which may use input parameters that are not based on observable market data. Unobservable inputs are based on assumptions that are neither supported by prices from observable current market transactions for the same instrument nor based on available market data. In these cases, judgment is required to establish fair values. Valuations that require the significant use of unobservable data are classified as level 3 valuations. In addition, the valuations used for investment properties and for group occupied properties are classified in the level 3 category.

Notes to the Statement of Financial Position – continued

The following table provides an analysis of financial instruments and other items that are measured subsequent to initial recognition at fair value as well as financial liabilities not measured at fair value, grouped into levels 1 to 3. The table does not include financial assets and liabilities not measured at fair value if the carrying value is a reasonable approximation of fair value.

As at 31 December 2016

| | Fair value hierarchy 2016 | | | | Total £m |
|--|---------------------------|---------------|---------------|---|---------------|
| | Level 1 £m | Level 2 £m | Level 3 £m | Less: Assets of operations classified as held for sale £m | |
| Group occupied property – land and buildings | – | – | 34 | 4 | 30 |
| Investment properties | – | – | 333 | – | 333 |
| Available for sale financial assets: | | | | | |
| Equity securities | 323 | – | 363 | – | 686 |
| Debt securities | 4,256 | 7,780 | 266 | 776 | 11,526 |
| Financial assets at FVTPL: | | | | | |
| Equity securities | – | – | 6 | – | 6 |
| Debt securities | – | – | 19 | – | 19 |
| | 4,579 | 7,780 | 1,021 | 780 | 12,600 |
| Derivative assets: | | | | | |
| At FVTPL | – | 47 | – | – | 47 |
| Designated as hedging instruments | – | 9 | – | – | 9 |
| Total assets measured at fair value | 4,579 | 7,836 | 1,021 | 780 | 12,656 |
| Derivative liabilities: | | | | | |
| At FVTPL | – | 38 | – | – | 38 |
| Designated as hedging instruments | – | 129 | – | – | 129 |
| Total liabilities measured at fair value | – | 167 | – | – | 167 |
| Loan capital | – | 1,129 | 8 | – | 1,137 |
| Total value of liabilities not measured at fair value | – | 1,129 | 8 | – | 1,137 |

During 2016, the Group has further refined the basis of valuation of certain investments. As a consequence, the Group transferred **£3,074m** of debt securities from a classification of Level 1 to a classification of Level 2.

As at 31 December 2015

| | Fair value hierarchy 2015 | | | | Total £m |
|--|---------------------------|---------------|---------------|---|---------------|
| | Level 1 £m | Level 2 £m | Level 3 £m | Less: Assets of operations classified as held for sale £m | |
| Group occupied property – land and buildings | – | – | 38 | – | 38 |
| Investment properties | – | – | 369 | 4 | 365 |
| Available for sale financial assets: | | | | | |
| Equity securities | 278 | – | 269 | – | 547 |
| Debt securities | 6,988 | 4,331 | 154 | 376 | 11,097 |
| Financial assets at FVTPL: | | | | | |
| Equity securities | – | – | 38 | – | 38 |
| Debt securities | – | – | 15 | – | 15 |
| | 7,266 | 4,331 | 883 | 380 | 12,100 |
| Derivative assets: | | | | | |
| At FVTPL | – | 31 | – | – | 31 |
| Designated as hedging instruments | – | 7 | – | – | 7 |
| Total assets measured at fair value | 7,266 | 4,369 | 883 | 380 | 12,138 |
| Derivative liabilities: | | | | | |
| At FVTPL | – | 42 | – | – | 42 |
| Designated as hedging instruments | – | 47 | – | – | 47 |
| Total liabilities measured at fair value | – | 89 | – | – | 89 |
| Loan capital | – | 1,361 | 8 | – | 1,369 |
| Total value of liabilities not measured at fair value | – | 1,361 | 8 | – | 1,369 |

Notes to the Statement of Financial Position – continued

The movement in the fair value measurements of Level 3 financial assets is shown in the table below:

| | Available for sale investments | | Investments at FVTPL | | |
|---|--------------------------------|-----------------------|-------------------------|-----------------------|-------------|
| | Equity securities £m | Debt securities £m | Equity securities £m | Debt securities £m | Total £m |
| At 1 January 2015 | 129 | 2 | 43 | 18 | 192 |
| Total (losses)/gains recognised in: | | | | | |
| Income statement | – | – | (7) | (1) | (8) |
| Other comprehensive income | (4) | 3 | – | – | (1) |
| Purchases | 152 | 149 | 7 | 14 | 322 |
| Disposals | (4) | – | (5) | (17) | (26) |
| Exchange adjustment | (4) | – | – | 1 | (3) |
| At 1 January 2016 | 269 | 154 | 38 | 15 | 476 |
| Total gains/(losses) recognised in: | | | | | |
| Income statement | 1 | – | 1 | (9) | (7) |
| Other comprehensive income | 16 | 1 | – | – | 17 |
| Purchases | 49 | 96 | 5 | 28 | 178 |
| Disposals | 7 | – | (38) | (15) | (46) |
| Exchange adjustment | 21 | 15 | – | – | 36 |
| Level 3 financial assets at 31 December 2016 | 363 | 266 | 6 | 19 | 654 |

The Group's Property portfolio (including the Group occupied properties) is almost exclusively located in the UK. An increase of 100bps in the discount rate used to value the UK property portfolio would result in a decrease of **£72m** (2015: £62m) in the fair value of the portfolio.

The Group's investments in financial assets classified as Level 3 in the hierarchy are primarily investments in various private fund structures investing in debt instruments where the valuation includes estimates of the credit spreads on the underlying holdings. The estimates of the credit spread are based upon market observable credit spreads for what are considered to be assets with similar credit risk. The aggregate value of these holdings included in the table above at 31 December 2016 is **£670m** (2015: £404m). An increase in the estimate of the credit spread of the underlying holdings of 100bps would result in a reduction in the fair value of these investments of **£29m** (2015: £19m).

27) Interests in structured entities

A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements.

The Group does not securitise any of its investments in financial instruments and does not create, promote or administer structured entities on behalf of third party investors. The Group therefore considers that it does not act as a sponsor for any structured entity.

However, the Group invests in unleveraged entities created by and managed by external specialist investment managers where investments are pooled within an investment vehicle to provide a diversified exposure to particular classes of underlying investments. The use of these products allows the Group to broaden the diversification of its investment portfolio in a cost-efficient manner. The Group normally limits its exposures in individual structured entities to less than 20% of the total capital of the entity.

The Group is exposed to the risks of the underlying investments of the investment vehicles. The investment return from the structured entities is expected to reflect the returns from the underlying investments of the entity.

In addition, the Group has commitments for future undrawn subscriptions limited to the amounts set out in the subscription agreements. The Group has no obligations to provide any other additional funding or other financial support to these entities. The Group has determined that its maximum exposure to structured entities is the sum of the carrying value and the undrawn commitments. These exposures at 31 December 2016 are summarised in the table below:

| Class of investments ¹ | Nature of the underlying investments of the vehicle | Carrying value 2016 £m | Undrawn commitments 2016 £m | Exposure 2016 £m | Re-presented ¹ | | |
|-----------------------------------|---|------------------------------|-----------------------------------|------------------------|------------------------------|-----------------------------------|------------------------|
| | | | | | Carrying value 2015 £m | Undrawn commitments 2015 £m | Exposure 2015 £m |
| Mortgage backed securities | Mortgages in Scandinavia and Canada | 10 | – | 10 | 36 | – | 36 |
| Collateralised debt obligations | Structured debt security backed by bonds | 203 | – | 203 | 143 | – | 143 |
| Cash Money Market funds | Short term cash deposits | 436 | – | 436 | 296 | – | 296 |
| Other | Mainly consist of property funds | 361 | 106 | 467 | 261 | 143 | 404 |
| | | 1,010 | 106 | 1,116 | 736 | 143 | 879 |

Note:

- Following a review of the definition of a structured entity, it is noted that covered bonds (which were included as part of commercial mortgage backed securities) and domestic mortgage backed securities do not meet the criteria of the definition. As a result, the underlying assets that were included in 2015 have been re-presented.

The line items in the statement of financial position in which the investments above are included are as follows:

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Investments – financial assets – equity securities | 363 | 297 |
| Investments – financial assets – debt securities | 205 | 112 |
| Cash and cash equivalents | 436 | 296 |
| Other | 6 | 31 |
| | 1,010 | 736 |

Notes to the Statement of Financial Position – continued

28) Reinsurers' share of insurance contract liabilities

| | 2016 £m | 2015 £m |
|---|--------------|--------------|
| Reinsurers' share of provisions for unearned premiums | 816 | 837 |
| Reinsurers' share of provisions for losses and loss adjustment expenses | 1,436 | 1,151 |
| Total reinsurers' share of insurance contract liabilities net of held for sale | 2,252 | 1,988 |
| To be settled within 12 months | 1,301 | 998 |
| To be settled after 12 months | 951 | 990 |

The following changes have occurred in the reinsurers' share of provision for unearned premiums during the year:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Reinsurers' share of provision for unearned premiums at 1 January | 961 | 709 |
| Premiums ceded to reinsurers | 1,068 | 1,398 |
| Reinsurers' share of premiums earned | (1,096) | (1,145) |
| Changes in reinsurance asset | (28) | 253 |
| Reinsurers' share of portfolio transfers and disposals of subsidiaries | (137) | (2) |
| Exchange adjustment | 22 | 1 |
| Reinsurers' share of provision for unearned premiums at 31 December | 818 | 961 |
| Less: Assets classified as held for sale | 2 | 124 |
| Total Reinsurers' share of provision for unearned premiums at 31 December net of held for sale | 816 | 837 |

The following changes have occurred in the reinsurers' share of provision for losses and loss adjustment expenses during the year:

| | 2016 £m | 2015 £m |
|--|--------------|--------------|
| Reinsurers' share of provisions for losses and loss adjustment expenses at 1 January | 1,264 | 1,317 |
| Reinsurers' share of total claims incurred | 915 | 589 |
| Total reinsurance recoveries received | (414) | (558) |
| Reinsurers' share of portfolio transfers and disposals of subsidiaries | (356) | (57) |
| Exchange adjustment | 113 | (35) |
| Other movements | 8 | 8 |
| Reinsurers' share of provisions for losses and loss adjustment expenses at 31 December | 1,530 | 1,264 |
| Less: Assets classified as held for sale | 94 | 113 |
| Total Reinsurers' share of provisions for losses and loss adjustment expenses at 31 December net of held for sale | 1,436 | 1,151 |

29) Current and Deferred Tax

Current Tax

| | Asset | | Liability | |
|---|------------|------------|------------|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| To be settled within 12 months | 60 | 48 | 25 | 28 |
| To be settled after 12 months | 5 | 8 | 11 | 35 |
| Net current tax position at 31 December | 65 | 56 | 36 | 63 |
| Less: Classified as held for sale | – | 5 | 4 | 32 |
| Net current tax position at 31 December net of held for sale | 65 | 51 | 32 | 31 |

Deferred Tax

| | Asset | | Liability | |
|--|------------|------------|------------|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| Deferred tax assets/liabilities | 270 | 180 | 54 | 54 |
| Less: Classified as held for sale | – | 17 | – | 14 |
| Net deferred tax position at 31 December net of held for sale | 270 | 163 | 54 | 40 |

The following are the major deferred tax assets/(liabilities) recognised by the Group:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Net unrealised gains on investments | (54) | (1) |
| Claims equalisation and other catastrophe reserves | – | (71) |
| Intangibles capitalised | (28) | (21) |
| Deferred acquisition costs | (7) | (24) |
| Tax losses and unused tax credits | 190 | 123 |
| Other deferred tax reliefs | 10 | 11 |
| Net insurance contract liabilities | (15) | (3) |
| Retirement benefit obligations | 55 | (3) |
| Provisions and other temporary differences | 65 | 115 |
| Net deferred tax asset at 31 December | 216 | 126 |
| Less: Net assets classified as held for sale | – | 3 |
| Net deferred tax asset at 31 December net of held for sale | 216 | 123 |

Provisions and other temporary differences arise predominately in respect of UK deferred capital expenditure **£56m** (2015: £80m) and transitional UK tax relief due to the change in taxation of available for sale assets **£16m** (2015: £nil).

Notes to the Statement of Financial Position – continued

The movement in the net deferred tax assets recognised by the continuing Group was as follows:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Net deferred tax position at 1 January | 123 | 118 |
| Amounts credited to income statement | 44 | 79 |
| Amounts credited/(charged) to other comprehensive income | 41 | (50) |
| Amounts charged to equity | – | (1) |
| Net arising on acquisition/disposal of subsidiaries and other transfers | 10 | (8) |
| Exchange adjustments | 7 | (4) |
| Effect of change in tax rates – income statement | (8) | (12) |
| – other comprehensive income | (1) | 1 |
| Net deferred tax asset at 31 December | 216 | 123 |

At the end of the reporting period, the Group's continuing operations have unused tax losses of **£1,629m** (2015: £1,840m) for which no deferred tax asset is being recognised. This includes **£nil** (2015: £4m) which will expire between 2017 and 2025 and **£1,194m** (2015: £1,210m) capital losses for which it is unlikely that a deferred tax asset would be recognised as most UK capital gains are exempt from tax. In addition, the Group has deductible temporary differences of **£654m** (2015: £486m) for which no deferred tax has been recognised.

The Group has temporary differences in respect of the retained earnings of overseas subsidiaries not held for sale of **£1,006m** (2015: £1,053m) on which overseas taxes, including withholding taxes, might be incurred on the remittance of these earnings to the UK. This amount relates to the Group's subsidiaries in Canada. The Group is able to control the remittance of earnings to the UK and there is no intention to remit the retained earnings in the foreseeable future if the remittance would trigger a material incremental tax liability. As such the Group has not recognised any deferred tax in respect of the potential taxes on the temporary differences arising on unremitted earnings of continuing overseas subsidiaries and associates.

Of the **£216m** (2015: £123m) net deferred tax asset recognised by the Group's continuing operations, **£179m** (2015: £117m) relate to tax jurisdictions in which the Group has suffered a loss in either the current or preceding period. The assets have been recognised on the basis that future taxable profits will be available against which these deferred tax assets can be utilised. The evidence for the future taxable profits is a forecast consistent with the three year operational plans prepared by the relevant businesses, which are subject to internal review and challenge. Where relevant, the forecast includes extrapolations of the operational plans using assumptions consistent with those used in the plans.

30) Insurance, reinsurance and other debtors

Insurance and reinsurance debtors

| | 2016 £m | 2015 £m |
|---|--------------|--------------|
| Insurance debtors comprise: | | |
| Due from policyholders | 1,180 | 1,409 |
| Due from intermediaries | 1,490 | 1,545 |
| Total insurance debtors | 2,670 | 2,954 |
| Reinsurance debtors | 168 | 168 |
| Total insurance and reinsurance debtors | 2,838 | 3,122 |
| Less: Assets classified as held for sale | 15 | 469 |
| Total insurance and reinsurance debtors net of held for sale | 2,823 | 2,653 |

Other debtors and other assets

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Derivatives designated as accounting hedging instruments | 9 | 7 |
| Other derivatives | 47 | 31 |
| Other debtors | 130 | 253 |
| Pension scheme surplus | 70 | 195 |
| Accrued interest and rent | 128 | 125 |
| Prepayments | 62 | 141 |
| Total other debtors and assets | 446 | 752 |
| Less: Assets classified as held for sale | 16 | 59 |
| Total other debtors and assets net of held for sale | 430 | 693 |
| To be settled within 12 months | 330 | 442 |
| To be settled after 12 months | 100 | 251 |

31) Cash and cash equivalents

The interest bearing financial assets included in cash and cash equivalents had an effective interest rate of **0.99%** (2015: 1.65%) and had an average maturity of **26 days** (2015: 32 days).

| | 2016 £m | 2015 £m |
|--|--------------|------------|
| Cash and cash equivalents and bank overdrafts (Consolidated Statement of Cashflows) | 1,087 | 902 |
| Add: Overdrafts reported in Other borrowings (note 35) | 2 | 11 |
| Total cash and cash equivalents | 1,089 | 913 |
| Less: Assets classified as held for sale | 104 | 97 |
| Total Cash and cash equivalents (Consolidated Statement of Financial Position) | 985 | 816 |

32) Share capital

The issued share capital of the Parent Company is fully paid and consists of two classes; Ordinary Shares with a nominal value of £1 each and Preference Shares with a nominal value of £1 each. The issued share capital at 31 December 2016 is:

| | 2016 £m | 2015 £m |
|--|--------------|--------------|
| Issued and fully paid | | |
| 1,019,554,986 Ordinary Shares of £1 each (2015: 1,017,059,842 Ordinary Shares of £1 each) | 1,020 | 1,017 |
| 125,000,000 Preference Shares of £1 each (2015: 125,000,000 Preference Shares of £1 each) | 125 | 125 |
| | 1,145 | 1,142 |

During 2016, the Company issued a total of **2,495,144 new Ordinary Shares of £1 each** ranking pari passu with Ordinary Shares in issue (2015: 1,572,969 new Ordinary Shares of £1 each), on the exercise of employee share options and in respect of employee share awards. The number of Ordinary Shares in issue, their nominal value and the associated share premiums are as follows:

| | Number of shares | Nominal value £m | Share premium £m |
|---|----------------------|---------------------|---------------------|
| At 1 January 2015 | 1,015,486,873 | 1,015 | 1,075 |
| Issued in respect of employee share options and employee share awards | 1,572,969 | 2 | 2 |
| At 1 January 2016 | 1,017,059,842 | 1,017 | 1,077 |
| Issued in respect of employee share options and employee share awards | 2,495,144 | 3 | 3 |
| At 31 December 2016 | 1,019,554,986 | 1,020 | 1,080 |

Rights attaching to the shares

The rights attaching to each class of share may be varied with the consent of the holders of 75% of the issued shares of that class.

Ordinary Shares of £1 each

Each member holding an Ordinary Share shall be entitled to vote on all matters at a general meeting of the Company, be entitled to receive dividend payments declared in accordance with the Articles of Association, and have the right to participate in any distribution of capital of the Company including on a winding up of the Company.

Notes to the Statement of Financial Position – continued

Preference Shares of £1 each

The Preference Shares are not redeemable but the holders of the Preference Shares have preferential rights over the holders of Ordinary Shares in respect of dividends and of the return of capital in the event of the winding up of the Company.

Provided a resolution of the Board exists, holders of Preference Shares are entitled to a cumulative preferential dividend of 7.375% per annum, payable out of the profits available for distribution, to be distributed in half yearly instalments. Preference shareholders have no further right to participate in the profits of the Company.

Full information on the rights attaching to shares is in the RSA Insurance Group plc Articles of Association which are available on the Group's website.

Employee share schemes

414,049 Ordinary Shares (2015: 741,636 Ordinary Shares) are held by various employee share trusts which may subsequently be transferred to employees (including Executive Directors) to satisfy Sharebuild Matching Share awards. These shares are presented as own shares. Own shares are deducted from equity. No gain or loss is recognised on the purchase, sale, issue or cancellation of the own shares. Any consideration paid or received is recognised directly in equity.

At 31 December 2016, the total number of options over Ordinary Shares outstanding under the Group employee share option plans is **5,047,441** (2015: 6,784,365) and the total number of potential shares outstanding under the long term incentive plan and under the Sharebuild is **12,638,394** Ordinary Shares (2015: 13,941,035 Ordinary Shares). Further information on the employee share schemes is provided in note 18 and in the Directors' Remuneration Report within the Directors' and Corporate Governance Report.

33) Non-controlling interests

The non-controlling interests (NCI) of the Group includes the interests in the following Group entities:

| | NCI shares at 31 December 2016 | | NCI shares at 31 December 2015 | |
|--|--------------------------------|---------------------------|--------------------------------|---------------------------|
| | % | Share of net assets £m | % | Share of net assets £m |
| Royal & Sun Alliance (Middle East) Ltd | 50 | 113 | 50 | 107 |
| British Aviation Insurance Company Limited | 43 | 17 | 43 | 16 |

Royal & Sun Alliance (Middle East) Ltd owns 50% of the ordinary share capital of Al Alimaya for Cooperative Insurance Company, a company operating in the Kingdom of Saudi Arabia and 70% of Al Ahlia Insurance Company, a company operating in the Sultanate of Oman.

During 2016 the dividends paid to the non-controlling interests in the Middle East were **£3m** (2015: £2m).

34) Loan capital

| | 2016 £m | 2015 £m |
|--|--------------|--------------|
| Subordinated guaranteed US\$ bonds | 6 | 5 |
| Guaranteed subordinated step-up notes due 2039 | 298 | 496 |
| Guaranteed subordinated notes due 2045 | 395 | 394 |
| Total dated loan capital | 699 | 895 |
| Perpetual guaranteed subordinated capital securities | 369 | 359 |
| Total loan capital | 1,068 | 1,254 |

The subordinated guaranteed US\$ bonds were issued in 1999 and have a nominal value of \$9m and a redemption date of 15 October 2029. The rate of interest payable on the bonds is 8.95%.

The dated guaranteed subordinated step-up notes were issued on 20 May 2009 at a fixed rate of 9.375%. The nominal £500m bonds have a redemption date of 20 May 2039. The Group has the right to repay the notes on specific dates from 20 May 2019. If the notes are not repaid on that date, the rate of interest would be reset at a rate of 8.475% plus the appropriate benchmark gilt for a further five year period. On 7 July 2016, the Group bought back £200m in nominal value of these step-up notes.

The dated guaranteed subordinated notes were issued on 10 October 2014 at a fixed rate of 5.125%. The nominal £400m bonds have a redemption date of 10 October 2045. The Group has the right to repay the notes on specific dates from 10 October 2025. If the bonds are not repaid on that date, the applicable rate of interest would be reset at a rate of 3.852% plus the appropriate benchmark gilt for a further five-year period.

The perpetual guaranteed subordinated capital securities issued on 12 May 2006 have a nominal value of £375m and the rate of interest payable is 6.701% of the nominal value. The Group has the option to repay the bonds on specific dates starting 12 July 2017. If the bonds are not repaid, from that date, the interest payable would be LIBOR plus 2.51%.

The bonds and the notes are contractually subordinated to all other creditors of the Group such that in the event of a winding-up or of bankruptcy, they are able to be repaid only after the claims of all other creditors have been met.

There have been no defaults on any bonds or notes during the year. The Group has the option to defer interest payments on the bonds and notes but has to date not exercised this right.

35) Other borrowings

The Group's borrowings as at 31 December 2016 are **£251m** (2015: £11m). The 2016 other borrowings relate to borrowings from credit institutions under repurchase agreements of **£249m** (2015: £nil) and bank accounts in overdraft where no right of offset exists **£2m** (2015: £11m).

At 31 December 2016 total unsecured loans from credit institutions under committed credit facilities of **£nil** (2015: £500m) are available to the Group. The Group retired its committed credit facility in August 2016. Accordingly, there are **no** amounts outstanding at 31 December 2016 (2015: £nil).

At 31 December 2016 the Group has in place a **US\$1bn** (2015: US\$1bn) Euro commercial paper programme. There are no amounts outstanding at 31 December 2016 (2015: £nil).

36) Insurance contract liabilities

Estimation techniques and uncertainties

Provisions for losses and loss adjustment expenses are subject to a robust reserving process by each of the Group's business units and at Group Corporate Centre, as detailed in the Risk and Capital Management note.

There is also considerable uncertainty in regard to the eventual outcome of the claims that have occurred by the end of the reporting period but remain unsettled. This includes claims that may have occurred but have not yet been notified to the Group and those that are not yet apparent to the insured.

The provisions for losses and loss adjustment expenses are estimated using previous claims experience with similar cases, historical payment trends, the volume and nature of the insurance underwritten by the Group and current specific case reserves. Also considered are developing loss payment trends, the potential longer term significance of large events, and the levels of unpaid claims, legislative changes, judicial decisions and economic, political and regulatory conditions.

The Group uses a number of commonly accepted actuarial projection methodologies to determine the appropriate provision to recognise. These include methods based upon the following:

- The development of previously settled claims, where payments to date are extrapolated for each prior year;
- Estimates based upon a projection of claims numbers and average cost;
- Notified claims development, where notified claims to date for each year are extrapolated based upon observed development of earlier years;
- Expected loss ratios;
- Bornhuetter-Ferguson method, which combines features of the above methods;
- Bespoke methods for specialist classes of business.

In selecting the method and estimate appropriate to any one class of insurance business, the Group considers the appropriateness of the methods and bases to the individual circumstances of the provision class and underwriting year.

Individually large and significant claims are generally assessed separately, being measured either at the face value of the loss adjusters' estimates or projected separately in order to allow for the future development of large claims.

The level of provision carried by the Group targets the inclusion of a margin of 5% for the core businesses on top of the actuarial indication outlined above. The appropriateness of the 5% target is subject to regular review as part of the Group reserving process at Group Corporate Centre.

Discount assumptions

The total value of provisions for losses and loss adjustment expenses less related reinsurance recoveries before discounting for continuing operations is **£8,784m** (2015: £8,766m).

Claims on certain classes of business (excluding annuities) have been discounted as follows:

| | | Discount rate | | Average number of years to settlement from reporting date | |
|-------------|----------------------------|---------------|--------|---|------------|
| | Category | 2016 % | 2015 % | 2016 Years | 2015 Years |
| UK | Asbestos and environmental | 4.0 | 4.0 | 11 | 11 |
| Scandinavia | Disability | 1.3 | 1.3 | 7 | 8 |

In determining the average number of years to ultimate claims settlement, estimates have been made based on the underlying claims settlement patterns.

Notes to the Statement of Financial Position – continued

As at 31 December 2016, the value of the discount on net claims liability reserves is **£388m** (2015: £403m) excluding annuities and periodic payment orders. All other factors remaining constant, a decrease of 1% in the discount rates would reduce the value of the discount by approximately **£120m** (2015: £127m).

A decrease of 1% in the real discount rate for UK & Scandinavia annuities would reduce the value of the discount by approximately **£110m** (2015: £86m). The sensitivity calculation has taken into consideration the undiscounted provisions for each class of business and the respective average settlement period.

Gross insurance contract liabilities and the reinsurers' share of insurance contract liabilities

The Group accounting policies in respect of insurance contract liabilities are described in note 4.

The gross insurance contract liabilities and the reinsurers' share of insurance contract liabilities presented in the statement of financial position are comprised as follows:

| | Gross | RI | Net |
|---|---------------|----------------|---------------|
| | 2016 £m | 2016 £m | 2016 £m |
| Provision for unearned premiums | 3,328 | (818) | 2,510 |
| Provision for losses and loss adjustment expenses | 10,083 | (1,530) | 8,553 |
| Total insurance contract liabilities | 13,411 | (2,348) | 11,063 |
| Less: Held for sale provision for unearned premiums | 17 | (2) | 15 |
| Less: Held for sale provisions for losses and loss adjustment expenses | 718 | (94) | 624 |
| Less: Total liabilities held for sale | 735 | (96) | 639 |
| Provision for unearned premiums at 31 December net of held for sale | 3,311 | (816) | 2,495 |
| Provision for losses and loss adjustment expenses at 31 December net of held for sale | 9,365 | (1,436) | 7,929 |
| Total insurance contract liabilities excluding held for sale | 12,676 | (2,252) | 10,424 |

| | Gross | RI | Net |
|---|---------------|----------------|---------------|
| | 2015 £m | 2015 £m | 2015 £m |
| Provision for unearned premiums | 3,445 | (961) | 2,484 |
| Provision for losses and loss adjustment expenses | 9,457 | (1,264) | 8,193 |
| Total insurance contract liabilities | 12,902 | (2,225) | 10,677 |
| Less: Held for sale provision for unearned premiums | 338 | (124) | 214 |
| Less: Held for sale provisions for losses and loss adjustment expenses | 373 | (113) | 260 |
| Less: Total liabilities held for sale | 711 | (237) | 474 |
| Provision for unearned premiums at 31 December net of held for sale | 3,107 | (837) | 2,270 |
| Provision for losses and loss adjustment expenses at 31 December net of held for sale | 9,084 | (1,151) | 7,933 |
| Total insurance contract liabilities excluding held for sale | 12,191 | (1,988) | 10,203 |

Provision for unearned premiums, gross of acquisition costs

The provision for unearned premiums is shown net of deferred acquisition costs of **£663m** (2015: £631m). The movement in deferred acquisition costs during 2016 is attributed to **£1,010m** (2015: £1,026m) increase due to acquisition costs deferred during the year, **£1,037m** (2015: £1,023m) decrease due to amortisation charged during the year, **£56m exchange gains** (2015: £45m exchange losses), **£6m** (2015: £10m) increase due to other movements, and **£3m** (2015: £124m) reduction due to assets transferred to held for sale. The reinsurers' share of deferred acquisition costs is included within accruals and deferred income.

| | 2016 £m | 2015 £m |
|---|--------------|--------------|
| Provision for unearned premiums (gross of acquisition costs) at 1 January | 4,200 | 4,388 |
| Premiums written | 7,477 | 8,224 |
| Less: Premiums earned | (7,624) | (8,158) |
| Changes in provision for unearned premiums | (147) | 66 |
| Gross portfolio transfers and acquisitions | (418) | (154) |
| Exchange adjustment | 357 | (94) |
| Other movements | 2 | (6) |
| Provision for unearned premiums (gross of acquisition costs) at 31 December | 3,994 | 4,200 |
| Less: Liabilities classified as held for sale | 20 | 462 |
| Provision for unearned premiums (gross of acquisition costs) at 31 December net of held for sale | 3,974 | 3,738 |

Provisions for losses and loss adjustment expenses

The following changes have occurred in the provisions for losses and loss adjustment expenses during the year:

| | 2016 £m | 2015 £m |
|---|---------------|--------------|
| Provisions for losses and loss adjustment expenses at 1 January | 9,457 | 10,336 |
| Gross claims incurred and loss adjustment expenses | 5,130 | 5,169 |
| Total claims payments made in the year net of salvage and other recoveries | (5,001) | (5,250) |
| Gross portfolio transfers, acquisitions and disposals | (578) | (459) |
| Exchange adjustment | 994 | (404) |
| Other movements | 81 | 65 |
| Provisions for losses and loss adjustment expenses at 31 December | 10,083 | 9,457 |
| Less: Liabilities classified as held for sale | 718 | 373 |
| Provisions for losses and loss adjustment expenses at 31 December net of held for sale | 9,365 | 9,084 |

Claims development tables

The tables below present changes in the historical provisions for losses and loss adjustment expenses that were established in 2006 and the provisions for losses and loss adjustment expenses arising in each subsequent accident year. The tables are presented at current year average exchange rates on an undiscounted basis and have been adjusted for operations that have been disposed of.

The top triangle of the tables presents the estimated provisions for ultimate incurred losses and loss adjustment expenses for each accident year as at the end of each reporting period.

The lower triangle of the tables presents the amounts paid against those provisions in each subsequent accounting period.

The estimated provisions for ultimate incurred losses change as more information becomes known about the actual losses for which the initial provisions were set up and as the rates of exchange change.

Notes to the Statement of Financial Position – continued

Consolidated claims development table gross of reinsurance

| | 2006 and prior £m | 2007 £m | 2008 £m | 2009 £m | 2010 £m | 2011 £m | 2012 £m | 2013 £m | 2014 £m | 2015 £m | 2016 £m | Total £m |
|---|----------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|---------------|
| Estimate of cumulative claims | | | | | | | | | | | | |
| At end of accident year | 8,890 | 2,577 | 2,522 | 2,426 | 2,658 | 2,853 | 2,714 | 3,018 | 2,725 | 2,718 | 2,700 | |
| One year later | 8,460 | 2,573 | 2,536 | 2,517 | 2,782 | 2,903 | 2,751 | 3,083 | 2,816 | 2,789 | | |
| Two years later | 7,994 | 2,542 | 2,515 | 2,474 | 2,731 | 2,930 | 2,726 | 3,007 | 2,733 | | | |
| Three years later | 7,670 | 2,454 | 2,458 | 2,433 | 2,759 | 2,858 | 2,717 | 2,968 | | | | |
| Four years later | 7,382 | 2,383 | 2,452 | 2,460 | 2,747 | 2,797 | 2,675 | | | | | |
| Five years later | 7,199 | 2,373 | 2,412 | 2,455 | 2,712 | 2,766 | | | | | | |
| Six years later | 6,986 | 2,363 | 2,397 | 2,417 | 2,675 | | | | | | | |
| Seven years later | 6,917 | 2,345 | 2,384 | 2,427 | | | | | | | | |
| Eight years later | 6,888 | 2,325 | 2,381 | | | | | | | | | |
| Nine years later | 7,073 | 2,323 | | | | | | | | | | |
| Ten years later | 7,112 | | | | | | | | | | | |
| 2016 Movement | (39) | 2 | 3 | (10) | 37 | 31 | 42 | 39 | 83 | (71) | | 117 |
| Claims paid | | | | | | | | | | | | |
| One year later | 1,997 | 1,109 | 1,205 | 1,161 | 1,443 | 1,307 | 1,274 | 1,413 | 1,292 | 1,271 | | |
| Two years later | 1,151 | 393 | 384 | 406 | 401 | 474 | 475 | 530 | 408 | | | |
| Three years later | 770 | 266 | 243 | 261 | 276 | 318 | 277 | 262 | | | | |
| Four years later | 661 | 166 | 181 | 193 | 206 | 184 | 182 | | | | | |
| Five years later | 417 | 135 | 119 | 145 | 112 | 104 | | | | | | |
| Six years later | 295 | 83 | 69 | 71 | 62 | | | | | | | |
| Seven years later | 340 | 35 | 38 | 39 | | | | | | | | |
| Eight years later | 261 | 16 | 36 | | | | | | | | | |
| Nine years later | 129 | 22 | | | | | | | | | | |
| Ten years later | 121 | | | | | | | | | | | |
| Cumulative claims paid | 6,142 | 2,225 | 2,275 | 2,276 | 2,500 | 2,387 | 2,208 | 2,205 | 1,700 | 1,271 | | |
| Reconciliation to the statement of financial position | | | | | | | | | | | | |
| Current year provision before discounting | 970 | 98 | 106 | 151 | 175 | 379 | 467 | 763 | 1,033 | 1,518 | 2,700 | 8,360 |
| Exchange adjustment to closing rates | | | | | | | | | | | | 348 |
| Discounting | | | | | | | | | | | | (114) |
| Annuities | | | | | | | | | | | | 771 |
| Present value recognised in the consolidated statement of financial position | | | | | | | | | | | | 9,365 |
| Held for sale | | | | | | | | | | | | 718 |
| Total Group | | | | | | | | | | | | 10,083 |

Consolidated claims development table net of reinsurance

| | 2006 and prior £m | 2007 £m | 2008 £m | 2009 £m | 2010 £m | 2011 £m | 2012 £m | 2013 £m | 2014 £m | 2015 £m | 2016 £m | Total £m |
|---|----------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|------------|--------------|
| Estimate of cumulative claims | | | | | | | | | | | | |
| At end of accident year | 7,507 | 2,215 | 2,299 | 2,199 | 2,351 | 2,494 | 2,463 | 2,639 | 2,410 | 2,290 | 2,142 | |
| One year later | 7,158 | 2,210 | 2,289 | 2,256 | 2,422 | 2,492 | 2,493 | 2,739 | 2,434 | 2,290 | | |
| Two years later | 6,766 | 2,180 | 2,290 | 2,217 | 2,399 | 2,477 | 2,467 | 2,667 | 2,396 | | | |
| Three years later | 6,438 | 2,095 | 2,244 | 2,189 | 2,413 | 2,429 | 2,427 | 2,635 | | | | |
| Four years later | 6,132 | 2,026 | 2,233 | 2,220 | 2,419 | 2,386 | 2,392 | | | | | |
| Five years later | 5,936 | 2,016 | 2,203 | 2,222 | 2,386 | 2,362 | | | | | | |
| Six years later | 5,734 | 2,012 | 2,183 | 2,201 | 2,365 | | | | | | | |
| Seven years later | 5,663 | 1,994 | 2,171 | 2,198 | | | | | | | | |
| Eight years later | 5,675 | 1,984 | 2,169 | | | | | | | | | |
| Nine years later | 5,857 | 1,983 | | | | | | | | | | |
| Ten years later | 5,903 | | | | | | | | | | | |
| 2016 Movement | (46) | 1 | 2 | 3 | 21 | 24 | 35 | 32 | 38 | – | | 110 |
| Claims paid | | | | | | | | | | | | |
| One year later | 1,645 | 928 | 1,074 | 1,066 | 1,223 | 1,127 | 1,148 | 1,262 | 1,122 | 1,069 | | |
| Two years later | 975 | 325 | 337 | 347 | 372 | 393 | 387 | 414 | 354 | | | |
| Three years later | 638 | 238 | 231 | 230 | 246 | 258 | 235 | 233 | | | | |
| Four years later | 512 | 146 | 171 | 184 | 191 | 170 | 187 | | | | | |
| Five years later | 335 | 124 | 102 | 126 | 97 | 103 | | | | | | |
| Six years later | 258 | 66 | 67 | 68 | 58 | | | | | | | |
| Seven years later | 299 | 35 | 34 | 32 | | | | | | | | |
| Eight years later | 230 | 14 | 29 | | | | | | | | | |
| Nine years later | 98 | 20 | | | | | | | | | | |
| Ten years later | 157 | | | | | | | | | | | |
| Cumulative claims paid | 5,147 | 1,896 | 2,045 | 2,053 | 2,187 | 2,051 | 1,957 | 1,909 | 1,476 | 1,069 | | |
| Reconciliation to the statement of financial position | | | | | | | | | | | | |
| Current year provision before discounting | 756 | 87 | 124 | 145 | 178 | 311 | 435 | 726 | 920 | 1,221 | 2,142 | 7,045 |
| Exchange adjustment to closing rates | | | | | | | | | | | | 292 |
| Discounting | | | | | | | | | | | | (104) |
| Annuities | | | | | | | | | | | | 696 |
| Present value recognised in the consolidated statement of financial position | | | | | | | | | | | | 7,929 |
| Held for sale | | | | | | | | | | | | 624 |
| Total Group | | | | | | | | | | | | 8,553 |

Notes to the Statement of Financial Position – continued

Insurance and reinsurance liabilities

| | 2016 £m | 2015 £m |
|--|------------|--------------|
| Direct insurance creditors | 110 | 229 |
| Reinsurance creditors | 849 | 891 |
| Total insurance and reinsurance liabilities | 959 | 1,120 |
| Less: Liabilities classified as held for sale | 5 | 175 |
| Total | 954 | 945 |

37) Post-retirement benefits and obligations

Defined contribution pension schemes

Costs of **£51m** (2015: £52m) were recognised in respect of defined contribution schemes by the Group. The Group's Swedish subsidiaries are part of a multi-employer defined benefit scheme along with other financial institutions in Sweden. As it is not possible to determine the assets and liabilities in respect of any one employer under this scheme, it is included in these accounts as a defined contribution scheme. Contributions of **£8m** (2015: £9m) were paid to this scheme during 2016 and are included in the costs shown above. The expected contributions in 2017 are **£8m**. Total estimated contributions to the scheme from all employers in 2016 were **£62m**. The latest information regarding the funding of this scheme is taken from the interim report for the first half of 2016, when the scheme funding rate was **111%** (2015: 114%).

Defined benefit pension schemes and other post-retirement benefits

Independent actuaries calculate the value of the defined benefit obligations by applying the projected unit credit method. The future expected cash outflows (calculated based on assumptions that include inflation and mortality) are discounted to present value, using a discount rate determined at the end of each reporting period by reference to current market yields on high quality corporate bonds ('AA' rated) identified to match the currency and estimated term of the obligations.

The actuarial valuation involves making assumptions about discount rates, future salary increases, future inflation, the employees' age upon termination and retirement, mortality rates, future pension increases, disability incidence and health and dental care cost trends.

If actual experience differs from the assumptions used, the expected obligation could increase or decrease in future years. Due to the complexity of the valuation and its long-term nature, the defined benefit obligation is highly sensitive to changes in the assumptions. Assumptions are reviewed at each reporting date. As such, the valuation of the liability is highly sensitive to changes in bond rates and will also be impacted by changes in equity markets.

UK Schemes

The major defined benefit pension schemes are located in the UK. The assets of these schemes are mainly held in separate trustee administered funds. The UK defined benefit schemes were effectively closed to new entrants in 2002. The schemes will close to future accruals with effect from 31 March 2017.

The profile of the members of the two main UK schemes at 30 September 2016 (the latest date at which full information is available) is as follows:

| | Number |
|--|---------------|
| Active members – members in employment with the Group and accruing benefits | 1,632 |
| Deferred members – members no longer accruing and not yet receiving benefits | 25,752 |
| Pensioners – members and dependants receiving benefits | 17,679 |
| Total members at 30 September 2016 | 45,063 |

Active members of the schemes accrue additional benefits in each year based on salaries (subject to a salary cap) in that year. Employees are entitled to join a stakeholder pension scheme for earnings above the cap.

Accrued benefits are revalued up to retirement in accordance with Government indices for inflation. A cap of 2.5% per annum applies to the revaluation of accrued benefits. A cap of 5% per annum applies for benefits which accrued prior to March 2010.

After retirement, pensions in payment are increased each year based on the increases in the Government indices for inflation. A cap of 5% applies to benefits (in excess of Guaranteed Minimum Pensions) which accrued prior to 31 December 2005, and a cap of 2.5% applies to benefits accruing after that date.

The UK schemes are managed through trusts with independent trustees responsible for the safeguard of the interests of all members. The trustees meet regularly with Group management to discuss the funding position and any proposed changes to the schemes. The schemes are regulated by The Pension Regulator. Each scheme is subject to triennial valuations, which are used to determine the future funding of the schemes by the Group including funding to repair any funding deficit. The effective date of the most recent valuations of the main UK funds is 31 March 2015.

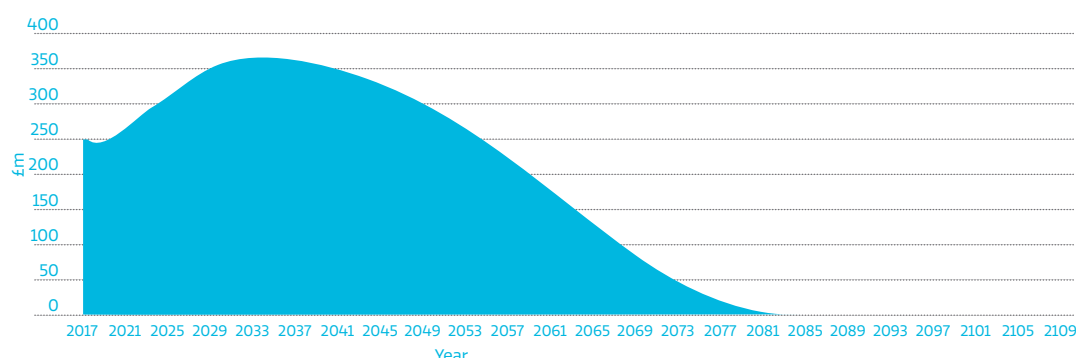
The Group is exposed to risks through its obligation to fund the schemes. These risks include market risk (assets not performing as well as expected), inflation risk and mortality risk over the lives of the members. The Group and the trustees of the schemes work together to reduce these risks through agreement of investment policy including the use of interest rate, inflation rate and mortality swaps.

During 2009 the Group entered into arrangements that provide coverage against mortality risk for 55% of the retirement obligations relating to pensions in payment of the two largest UK schemes at that time. The arrangement provides for reimbursement of the covered pension obligations in return for the contractual return receivable on portfolios of assets (including some interest rate swaps) held by the pension funds at the inception of the arrangement. The arrangement is accounted for as a longevity swap. The longevity swap is measured at fair value under IFRS 13 by discounting all future cashflows using a discount rate that appropriately reflects the terms of the arrangements. The pension schemes continue to hold the original assets used to fund the arrangements.

At the most recent funding valuations, the main UK funds had an aggregate funding deficit of **£392m**, equivalent to a funding level of 95%. The Group and the Trustees agreed funding plans at that time to eliminate the funding deficits by 2025. Details of the deficit contributions paid in 2015 and 2016 and that are due to be paid in 2017 under these plans are disclosed below. The funding plans will be reviewed again following the next triennial funding valuations which will have an effective date of 31 March 2018.

For the two main UK defined benefit schemes, the level of contributions in 2016 were **£96m** (2015: £93m) of which **£66m** (2015: £65m) was additional contributions in line with the plan to reduce funding deficits. Expected contributions to the two schemes for the year ending 31 December 2017 are approximately **£76m** including **£65m** of additional contributions to reduce the deficit.

The maturity profile of the undiscounted cashflows of the two main UK schemes is shown below:



The weighted average duration of the defined benefit obligation of the two main UK schemes at the end of the reporting period is **18.5 years** (2015: 17 years).

The 2002 Scheme (which was the scheme to which new UK employees had been admitted following the closure of the main defined benefit schemes) has been closed to further accrual from 1 January 2006. It has been replaced by a stakeholder arrangement and members of the 2002 Scheme and future new employees in the UK now accrue future benefits on a defined contribution basis under the stakeholder pension scheme.

Notes to the Statement of Financial Position – continued

Non-UK schemes

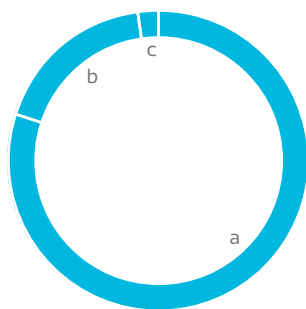
The Group also operates defined benefits schemes in other countries. The most significant of these schemes are in Canada and Ireland.

The Group also provides post-retirement healthcare benefits to certain current and retired Canadian employees. The benefits are not prefunded. Life insurance benefits, which provide varying levels of coverage, are provided at no cost to retirees. Healthcare benefits, which also provide varying levels of coverage, require retiree contributions in certain instances and benefits are generally payable for life.

The split of post-retirement liabilities across other countries is shown below:

Non-UK liability split by country

- a. Canada 80%
- b. Ireland 18%
- c. Scandinavia 2%



All schemes

The estimated discounted present values of the accumulated obligations are calculated in accordance with the advice of independent, qualified actuaries.

Movement in surplus/(deficit) during the year:

| | 2016 £m | 2015 £m |
|--|--------------|------------|
| Surplus/(deficit) at 1 January | 67 | (98) |
| Current service costs | (23) | (30) |
| Past service costs | (5) | (4) |
| Pension net interest credit | 6 | – |
| Administration costs | (9) | (7) |
| Total pension expense | (31) | (41) |
| Contributions by the Group | 110 | 113 |
| Return on scheme assets less amounts included in pension net interest credit | 1,279 | (343) |
| Effect of changes in financial assumptions | (1,770) | 322 |
| Effect of changes in demographic assumptions | 1 | (24) |
| Experience gains and losses | 120 | 140 |
| Investment expenses | (10) | (14) |
| Remeasurements of net defined benefit liability | (380) | 81 |
| Exchange adjustment | (18) | 12 |
| Pension and post-retirement (deficit)/surplus | (252) | 67 |
| Deferred tax in respect of net pension and post-retirement (deficit)/surplus | 55 | (3) |
| Net pension and post-retirement (deficit)/surplus at 31 December | (197) | 64 |

The value of scheme assets and the scheme obligations are as follows:

| | 2016 | | 2015 | |
|---|--------------|--------------|--------------|-------------|
| | UK £m | Other £m | Total £m | Total £m |
| Present value of funded obligations | 8,314 | 460 | 8,774 | 7,030 |
| Present value of unfunded obligations | 7 | 112 | 119 | 96 |
| Present value of obligations | 8,321 | 572 | 8,893 | 7,126 |
| Equities | 597 | 167 | 764 | 723 |
| Government debt | 5,157 | 132 | 5,289 | 4,113 |
| Non government debt | 3,151 | 125 | 3,276 | 2,495 |
| Derivatives | 808 | – | 808 | 476 |
| Other (including infrastructure, commodities, hedge funds, loans) | – | 27 | 27 | – |
| Securities at fair value | 9,713 | 451 | 10,164 | 7,807 |
| Property | 164 | – | 164 | 166 |
| Cash | 55 | 6 | 61 | 73 |
| Other (including infrastructure, commodities, hedge funds, loans) | 484 | – | 484 | 744 |
| Other investments | 703 | 6 | 709 | 983 |
| Value of asset and longevity swaps | (2,232) | – | (2,232) | (1,597) |
| Total assets in the schemes | 8,184 | 457 | 8,641 | 7,193 |
| Total surplus/(deficit) | (137) | (115) | (252) | 67 |
| Defined benefit pension schemes | (137) | (59) | (196) | 111 |
| Other post-retirement benefits | – | (56) | (56) | (44) |
| Schemes in surplus (note 30) | 58 | 12 | 70 | 195 |
| Schemes in deficit (note 38) | (195) | (127) | (322) | (128) |

The UK pension schemes do not hold any of the Group's own transferable financial instruments as plan assets, and no property held by the schemes are occupied by the Group.

The following is a reconciliation of the Group's retirement benefit obligations:

| | 2016 £m | 2015 £m |
|--|--------------|--------------|
| Retirement benefit obligation at 1 January | 7,126 | 7,598 |
| Current service costs | 23 | 30 |
| Past service costs and losses arising from settlements | 5 | 4 |
| Interest cost | 276 | 274 |
| Contributions by scheme participants | 1 | 1 |
| Actuarial losses/(gains) | 1,649 | (439) |
| Gains on curtailments | – | (3) |
| Payments from the schemes | (286) | (286) |
| Exchange rate adjustment | 99 | (53) |
| Retirement benefit obligations at 31 December | 8,893 | 7,126 |

Notes to the Statement of Financial Position – continued

The following is a reconciliation of the Group's pension schemes' assets:

| | 2016 £m | 2015 £m |
|--|--------------|--------------|
| Pension schemes' assets at 1 January | 7,193 | 7,500 |
| Return on schemes' assets included in pension net interest cost | 282 | 274 |
| Return on scheme assets less amounts included in pension net interest cost | 1,279 | (343) |
| Contributions by the Group | 110 | 113 |
| Contributions by schemes' participants | 1 | 1 |
| Total expenses paid from the scheme | (19) | (21) |
| Payments from the schemes | (286) | (286) |
| Settlements | – | (3) |
| Exchange rate adjustment | 81 | (42) |
| Pension schemes' assets at 31 December | 8,641 | 7,193 |

Assumptions

The principal actuarial assumptions used are:

| | UK | | Other | |
|---|-----------|-----------|-----------|-----------|
| | 2016 % | 2015 % | 2016 % | 2015 % |
| Assumptions used in calculation of retirement benefit obligations: | | | | |
| Discount rate | 2.81 | 3.92 | 3.56 | 3.90 |
| Annual rate of inflation (RPI) | 3.37 | 3.02 | – | – |
| Annual rate of inflation (CPI) | 2.27 | 1.92 | 1.72 | 1.52 |
| Annual rate of increase in salaries | 3.37 | 3.02 | 2.74 | 2.57 |
| Annual rate of increase in pensions ¹ | 3.10 | 2.93 | 1.72 | 1.52 |
| Assumptions used in calculation of pension net interest costs for the year: | | | | |
| Discount rate | 3.92 | 3.70 | 3.90 | 3.70 |

Note:

1. For the UK the annual rate of increase in pensions shown is the rate that applies to pensions that increase at RPI subject to a cap of 5%. For other schemes the weighted average assumption is shown.

Mortality rate

The mortality assumptions are set following investigations of the main schemes' recent experience by the schemes' actuaries for the funding valuations. At the funding valuation in March 2015, the mortality assumptions adopted for the main UK schemes used the S2 base tables with percentage adjustments to reflect the schemes' recent experience compared with that expected under these tables.

Reductions in future mortality rates are allowed for by using the CMI 2015 tables with a long term rate of 1.25%. The weighted average assumptions imply that a current pensioner aged 60 has an expected future lifetime of **28.1** (2015: 28.0) years for males and **29.2** (2015: 29.1) years for females and a future pensioner aged 60 in 15 years' time has a future expected lifetime from age 60 of **29.3** (2015: 29.3) years for males and **30.7** (2015: 30.6) years for females.

Sensitivity analysis

Sensitivities for the defined benefit obligations of the two main UK schemes are shown below (net of tax):

| | Changes in assumption | 2016 £m | 2015 £m |
|-----------------------------------|-----------------------|------------|------------|
| Discount rate | Increase by 0.25% | (310) | (222) |
| RPI/CPI ¹ | Increase by 0.25% | 195 | 166 |
| Mortality long-term rate | Increase by 0.25% | 104 | 62 |
| Mortality assumption ² | Reduce by 12% | 274 | 187 |

Notes:

1. The impact shown is for the appropriate increase in the revaluation of deferred pensions and the increases to pensions in payment resulting from the specified increase in RPI and CPI.
 2. Reducing the mortality assumption by 12% is the equivalent of increasing the life expectancy of a male aged 60 years by 1 year.

38) Provisions

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Pensions and post-retirement obligations | 322 | 128 |
| Reorganisation provisions | 14 | 52 |
| Other provisions | 84 | 82 |
| Total provisions at 31 December | 420 | 262 |
| Less: Provisions classified as held for sale | – | 1 |
| Total provisions at 31 December net of held for sale | 420 | 261 |

Of the above, **£320m** (2015: £122m) is due to be settled outside of 12 months.

Other provisions includes **£12m** (2015: £15m) held relating to vacant property leases, dilapidations and refurbishments, the costs relating to which will be borne across the period over which the leases expire, which is up to 20 years, and Motor Insurance Bureau provisions of **£16m** (2015: £13m).

The balance consists of a number of provisions none of which are individually significant.

See note 37 for further information regarding the pensions and post-retirement benefit obligations.

Movements during the year on reorganisation and other provisions

| | Reorganisation provisions 2016 £m | Other provisions 2016 £m |
|--|--|-----------------------------------|
| Provisions at 1 January 2016 | 52 | 82 |
| Exchange adjustment | 2 | 6 |
| Additional provisions during the year | 15 | 42 |
| Utilised | (52) | (34) |
| Released | (3) | (7) |
| Acquisition of subsidiary undertaking | – | (5) |
| Provisions at 31 December 2016 net of held for sale | 14 | 84 |

39) Other liabilities

| | 2016 £m | 2015 £m |
|---|--------------|--------------|
| Deposits received from reinsurers | 67 | 16 |
| Derivatives designated as accounting hedges | 129 | 47 |
| Other derivatives | 38 | 42 |
| Other creditors | 299 | 462 |
| Accruals and deferred income | 560 | 607 |
| Total other liabilities | 1,093 | 1,174 |
| Less: Liabilities classified as held for sale | 6 | 157 |
| Total other liabilities net of held for sale | 1,087 | 1,017 |
| | | |
| To be settled within 12 months | 862 | 843 |
| To be settled after 12 months | 225 | 174 |

Other creditors of **£299m** (2015: £462m) mainly includes payroll and other indirect taxes **£165m** (2015: £201m), outstanding settlements for investment purchases **£nil** (2015: £50m), impairment loss **£nil** (2015: £30m), non-insurance creditors **£32m** (2015: £24m) and other creditors **£102m** (2015: £157m).

Other Commitments and Contingent Liabilities

40) Leases

The operating lease payments recognised as an expense during the year are **£54m** (2015: £54m). The Group has no significant lease agreements that include contingent rent.

Operating lease commitments where the Group is the lessee

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

| | Land and buildings | | Other | |
|--------------------------------|--------------------|------------|------------|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| One year or less | 44 | 42 | 1 | 1 |
| Between one and five years | 138 | 131 | 2 | 1 |
| After five years | 144 | 122 | – | – |
| | 326 | 295 | 3 | 2 |
| Recoveries under sub tenancies | (5) | (7) | – | – |
| Total | 321 | 288 | 3 | 2 |

Operating lease commitments where the Group is the lessor

The future aggregate minimum lease receipts under non-cancellable operating leases are as follows:

| | Land and buildings | |
|----------------------------|--------------------|------------|
| | 2016 £m | 2015 £m |
| One year or less | 22 | 23 |
| Between one and five years | 74 | 81 |
| After five years | 62 | 72 |
| Total | 158 | 176 |

41) Other commitments

Capital Commitments

The Group's significant capital commitments in respect of property and equipment and intangible assets are detailed in the table below:

| | 2016 £m | 2015 £m |
|------------------------|------------|------------|
| Property and equipment | 30 | 53 |
| Intangible assets | 98 | 48 |
| Total | 128 | 101 |

Funding commitments to structured entities and invested assets

The future commitments to structured entities are disclosed in the note 27 of these financial statements. In addition, the Group has committed to invest **£24m** (2015: £147m) in other classes of investments.

42) Other contingent liabilities

In Canada the Group has purchased annuities from regulated Canadian life insurers in order to pay fixed and recurring payments to certain claimants. This arrangement exposes the Group to a credit risk that the life insurers are unable to make these payments which is mitigated by an industry compensation scheme which in that event would assume a significant majority of the remaining outstanding obligations. The likelihood of both a Canadian regulated life insurer and the industry compensation scheme being unable to pay their obligations is considered very remote and so no provision has been recognised in respect of this risk.

The Group receives liability claims and may also become involved in actual or threatened litigation, during the ordinary course of its business operations. The Group reviews and, in the opinion of the directors, maintains sufficient provisions, capital and reserves in respect of such claims.

In addition, the Group has given guarantees, indemnities and warranties in relation to the disposals of its businesses and business interests to external parties. These are kept under review and, in the opinion of the directors, no material loss will arise in respect of these guarantees, indemnities and warranties.

Events after the Reporting Period

43) Events after the Reporting Period

On 7 February 2017, the Group signed contracts to dispose of UK legacy insurance liabilities to Enstar Group Limited.

The transaction takes the form of an initial reinsurance agreement, effective at 31 December 2016, which substantially effects the economic transfer pending completion of a subsequent legal transfer of the business. These assets and liabilities have been presented as held for sale. In accordance with the Group's accounting policy, collateral will be held against the reinsurance contract.

For further information, see note 6(ii).

As a consequence of the sale of the UK Legacy insurance liabilities, the Group's Adverse Development Cover reinsurance protection bought in 2014 to partly protect these liabilities is no longer required. The Group has therefore in February 2017 agreed to commute it for a one-time charge of £22m.

Appendices

Appendix A: Other accounting policies

Subsidiaries

Subsidiaries are entities over which the Group has control. The Group controls a subsidiary if the Group has all of the following:

- power over the subsidiary;
- exposure, or rights, to variable returns from its involvement with the subsidiary; and
- the ability to use its power over the subsidiary to affect its returns.

Subsidiaries are fully consolidated from the date on which control is entitled by the Group. They are deconsolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group.

The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of acquisition.

For business combinations completed on or after 1 January 2010 the cost of acquisition include the fair value of deferred and contingent consideration at the acquisition date and subsequent changes in the carrying value of the consideration are recognised in the consolidated income statement. For business combinations completed prior to 31 December 2009, the cost also includes costs directly attributable to the acquisition and the value of contingent consideration on settlement.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the consolidated income statement.

Changes in the ownership interests of a subsidiary between shareholders of the Group and shareholders holding a non-controlling interest are accounted for as transactions between equity holders of the Group. Any difference between the fair value of the consideration given by the transferee and the carrying value of the ownership interest transferred is recognised directly in equity.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated on consolidation. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries are aligned to ensure consistency with the policies adopted by the Group.

Investment in associates

Associates are entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost.

The Group's shares of its associates' profits or losses are recognised in the consolidated income statement and its share of comprehensive income is recognised in the consolidated statement of comprehensive income. The cumulative post acquisition movements are adjusted in the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Adjustments are made on consolidation, where necessary, to the accounting policies of associates to ensure consistency with the policies adopted by the Group.

Translation of foreign operations

The results and financial position of subsidiaries and associates whose functional currency is not Sterling are translated into Sterling as follows:

- Assets and liabilities for each statement of financial position presented are translated at closing exchange rates at the end of the period;
- Income and expenses for each income statement are translated at average exchange rates during each period;
- All resulting exchange differences are recognised in other comprehensive income and accumulated in the foreign currency translation reserve.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are recognised in other comprehensive income within the foreign currency translation reserve. Further information can be found in note 21. When a foreign entity is sold, the cumulative exchange differences relating to that foreign entity are recognised in the consolidated income statement as part of the gain or loss on sale.

Earnings per share

Basic earnings per share are calculated by dividing the profit attributable to the ordinary shareholders of the Parent Company by the weighted average number of Ordinary Shares in issue during the period, excluding Ordinary Shares purchased by various share trusts of the Group and held as own shares.

Diluted earnings per share is calculated by increasing the weighted average number of Ordinary Shares outstanding to assume conversion of all dilutive potential Ordinary Shares, notably those related to the employee share schemes.

Hedge Accounting

Transactions are classified as hedging transactions when the following conditions for hedge accounting are met:

- There is a formal designation and documentation of the hedging relationship and the Group's risk management objective and strategy for undertaking the hedge;
- The hedge is expected to be highly effective in achieving offsetting changes in fair value or cashflows attributable to the hedged risk, consistent with the originally documented risk management strategy for that particular hedging relationship;
- The effectiveness of the hedge can be reliably measured;
- The hedge is assessed on an ongoing basis and determined to have been highly effective.

Hedge of a net investment in a foreign operation

Where a foreign exchange derivative is designated as a hedging instrument against a net investment in foreign operations, the effective portion of the hedge is recognised in other comprehensive income; the gain or loss relating to the ineffective portion is recognised immediately in the consolidated income statement. At the point at which the net investment in the foreign operation is derecognised, the gains and losses accumulated in other comprehensive income are transferred to the consolidated income statement.

On designation of forward foreign exchange contracts the interest element is separated from the forward exchange rate and is excluded from the hedge relationship. Effectiveness of the hedge is then measured using the spot rate, which is also the exchange rate used when measuring the net investment in the designated subsidiaries.

For foreign exchange options the hedge designation is to hedge the value of the foreign operations at the strike price at the exercise date of the option.

Hedge of future cashflows

Where a derivative is designated as a hedging instrument against the cashflows from a fixed interest security, the gains and losses arising from the change in fair value of the derivative are recognised initially in other comprehensive income in the cashflow hedge reserve. This amount is adjusted to be the lesser of the cumulative gain or loss on the derivative and the cumulative change in fair value of the expected future cashflows of the security, both since the inception of the hedge.

The accumulated amount in the cashflow hedge reserve, is reclassified to the consolidated income statement in the period in which the hedged cashflows affect profit or loss.

Hedge of changes in fair value

Where a derivative is designated as a hedging instrument in a fair value hedge of the changes in value of a fixed interest security, the gains and losses arising from the change in fair value of the derivative are recognised in the consolidated income statement. The change in fair value of the hedged investments that are attributable to the hedged risk is transferred from the revaluation reserve to the consolidated income statement.

Property, Plant and Equipment

Property, plant and equipment is comprised of Group occupied land and buildings and other equipment (comprising of fixtures, fittings and other equipment including computer hardware and motor vehicles) and is initially recognised at cost.

Group occupied property is stated at fair value, less subsequent depreciation for buildings. The fair value methodology is set out note 26. Increases in the carrying amount arising on revaluation are recognised in other comprehensive income and credited to a separate revaluation reserve within equity. Decreases in the carrying amount arising on revaluation are recognised in other comprehensive income and reduce the revaluation reserve, to the extent they offset previous revaluation increases; further decreases are charged to the consolidated income statement. Buildings are depreciated to their residual value on a straight line basis over the useful economic life of the building; depreciation is charged to the consolidated income statement except where a building has been revalued upwards, in which case the amount of the depreciation relating to the difference between the buildings revalued amount and the original cost is transferred from revaluation reserve to retained earnings. Land is not depreciated.

Appendices – continued

All other plant and equipment is stated at cost less accumulated depreciation and accumulated impairment loss. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset only when it is probable that the expenditure will result directly in future economic benefits to the Group, and the cost can be measured reliably.

The estimated useful lives of property, plant and equipment is as follows:

| | |
|--------------------------|-------------------|
| Group occupied buildings | normally 30 years |
| Fixtures and fittings | 10 years |
| Equipment | 3 – 5 years |

The useful economic life and residual value are reviewed on an annual basis. Where the carrying value of an asset is deemed to be greater than its recoverable amount, the asset is impaired as outlined in the significant accounting policies note. Gains and losses on disposal are recognised based on the carrying amount of the asset. On disposal of buildings, any associated revaluation surplus is transferred to retained earnings.

Foreign currency transactions

Foreign currency transactions are translated into the functional currency of the Group's business operations using the exchange rates prevailing at the time of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement.

Investment property and rental income

Investment property is stated at fair value. The fair value methodology is set out in more detail in note 26. Unrealised gains and unrealised losses or changes are recognised in net investment return in the consolidated income statement. Rental income from operating leases on investment property is recognised in the consolidated income statement on a straight line basis over the length of the lease.

Policy acquisition costs

Policy acquisition costs incurred in acquiring insurance contracts include commissions and premium taxes directly related to the writing or renewal of insurance policies. These acquisition costs are deducted from unearned premiums and recognised in the consolidated income statement on the same basis as the unearned premiums.

Loan capital

Loan capital comprises subordinated bonds which are initially measured at the consideration received less transaction costs. Subsequently, loan capital is measured at amortised cost using the effective interest rate method.

Provisions

A provision is recognised when the Group has a present legal or constructive obligation as a result of past events that are more likely than not to result in an outflow of economic resources in order to settle the obligation, and the amount of that outflow can be reliably estimated.

Contingent liabilities

A contingent liability is recognised if the Group has a possible future obligation as a result of past events, and either the amount of the expected future outflow of economic resources or the likelihood of payment cannot be reliably estimated.

Termination benefits

Termination benefits are payable when either employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. Termination benefit expenses are recognised in the income statement at the earlier of the date when the Group can no longer withdraw the offer and the date when any related restructuring costs are recognised. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

Own shares

Own shares are deducted from equity. No gain or loss is recognised on the purchase, sale, issue or cancellation of shares. Any consideration paid or received is recognised directly in equity.

Other operating income

Other operating income is comprised principally of:

- Administration fee income: is received from policyholders in order for certain changes to their policy or policyholder details within their period of cover and is recognised in full on the date that the change is made;
- Premium policy instalment fee income: is received from policyholders as a finance charge on premiums paid in instalments and is recognised over the period that the instalments are made on a straight line basis;
- Introductory commission income is received from third parties for introducing business to them and is recognised when the introduction is made;
- Service income refers to income received for operating a settlement function primarily for the Group and its Global Network Partners.

Share based payments

The fair value of the employee share options and other equity settled share based payments is calculated at the grant date and recognised as an expense over the vesting period. The vesting of share awards is dependent on service and performance conditions, as well as market conditions. The assumption of the number of shares expected to vest is revised at the end of each reporting period, with the corresponding credit or charge recognised immediately in the income statement. Where an option is cancelled by an employee, the full value of the option (less any value previously recognised) is recognised at the cancellation date. The proceeds received by RSA upon exercise of share options, net of any transaction costs, are credited to share capital (nominal value) and share premium when the options are exercised, with a corresponding increase in equity.

Dilution levels for all schemes are held strictly within limits set by the Investment Association.

Further information on the share schemes the Group operates can be found in note 18 and in the Directors Remuneration Report.

Dividends

The final dividend is recognised as a liability when approved at the Annual General Meeting.

Operating lease commitments

The Group leases various properties and equipment under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights. Payments made under operating leases are charged on a straight line basis over the term of the lease.

Appendices – continued

Appendix B: Subsidiaries and associates

Unless otherwise stated, the share capital disclosed comprises ordinary shares (or equivalent) which are 100% held within the Group.

The proportion of voting power held equals the proportion ownership interest unless indicated.

| Country | Class of shares held | % held |
|---|----------------------|--------|
| Bahrain | | |
| Al foo, Building, office no. 21, 2nd floor, Building no. 662, Road no. 2811, Black no. 428, Al Seef, Manama, Kingdom of Bahrain | | |
| Royal & Sun Alliance Insurance (Middle East) BSC (c) | | 50 |

Brazil

Avenida Major Sylvio de Magalhães Padilha, 5200, America Business Park, Ed. Dallas, conj. 31, sala 02, Jardim Morumbi, Zip Code 05693-000, City of São Paulo, State of São Paulo, Brazil

Royal & Sun Alliance Insurance plc – Escritório de Representação no Brasil Ltda.

Canada

1 Place Ville Marie, Ste. 4000, Montreal QC H3B 4M4, Canada

| | | |
|------------------|----------------|--|
| Johnson, L. Inc. | Class A Common | |
| Johnson, L. Inc. | Class B Common | |

18 York Street, Suite 800, Toronto ON M5J 2T8, Canada

| | | |
|---|-------------------------------------|-------|
| 3342484 Canada Limited | | |
| 8301140 Canada Limited | | |
| 8301140 Canada Limited ⁽⁴⁾ | Preferred | |
| Ascentus Insurance Ltd. | | |
| Reilly & Wickens Brokers Ltd. ⁽³⁾ | Class A Voting Shares Unlimited | 9.99 |
| Reilly & Wickens Brokers Ltd. ^{(3) (4)} | Class B Non-Voting Shares Unlimited | 32.51 |
| Roins Financial Services Limited | | |
| Roins Financial Services Limited ⁽⁴⁾ | Preference | |
| Roins Holding Limited | | |
| Royal & Sun Alliance Insurance Company of Canada ⁽⁴⁾ | Class A Preferred | |

| Country | Class of shares held | % held |
|--|----------------------|--------|
| Royal & Sun Alliance Insurance Company of Canada | | 99.996 |
| RSA Travel Insurance Inc. | | |
| Western Assurance Company | | |

208-4940 No. 3 Road, Richmond BC V6X 3A5, Canada

| | | |
|---|-----------------------------|-------|
| Coast Underwriters Limited ⁽⁴⁾ | Class 1 Preferred Unlimited | |
| Coast Underwriters Limited ⁽⁴⁾ | Class 2 Preferred Unlimited | |
| Coast Underwriters Limited | Class A | 85.42 |
| Coast Underwriters Limited ⁽⁴⁾ | Class B1 | |
| MRM Solutions Limited ⁽⁶⁾ | Class A Common | |
| MRM Solutions Limited ^{(4) (6)} | Class B Common | |

555 West Hastings Street, Suite 1900, Vancouver BC V6B 4N6, Canada

Canadian Northern Shield Insurance Company

2475 Laurier Blvd., Quebec City, Québec G1T 1C4, Canada

Quebec Assurance Company

1800 – 401 West Georgia Street, Vancouver BC V6B 5A1, Canada

| | | |
|---|------------------|----|
| Shaw Sabey & Associates Ltd. ⁽³⁾ | Common Unlimited | 25 |
|---|------------------|----|

Fort William Building, 10 Factory Lane, St. John's Newfoundland A1C 6H5, Canada

| | | |
|--|-----------------|--|
| Johnson Inc. | Series A Common | |
| Johnson Inc. | Series B Common | |
| The Johnson Corporation | | |
| Unifund Assurance Company | | |
| Unifund Assurance Company ⁽⁴⁾ | Preferred | |
| Unifund Claims Inc. | | |

Denmark

Codanhus, Gammel Kongevej 60, DK-1790 Kobenhavn V, Denmark

Besigtelses Kontoret af 1914 A/S

Codan A/S

Codan Ejendomme II A/S

Codan Forsikring A/S

Forsikringselskabet Privatsikring A/S

| Country | Class of shares held | % held | Country | Class of shares held | % held |
|---|----------------------|--------|--|----------------------|--------|
| Guernsey | | | Isle of Man | | |
| Dixcart House, Sir William Place, St. Peter Port, Guernsey, GY1 4EY | | | 33-37 Athol Street, Douglas, IM1 1LB, Isle of Man | | |
| Insurance Corporation of the Channel Islands Limited | | | RSA Isle of Man No.1 Limited | | |
| Insurance Corporation Service Company Limited | | | Fort Anne, Douglas, IM1 5PD, Isle of Man | | |
| | | | RSA Manx Holdings Limited | | |
| India | | | Jubilee Buildings, 1 Victoria Street, Douglas, IM99 1BF, Isle of Man | | |
| Rider House, Plot No.136, Sector 44, Gurgaon, Haryana, 122002, India | | | Royal Insurance Service Company (Isle of Man) Limited | | |
| Royal & Sun Alliance IT Solutions (India) Private Limited | | | Tower Insurance Company Limited | | |
| First Floor, Building 10 C, Cyber City Complex, DLF Phase II, Gurgaon, Haryana, 122002, India | | | Jersey | | |
| RSA Actuarial Services (India) Private Limited | | | Elizabeth House, 9 Castle Street, St Helier, JE2 3RT, Jersey | | |
| | | | URICA Capital Limited ⁽³⁾ | Participating | 49.95 |
| Ireland | | | Luxembourg | | |
| RSA House, Dundrum Town Centre, Sandyford Road, Dublin 16, Ireland | | | 412F Route d'Esch, L 1030, Luxembourg | | |
| 123 Money Limited ⁽⁴⁾ | B1 Ordinary | | RSA Overseas Holdings (Luxembourg) (No 1) SARL | | |
| 123 Money Limited ⁽⁴⁾ | B2 Ordinary | | Netherlands | | |
| 123 Money Limited ⁽⁴⁾ | B3 Ordinary | | 20 Fenchurch Street, London, EC3M 3AU, United Kingdom | | |
| 123 Money Limited ⁽⁴⁾ | B4 Ordinary | | IDIP Direct Insurance B.V. | | |
| 123 Money Limited ⁽⁴⁾ | B5 Ordinary | | Intouch Insurance Group B.V. | | |
| 123 Money Limited ⁽⁴⁾ | C Ordinary | | Royal & SunAlliance Benelux Holdings N.V. | | |
| 123 Money Limited | | | RSA Overseas (Netherlands) B.V. | | |
| Benchmark Underwriting Limited | | | RSA Overseas Holdings B.V. | | |
| Europa General Underwriters Limited | | | Sun Alliance Finance B.V. | | |
| Royal & Sun Alliance (Ireland) Limited | | | Claude Debussylaan, 24, 1082MD, Amsterdam, Netherlands | | |
| RSA Insurance Ireland DAC | | | GDII – Global Direct Insurance Investments V.O.F. | Partnership Interest | |
| RSA Reinsurance Ireland Limited | | | Wilhelminalakeade 97-99, 3072 AP Rotterdam, Netherlands | | |
| Sertus Underwriting Limited | | | Royal Insurance Global B.V. | | |
| The Patriotic Limited | | | | | |
| 6th Floor, 2 Grand Canal Square, Dublin 2, Ireland | | | | | |
| EGI Holdings Limited | | | | | |
| RSA Overseas (No.3) Limited | | | | | |
| RSA Overseas Holdings (No 1) Unlimited Company | | | | | |
| RSA Overseas Holdings (No. 2) Unlimited Company | | | | | |

Appendices – continued

| Country | Class of shares held | % held | Country | Class of shares held | % held |
|--|----------------------|--------|---|----------------------|--------|
| Norway | | | 10 Buckingham Gate, London, SW1E 6LA, United Kingdom | | |
| Drammensveien 134, Oslo, 0277, Norway | | | Punchbowl Park Management Limited ^{(3) (5)} | | 65.09 |
| NIS Norway AS | | | | | |
| Oman | | | 30 Finsbury Square, London, EC2P 2YU, United Kingdom | | |
| PO Box 889, 100, Oman | | | British and Foreign Marine Insurance Company Limited | | |
| Al Ahlia Insurance Company SAOC ⁽⁷⁾ | | 70 | Liverpool Marine and General Insurance Company Limited | | |
| Russian Federation | | | London Guarantee & Reinsurance Company Limited | | |
| Sadovay Square, 3 Office 667, 121099, Moscow, Russia | | | Royal Insurance Operational Services (U.K.) Limited | Deferred Ordinary | |
| GDII – Rus L.L.C. | | | Royal Insurance Operational Services (U.K.) Limited | | |
| Saudi Arabia | | | RSA CRS (US) Limited | | |
| Office No.203, 2nd Floor, Home Centre Building, Tahlia Street, Suleymaniyah, Riyadh, Kingdom of Saudi Arabia | | | RSA Engineering Limited ⁽¹⁾ | | |
| Al Alamiya for Cooperative Insurance Company ⁽⁷⁾ | | 50.07 | Sun Alliance Insurance UK Limited | | |
| Singapore | | | Suinchan Holdings Limited ⁽¹⁾ | | |
| 8 Cross Street, #10–00, PWC Building, Singapore (048424) | | | The Northern Maritime Insurance Company Limited | | |
| Survey Association Pte. Ltd. | | | The Union Marine and General Insurance Company Limited | | |
| Sweden | | | 82 King Street, Manchester, England, M2 4WQ, United Kingdom | | |
| c/o Trygg-Hansa Försäkring Filial, 10626, Stockholm, Sweden | | | Counce O'Hara & Company Limited ⁽³⁾ | | 39 |
| NIS Sweden I AB | | | | | |
| Fleminggatan 18, S-106 26 Stockholm, Sweden | | | c/o UCL Business Plc, The Network Building 97, Tottenham Court Road, London, W1T 4TP, United Kingdom | | |
| Holmia Livförsäkring AB | | | Eurotempest Limited ⁽³⁾ | | 33.33 |
| Stortorget 11, S-702 11 Örebro, Sweden | | | Clinton House, 12 Lombard Street, Newark, Nottinghamshire, NG24 1XB, United Kingdom | | |
| CAB Group AB ⁽³⁾ | | 27.27 | Noble Marine (Insurance Brokers) Limited | | |
| United Kingdom | | | Noble Marine (Underwriting Agencies) Limited | | |
| 1 More London Place, London, SE1 2AF, United Kingdom | | | New London House, 6 London Street, London, EC3R 7LP, United Kingdom | | |
| Professional Indemnity Direct Limited | | | Polaris U.K. Limited ⁽³⁾ | | 25.38 |
| 5th Floor, United Kingdom House, 180 Oxford Street, London, W1D 1NN, United Kingdom | | | Fitzwilliam House, 10 St Mary Axe, London, EC3A 8EQ, United Kingdom | | |
| Centrium Management Company Limited ⁽³⁾ | | 31.45 | British Aviation Insurance Company Limited | | 57.10 |

| Country | Class of shares held | % held | Country | Class of shares held | % held |
|--|----------------------|--------|---|----------------------|--------|
| Hill House, 1 Little New Street, London, EC4A 3TR, United Kingdom | | | Royal International Insurance Holdings Limited | US\$1.00 Ordinary | |
| Coverselect Limited | | | Roysun Limited | | |
| Fyfe Group Limited | | | RSA Accident Repairs Limited | | |
| Liability Insurance Solutions Limited | | | RSA Claims Management Limited | | |
| Magian Underwriting Agency (1998) Limited | | | RSA E-Holdings Limited | | |
| Martello Professional Risks Limited | | | RSA Finance | | |
| Motor Trade Solutions Limited | | | RSA Law Limited | | 90 |
| Road Runner Motor Trade Limited | | | RSA Overseas Holdings (UK) Limited | | |
| Saturn Professional Risks Limited | | | Sal Pension Fund Limited ⁽¹⁾ | | 99.99 |
| Law Society House, 90-106 Victoria Street, Belfast, BT1 3GN, Northern Ireland | | | Sun Alliance and London Insurance plc | | |
| RSA Northern Ireland Insurance Limited | | | Sun Alliance Fund Management Limited ⁽¹⁾ | | |
| Level 8, 110 Queen Street, Glasgow, G1 3BX, United Kingdom | | | Sun Alliance Insurance International Limited | | |
| Century Insurance Company Limited | | | Sun Alliance Insurance Overseas Limited | | |
| St Mark's Court, Chart Way, Horsham, West Sussex, RH12 1XL, United Kingdom | | | Sun Alliance Management Services Limited | | |
| Acrecrest Limited | | | Sun Alliance Mortgage Company Limited ⁽¹⁾ | | |
| Alliance Assurance Company Limited | | | Sun Insurance Office Limited | | |
| Bradford Insurance Trustee Limited | | | The Globe Insurance Company Limited | | |
| Codan Finance Limited | | | The London Assurance | | |
| National Vulcan Engineering Insurance Group Limited | | | The Marine Insurance Company Limited | | |
| Non-Destructive Testers Limited | | | The Sea Insurance Company Limited | | |
| Oak Underwriting plc | | | The Westminster Fire Office Limited | | |
| R&SA Global Network Limited | | 64 | Westgate Properties Limited | | |
| R&SA Marketing Services plc | | | | | |
| Royal & Sun Alliance Insurance (Global) Limited | | | United States | | |
| Royal & Sun Alliance Insurance plc | Class A Ordinary | | Wall Street Plaza, 88 Pine Street, 31st Floor, New York, NY 10005, United States | | |
| Royal & Sun Alliance Insurance plc ⁽⁴⁾ | Class B Ordinary | | Royal & Sun Alliance Insurance Agency Inc. | | |
| Royal & Sun Alliance Pension Trustee Limited | | | | | |
| Royal & Sun Alliance Property Services Limited | | | | | |
| Royal & Sun Alliance Reinsurance Limited | | | | | |
| Royal Insurance (U.K.) Limited | | | | | |
| Royal Insurance Holdings Limited ⁽¹⁾ | | | | | |
| Royal International Insurance Holdings Limited | £1.00 Ordinary | | | | |

Notes:

1. Directly owned by the parent company RSA Insurance Group plc.
2. All of the subsidiaries listed are wholly owned within the Group and included in the consolidated accounts.
3. Indicates that the holding represents an Investment or is an Associate of the Group.
4. Indicates ownership of non-voting shares.
5. There is no subsidiary where the Group holds less than 50% of the voting rights and there are no entities where the Group holds more than 50% of the voting rights which are not subsidiaries unless indicated.
6. The percentage held relates to the actual percentage of the share capital held and not the effective percentage held (85.42%).
7. In relation to Al Ahlia Insurance Company SAOC, and Al Alamiya for Cooperative Insurance Company, the percentage held relates to the actual percentage of the share capital held and not the effective percentage held (which is 35.00% and 25.04% respectively).
8. No subsidiary holds a disclosable interest in the shares of RSA Insurance Group plc.

Financial Statements of the Parent Company

Parent Company Statement of Comprehensive Income

for the year ended 31 December 2016

| | 2016 £m | 2015 £m |
|--|--------------|--------------|
| Profit/(loss) for the year net of tax | 347 | (52) |
| Fair value gains/(losses) net of tax | 1,285 | (91) |
| Total comprehensive income/(expense) for the year | 1,632 | (143) |

The profit for the year net of tax includes a tax charge of **£6m** (2015: credit £8m). There is no tax relating to fair value gains.

Parent Company Statement of Changes in Equity

for the year ended 31 December 2016

| | Ordinary share capital £m | Ordinary share premium £m | Own shares £m | Preference shares £m | Revaluation reserves £m | Capital redemption reserve £m | Retained earnings £m | Total equity £m |
|--|------------------------------------|------------------------------------|------------------|----------------------------|-------------------------------|--|----------------------------|-----------------------|
| Balance at 1 January 2015 | 1,015 | 1,075 | – | 125 | 1,261 | 389 | 1,095 | 4,960 |
| Total comprehensive income for the year | | | | | | | | |
| Loss for the year net of tax | – | – | – | – | – | – | (52) | (52) |
| Fair value losses net of tax | – | – | – | – | (91) | – | – | (91) |
| | – | – | – | – | (91) | – | (52) | (143) |
| Dividends – paid (note 7) | – | – | – | – | – | – | (65) | (65) |
| Issued for cash (note 4) | 1 | 2 | – | – | – | – | – | 3 |
| Share based payments | 1 | – | – | – | – | – | 13 | 14 |
| Balance at 1 January 2016 | 1,017 | 1,077 | – | 125 | 1,170 | 389 | 991 | 4,769 |
| Total comprehensive income for the year | | | | | | | | |
| Profit for the year net of tax | – | – | – | – | – | – | 347 | 347 |
| Fair value gains net of tax | – | – | – | – | 1,285 | – | – | 1,285 |
| | – | – | – | – | 1,285 | – | 347 | 1,632 |
| Dividends – paid (note 7) | – | – | – | – | – | – | (131) | (131) |
| Purchase of own shares | – | – | (1) | – | – | – | – | (1) |
| Shares issued for cash (note 4) | 2 | 3 | – | – | – | – | – | 5 |
| Share based payments | 1 | – | – | – | – | – | 15 | 16 |
| Balance at 31 December 2016 | 1,020 | 1,080 | (1) | 125 | 2,455 | 389 | 1,222 | 6,290 |

The attached notes form an integral part of these separate financial statements.

Parent Company Statement of Financial Position

as at 31 December 2016

| | Notes | 2016 £m | 2015 £m |
|-------------------------------------|-------|--------------|--------------|
| Assets | | | |
| Intangible assets | | – | 1 |
| Investments | 2 | 5,386 | 4,317 |
| Amounts owed by subsidiaries | 8 | 2,210 | 2,356 |
| Current tax assets | 6 | 1 | 8 |
| Deferred tax assets | 6 | – | 8 |
| Other debtors and other assets | 3 | 1 | 68 |
| | | 2,212 | 2,440 |
| Cash and cash equivalents | | 3 | 4 |
| Total assets | | 7,601 | 6,762 |
| Equity and liabilities | | | |
| Equity | | | |
| Shareholders' equity | 4 | 6,290 | 4,769 |
| Total equity | | 6,290 | 4,769 |
| Liabilities | | | |
| Amounts owed to subsidiaries | 8 | 168 | 646 |
| Loan capital | 5 | 1,068 | 1,254 |
| Accruals and other liabilities | | 75 | 93 |
| Total liabilities | | 1,311 | 1,993 |
| Total equity and liabilities | | 7,601 | 6,762 |

The attached notes form an integral part of these separate financial statements.

The profit/(loss) for the year net of tax was **£347m** (2015: loss £52m).

The separate financial statements were approved on 22 February 2017 by the Board of Directors and are signed on its behalf by:



Scott Egan
Group Chief Financial Officer

Financial Statements of the Parent Company – continued

Parent Company Statement of Cashflows

for the year ended 31 December 2016

| | 2016 £m | Re-presented ¹ 2015 £m |
|--|--------------|---|
| Net profit/(loss) for the year before tax | 353 | (61) |
| Adjustments for non-cash movements in net profit/loss for year | 47 | 28 |
| Changes in operating assets/liabilities | 167 | 42 |
| Net cashflows from operating activities | 567 | 9 |
| Net movement in amounts owed by subsidiaries | (331) | 140 |
| Repayment of loan capital from subsidiaries | 239 | – |
| Net cashflows from investing activities | (92) | 140 |
| Proceeds from issue of share capital | 5 | 3 |
| Purchase of own shares | (1) | – |
| Dividends paid | (131) | (65) |
| Subordinated debt – repayments | (200) | – |
| Interest paid | (149) | (93) |
| Net cashflows from financing activities | (476) | (155) |
| Net decrease in cash and cash equivalents | (1) | (6) |
| Cash and cash equivalents at beginning of the year | 4 | 10 |
| Cash and cash equivalents at end of the year | 3 | 4 |

Note:

- Following a review of changes in operating assets/liabilities, specific balances have been further analysed and classified as adjustments for non-cash movements in net profit/loss for the year, net movement in amounts owed by subsidiaries and interest paid for 2015. These adjustments improve cashflow from other operating activities by £107m and reduce net cashflows from investing activities by £(14)m and net cashflows from financing activities by £(93)m.

The attached notes form an integral part of these separate financial statements.

Notes to the Parent Company Financial Statements

1) Significant accounting policies

RSA Insurance Group plc, ('the Company'), incorporated in England and Wales, is the ultimate Parent Company of the RSA group of companies. The principal activity of the Company is to hold investments in its subsidiaries and the receipt and payment of dividends.

These separate financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

Except where otherwise stated, all figures included in the separate financial statements are presented in millions of Pounds Sterling ('Sterling'), shown as £m, rounded to the nearest million.

In accordance with section 408 of Companies Act 2006, the Company's income statement and related notes have not been presented in these separate financial statements.

The accounting policies that are used in preparation of these separate financial statements are consistent with the accounting policies used in preparation of the consolidated financial statements of RSA Insurance Group plc as set out in those financial statements.

The additional accounting policies that are specific to the separate financial statements of the Company are set out below.

Investment in subsidiaries

The Company accounts for its investments in directly owned subsidiaries as available for sale financial assets, which are included in the accounts at fair value.

Changes in the fair value of the investments in subsidiaries are recognised directly in equity in the statement of comprehensive income. Where there is a decline in the fair value of a directly owned subsidiary below cost, and there is objective evidence that the investment is impaired, the cumulative loss that has been recognised in equity is removed from equity and recognised in the income statement.

Dividend income

Dividend income from investments in subsidiaries is recognised when the right to receive payment is established.

Adoption of new and revised standards

The Company will apply IFRS 9 'Financial Instruments' in its separate financial statements during the year ending 31 December 2018. In these financial statements, it will not be able to use the option permitted by the amendment to IFRS 4 'Insurance Contracts' to defer the adoption of IFRS 9 as the Parent Company's activities are not predominantly connected with insurance as defined in IFRS 4.

The main impact of the IFRS 9 is that the Company will recognise a loss allowance for expected credit losses on of amounts owed by subsidiaries, at their date of initial recognition and at each subsequent reporting date. If IFRS 9 had been adopted during 2016, there would not have been a significant impact on the Company's financial position or on its results for the year.

2) Investments

| | 2016 £m | 2015 £m |
|-----------------------------------|--------------|--------------|
| Investments at 1 January | 4,317 | 4,408 |
| Disposals during the year | (200) | – |
| Impairment during the year | (16) | – |
| Fair value adjustments | 1,285 | (91) |
| Investments at 31 December | 5,386 | 4,317 |

The balance at 31 December comprises:

| | 2016 £m | 2015 £m |
|----------------------------|--------------|--------------|
| Investment in subsidiaries | 4,970 | 3,663 |
| Loans to subsidiaries | 416 | 654 |
| | 5,386 | 4,317 |

The investments in subsidiaries are recognised in the statement of financial position at fair value measured in accordance with the Company's accounting policies. The Company's investments are classified as Level 2 financial assets. Fair value of the Company's significant subsidiary is determined by reference to the market value (derived from relevant indices) of the Company's Ordinary Shares and loan capital instruments at the end of the reporting period, being the most transparent independent available indicator. The market value is adjusted for the fair value of the Company's Preference Shares, assets and liabilities, excluding directly owned subsidiaries. The adjusting items have been fair valued by determining the present value of future cashflow projections, using an appropriate arm's length discount rate. The remaining subsidiaries are held at fair value which has been determined to be net asset value.

Notes to the Parent Company Financial Statements – continued

The subordinated loans to a subsidiary have the same terms as the external loan capital from which the loans to the subsidiary were financed. The fair values of these loans are based on the quoted prices for the external loan capital. The nominal values of the two loans are **£78m** (2015: £78m) and **£292m** (2015: £492m) with interest rates of 6.701% and 9.375% respectively.

The Directors believe that the methodology used supports the inclusion of the investments in subsidiaries in the statement of financial position, at the fair values ascribed to them. The market value of the Company's ordinary shares at 31 December 2016 was 5.86p. A movement of 1% in the share price would have an impact of £60m on the fair value.

Full details of the principal subsidiaries of the Company are set out in Appendix B to the consolidated financial statements.

3) Other debtors and other assets – to be settled within 12 months

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Other prepayments and accrued income | 1 | 68 |
| Total other debtors and other assets | 1 | 68 |

4) Share capital

Full details of the share capital of the Company are set out in note 32 to the consolidated financial statements.

5) Loan capital

Full details of the loan capital of the Company are set out in note 34 to the consolidated financial statements.

6) Current and deferred tax

| | Asset | | Liability | |
|--------------------------------|------------|------------|------------|------------|
| | 2016 £m | 2015 £m | 2016 £m | 2015 £m |
| To be settled within 12 months | 1 | 8 | – | – |

The current tax relating to items that are credited to equity is **£nil** (2015: £2m).

Deferred tax assets

Deferred tax for the current year is based on a rate of **17%** (2015: 18%). The following are the major deferred tax assets recognised by the Company and movements during the year:

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Other temporary differences | – | 1 |
| Accelerated capital allowances | – | 7 |
| Net deferred tax position at 31 December | – | 8 |

The movement in the net deferred tax assets recognised by the Company was as follows:

| | 2016 £m | 2015 £m |
|--|------------|------------|
| Net deferred tax position at 1 January | 8 | 9 |
| Amount charged to income statement | (7) | 1 |
| Amount charged to equity | – | (1) |
| Effect of change in tax rates – income statement | (1) | (1) |
| Net deferred tax position at 31 December | – | 8 |

No deferred tax has been recognised in respect of **£47m** (2015: £58m) of deferred tax reliefs due to the unpredictability of future profits streams.

Net deferred tax assets of **£nil** (2015: £8m), that relate to tax jurisdictions in which the Company has suffered a loss in either the current or preceding period, have been recognised on the basis that future taxable profits will be available against which these can be utilised. The evidence for the future taxable profits is a forecast consistent with the three year operational plans prepared by the relevant businesses, which are subject to internal review and challenge. Where relevant, the forecast includes extrapolations of the operational plans using assumptions consistent with those used in the plans.

7) Dividends paid and proposed

Full details of the dividends paid and proposed by the Company are set out in note 20 to the consolidated financial statements.

8) Related party transactions

The following transactions were carried out with related parties:

RSA Insurance Group plc provides services and benefits to its subsidiary companies operating within the UK and overseas as follows:

- Provision of technical support in relation to risk management, information technology and reinsurance services. Services are charged for annually on a cost plus basis, allowing for a margin of **5%** (2015: 5%);
- Issue of share options and share awards to employees of subsidiaries. Costs are charged for annually, based on the underlying value of the awards granted calculated in accordance with the guidance set out within IFRS 2.

The amounts charged in respect of these services to the Company's subsidiaries totalled **£80m** (2015: £67m).

Key management compensation

| | 2016 £m | 2015 £m |
|---|------------|------------|
| Salaries and other short-term employee benefits | 7 | 9 |
| Bonus awards | 5 | 5 |
| Pension benefits | 1 | 1 |
| Share based awards | 4 | 2 |
| Total | 17 | 17 |

Other transactions

Year-end balances with related parties are set out below:

| | 2016 £m | 2015 £m |
|---|--------------|--------------|
| Receivable from related parties: | | |
| Receivable from subsidiaries, interest bearing loans | 1,857 | 1,816 |
| Receivable from subsidiaries, non-interest bearing loan | 353 | 540 |
| Total receivable from related parties | 2,210 | 2,356 |
| Payable to related parties: | | |
| Payable to subsidiaries, interest bearing loans | 15 | 185 |
| Payable to subsidiaries, non-interest bearing loan | 153 | 461 |
| Total payable to related parties | 168 | 646 |

Interest is receivable on interest bearing loans to subsidiaries, which are repayable on 24 hours written notice. The rates of interest charged are at three months LIBOR plus margins ranging from 0.60% to 2.50%.

Interest is payable on interest bearing loans from subsidiaries, which are repayable on 24 hours written notice; **£15m** (2015: £15m) at three months LIBOR plus 200bps. In 2015, there was an additional £170m with interest payable at three months LIBOR plus 0.6%.

Interest received from subsidiaries is **£72m** (2015: £81m), and interest paid to subsidiaries is **£3m** (2015: £2m).

Royal & Sun Alliance Insurance plc (RSAI), a subsidiary of the Company, has provided guarantees to the Company's creditors for amounts arising from its loan capital agreements (as set out in note 34 to the consolidated financial statements) and for amounts arising from its committed credit facilities (as set out in note 35 to the consolidated financial statements). The guarantees relating to the loan capital agreements are subordinated to all other creditors of RSAI.

9) Share based payments

Full details of share based compensation plans are provided in note 18 to the consolidated financial statements.

10) Risk and capital management

The risks faced by the Company are derived from its investment in subsidiaries and are therefore the same as those of the RSA Group of companies. Details of the key risks to the Group and the steps taken to manage them are disclosed in the Risk Management section of the consolidated financial statements.

Other information

Shareholder information

Registered office and group corporate centre

20 Fenchurch Street, London EC3M 3AU. Telephone: +44(0) 20 7111 7000.

Registered in England and Wales No. 2339826.

Group website

The Company's corporate website provides shareholders with a broad range of information about the Group's heritage, social and environmental responsibilities and investor information such as the Group's financial statements, current and historic share prices, Annual General Meeting (AGM) materials, events, governance information and answers to frequently asked questions in respect of shareholder matters. Visit the investor website at www.rsagroup.com/investorrelations for further information.

Registrar

The Company's share register is maintained by Equiniti Limited. Any administrative enquiries relating to shareholdings, such as dividend payment instructions or a change of address, should be notified to Equiniti at the following address:

Equiniti Limited

Aspect House
Spencer Road
Lancing
West Sussex
BN99 6DA

Telephone: 0371 384 2048

When contacting Equiniti, please quote your shareholder reference number which can be found on your share certificate or dividend tax voucher. Telephone lines are open 8.30am to 5.30pm (UK time), Monday to Friday, excluding English public holidays. Overseas callers should use +44(0) 121 415 7064. Shareholders with a text phone facility should use +44(0) 371 384 2255 or alternatively use the Text Relay service by dialling 18001 0121 415 7064 directly from the text phone. To securely email Equiniti with an enquiry visit www.help.shareview.co.uk.

Annual General Meeting

Holders of the Company's Ordinary Shares are invited to attend the Company's 2017 AGM, which will be held at 200 Aldersgate, St Paul's, London EC1A 4HD at 11.00am on Friday 5 May 2017.

Managing your Shareholding

Information on how to manage your shareholding can be found at www.help.shareview.co.uk. If you do not find the information you require, you can send your enquiry via secure email from these pages. You will be asked to complete a form providing your name, address and shareholder reference number. If you require an email response, you will need to provide your email address.

Amalgamation of accounts

Shareholders who receive duplicate sets of Company mailings owing to multiple accounts in their name may contact Equiniti to request that their accounts be amalgamated.

Electronic communications

Receiving the Company's communications electronically allows the Company to communicate with its shareholders in a more environmentally friendly, cost effective and timely manner.

You can elect to receive email notification of shareholder communications by registering at www.shareview.co.uk where you can also set up a bank mandate to receive dividends directly to your bank account and submit proxy votes for shareholder meetings. Shareholders may elect to receive a printed copy of the Annual Report and Accounts at any time by contacting Equiniti.

Additionally, if you wish to register for the Company's investor news service to receive the latest news and press releases by email, visit www.rsagroup.com/investornewsalert.

Dividends

Shareholders are encouraged to have their dividends paid directly into their bank account. It is a more secure and faster way to receive the dividend payment with cleared funds available to shareholders on the dividend payment date. Shareholders who have their dividends paid directly into their bank account, receive a consolidated tax voucher once a year, showing payments received in the respective tax year. Alternatively, individual tax vouchers are available upon request. To take advantage of this convenient method of payment visit www.shareview.co.uk or contact Equiniti. Details of 2017 dividend dates can be found at www.rsagroup.com/investors/calendar/dividends.

Scrip Dividend Scheme

The Company renewed its authority to offer a Scrip Dividend Scheme to shareholders at the 2014 AGM.

The Company will not be offering a Scrip Dividend alternative in respect of the final 2016 Ordinary dividend.

In 2016, the Terms and Conditions of the Scheme were amended to make it clearer that a scrip dividend will not be available in the event that a cash dividend is not paid (including where it is cancelled or deferred by the Board). The revised Terms and Conditions of the Scheme are available on the shareholder services area of the Company's website or from Equiniti. Shareholders with a scrip dividend mandate in place need take no further action as your mandate remains effective until notified to the Registrar in writing.

For dividends where a Scrip alternative is offered, shareholders wishing to receive a Scrip dividend instead of a cash dividend should contact Equiniti for details or visit the shareholder services area of the Company's website www.rsagroup.com/investors/ shareholders.

American Depositary Receipts

The Company operates a sponsored American Depositary Receipts ('ADR') programme which is managed by JPMorgan Chase NA. The programme allows shareholders to invest in the Company through US dollar denominated funds. Any enquiry relating to the sponsored ADR programme should be addressed to:

JPMorgan Chase & Co
PO Box 64504
St Paul
MN 55164-0854 USA

or alternatively visit adr.com/shareholder and select Contact Us.

Low cost share dealing facilities

Shareholders may purchase or sell their RSA Ordinary Shares through their stockbroker, a high street bank or one of the providers detailed below:

Equiniti offer a telephone and internet dealing service. Commission is currently 1.5 percent on amounts up to £50,000 and 0.25 percent on the excess thereafter, with a minimum charge of £60 for telephone dealing and £45 for internet dealing. For telephone sales, call +44(0) 345 6037 037. Lines are open 8.30am to 5.30pm (UK time), Monday to Friday, excluding English public holidays. For internet sales log on to www.shareview.co.uk/dealing. Please quote your shareholder reference number.

Stocktrade also offer a telephone dealing service. Commission is currently 1 percent which is subject to a minimum charge of £25. For telephone sales call +44(0) 131 240 0414 between 8.00am and 4.30pm, Monday to Friday. Please quote reference: 'RSA Group dial and deal service'.

Alternatively visit their website, www.stocktrade.co.uk.

Please note that rates quoted are as at February 2017 and may be subject to change. Please contact either provider for further guidance on their full terms and conditions.

Share register fraud: protecting your investment

UK law requires that our shareholder register is available for public inspection. We are unable to control the use of information obtained by persons inspecting the register. Details of any share dealing facilities that the Company endorses will be included in Company mailings or on our website.

Shareholders are advised to be wary of any unsolicited advice, offers to buy shares at a discount, or offers of free reports about the Company. If you receive any unsolicited advice, make sure you get the correct name of the person and organisation and check that they are appropriately authorised by the FCA by visiting www.scamsmart.fca.org.uk. More information on protecting your investment can be found at www.scamsmart.fca.org.uk. If you do receive a fraudulent approach, please advise the FCA using the share fraud reporting form at www.fca.org.uk/scams or call the FCA Consumer Helpline on 0800 111 6768.

Tips on protecting your shares

- Keep any documentation that contains your shareholder reference number in a safe place and destroy any documentation you no longer require by shredding it.
- Inform Equiniti promptly when you change your address.
- Be aware of dividend payment dates and contact Equiniti if you do not receive your dividend cheque, or better still, make arrangements to have the dividend paid directly into your bank account.
- Consider holding your shares electronically in a CREST account via a nominee account.

Sharegift

Shareholders with a small number of shares, the value of which makes it uneconomic to sell them, may wish to consider donating them to charity through ShareGift, a registered charity administered by The Orr Mackintosh Foundation, registered charity number 1052686. The relevant share transfer form can be obtained from Equiniti. Further details can be obtained from www.sharegift.org or by calling +44(0) 20 7930 3737.

Other information

Jargon buster

Below is a simple explanation of some of the key technical terms used within this report.

| Term | Definition |
|--|---|
| Affinity | · Selling insurance through a partner's distribution network, usually to a group of similar customers, e.g. store-card holders, alumni groups, unions and utility company customers. |
| Attritional loss ratio | · Claims incurred during the period expressed as a percentage of earned premiums, including claims handling expenses but excluding claims incurred in respect of large losses, weather events and subsidence losses. |
| Capital | · The money invested in the Group. This includes the money invested by shareholders and profits retained within the Group. |
| Claims Frequency | · Average number of claims per policy over the year. |
| Claims Handling Expenses | · The administrative cost of processing a claim (salary costs, costs of running claims centres, etc. and allocated share of the costs of head office units). Not the cost of the claim itself. |
| Claims Ratio (Loss Ratio) | · Percentage of Net Earned Premiums which is paid out in claims and Claims Handling expenses. |
| Claims Reserve (Provision for Losses and Loss Adjustment Expenses) | · Reserve established by the Group to reflect the estimated cost of claims payments and claims handling expenses that we estimate we will ultimately be required to pay in respect of insurance cover we have provided up until the reporting date. |
| Claims Severity | · Average cost of claims incurred over the period. |
| Combined Operating Ratio (COR) | · The sum of the Claims Ratio, Expense Ratio and Commission Ratio. · Measures how much we pay out in claims and expenses for each unit of net premium earned. · A COR of less than 100 percent indicates that we are writing profitable business. · Calculated as: $\frac{\text{Net Incurred Claims} + \text{Expenses} + \text{Commissions}}{\text{Net Earned Premiums}} \%$ |
| Commission | · An amount paid to an intermediary such as a broker for generating business. |
| Commission Ratio | · Ratio of net commission costs to Net Earned Premiums. |
| Current Year Result | · The underwriting profit or loss earned from business for which protection has been provided in the current financial period. |
| Expense Ratio | · Percentage of Net Earned Premiums which is paid out in operating expenses, e.g. salaries, premises costs, etc. The ratio does not include claims related or investment expenses but can include or exclude commissions. |
| Exposure | · A measurement of risk we are exposed to through the premiums we have written. For example, in motor insurance one vehicle insured for one year is one unit of exposure. |
| Financial Conduct Authority (FCA) | · The regulatory authority with responsibility for the conduct of the UK financial services industry. |
| Gross Written Premium (GWP) | · Total premium written or processed in the period, irrespective of whether it has been paid. |
| IBNR (Incurred but Not Reported) | · A reserve for accidents or incidents (which we have provided cover for) that have occurred but which have not yet been reported to us. |
| Large losses | · Single claims or events with a net cost of £500k or higher. |
| Net Earned Premium (NEP) | · The proportion of premium written, net of the cost of associated reinsurance, that represents what we have charged to provide insurance cover during the period. |

| Term | Definition |
|--|---|
| Net Incurred Claims (NIC) | · The total claims cost incurred in the period less any share to be paid by reinsurers. It includes both claims payments and movements in claims reserves, as well as claims handling expenses in the period. |
| Net Written Premium (NWP) | · Premium written or processed in the period, irrespective of whether it has been paid, less the amount due to reinsurance. |
| Prior Year Result | · Profit or loss generated by changing the estimate for claims incurred in a previous year to a better or worse level than the previous estimated cost. |
| Property and Casualty (P&C) (Non-Life Insurance or General Insurance) | · Property insurance covers loss or damage through fire, theft, floods, storms and other specified risks. Casualty insurance primarily covers losses arising from accidents that cause injury to other people or damage to the property of others. |
| Prudential Regulation Authority (PRA) | · The regulatory authority with responsibility for the prudential regulation and supervision of the UK financial services industry. |
| Rate | · The price of a unit of insurance based on a standard risk for one year. Actual premium charged to the policyholder may differ from the rate due to individual risk characteristics and marketing discounts. |
| Reinsurance | · The practice whereby we transfer part or all of the risk we have accepted to another insurer (the reinsurer). |
| Solvency II | · New capital adequacy regime for the European insurance industry which commenced in 2016. Establishes a revised set of EU wide capital requirements and risk management standards. |
| Scrip Dividend | · Where shareholders choose to receive the dividend in the form of additional shares rather than cash. The Group would issue new shares to meet the scrip demand. |
| Tangible Net Asset Value (TNAV) | · The tangible value of the Group calculated by subtracting our total liabilities including loan capital from our total tangible assets (total assets less goodwill and intangibles). |
| Total Shareholder Return | · A measure of performance based on the overall value to shareholders of their investment in the Group over a period of time. Includes the movement in the share price and dividends paid, expressed as a percentage of the share price at the beginning of the period. |
| Underlying Return on Tangible Equity | · A measure of the underlying profits the Group earns, adjusted for profit/loss on disposal of subsidiaries, reorganisation and integration costs and business acquisition costs, relative to opening tangible funds attributable to ordinary shareholders. |
| Underwriting Result | · This is a measure of how well the Group has done excluding its investment performance and is calculated as: NEP – Net Incurred Claims (including Claims Handling Expenses) – Expenses – Commissions |
| Unearned Premium | · The portion of a premium that relates to future periods, for which protection has not yet been provided, irrespective of whether the premium has been paid or not. |
| Weather losses | · Weather events with a net cost of £500k or higher. |
| Yield | · Rate of return on an investment in percentage terms. · The dividend payable on a share expressed as a percentage of the market price. |

Other information

Alternative performance measures

Underlying and alternative performance measures

The Group uses alternative performance measures, including certain underlying measures, to help explain business performance and financial position. Where not defined in the body of this report, further information is set out below.

Note 8 on pages 132 to 134 of the condensed consolidated financial statements presents a reconciliation of the Management basis to Statutory income statement.

Underlying premiums

Underlying growth rate in Scandinavia has been calculated by adjusting Scandinavian 2015 premiums downwards by £26m for the non-repeat of two large multi-year deals and also by £33m for the transfer of Marine business from Scandinavia to the UK in FY 2016.

Combined operating ratio

The Group's combined operating ratio (COR) is calculated on an 'earned' basis as follows:

$\text{COR} = \text{loss ratio} + \text{commission ratio} + \text{expense ratio}$

Where:

$\text{Loss ratio} = \text{net incurred claims} / \text{net earned premiums}$

$\text{Commission ratio} = \text{commissions} / \text{net earned premiums}$

$\text{Expense ratio} = \text{operating expenses} / \text{net earned premiums}$

Underlying profit before tax

Underlying profit before tax is calculated as operating profit less interest costs.

Underlying Core Group tax rate

The underlying Core Group tax rate mainly comprises the local statutory tax rates in our territories applied to underlying regional profits (operating profits less interest costs).

Net asset value and tangible net asset value per share

Net asset value per share data at 31 December 2016 was based on total shareholders' funds of £3,715m, adjusted by £125m for Preference Shares. Tangible net asset value per share was based on a tangible book value of £2,862m (equal to shareholders' funds of £3,715m, less goodwill & intangible assets of £728m, less £125m preference share capital).

Earnings per share

The earnings per share (EPS) is calculated using the result attributable to the ordinary shareholders of the Parent Company and the weighted average number of shares in issue during the period. On a basic and diluted basis these were 1,018,174k and 1,024,449k respectively (net of RSA owned shares). The number of shares in issue at 31 December 2016 was 1,019,555k (net of RSA owned shares).

Stated EPS uses profit attributable to ordinary shareholders (profit after tax less non-controlling interests and preference share dividends). Underlying EPS uses an underlying profit measure calculated as operating profit less interest costs taxed at an underlying tax rate of 24% for FY 2016, less non-controlling interests and preference share dividends.

Constant exchange (CFX)

Prior period comparative translated at current period exchange rates.

Controllable costs

Total controllable costs are stated on a 'written' basis, and include underwriting operating expenses, claims expenses, investment expenses, central expenses, and Solvency II costs.

Current year underwriting result

The profit or loss earned from business for which protection has been provided in the current financial period.

Prior year underwriting result

The profit or loss arising from settling claims incurred in previous years at a better or worse level than the previous estimated costs.

'Record' underwriting performance

Record FY Group underwriting profit and combined ratio considers the FY periods for 2006–2016. In order to compare on a 'like-for-like' basis, historical periods have been adjusted for central expense reallocation changes made in 2015, Scandinavian discount rate changes made in 2014, and IAS 19 pension net interest cost changes made in 2012. In the case of the expense reallocations and IAS 19 changes, the restatement value applied in the year of change has been applied to all preceding years back to 2006.

Return on equity and tangible equity

| | | FY 2016 £m | FY 2015 £m |
|------------|--|-------------------|---------------|
| | Profit after tax | 20 | 244 |
| | Less: non-controlling interest | 7 | (9) |
| | Less: preference dividend | (9) | (9) |
| A | Profit attributable to ordinary shareholders | 18 | 226 |
| | Operating profit before tax | 655 | 523 |
| | Less: interest costs | (99) | (106) |
| | Underlying profit before tax | 556 | 417 |
| | Less: tax ¹ | (133) | (117) |
| | Less: non-controlling interest | (12) ² | (9) |
| | Less: preference dividend | (9) | (9) |
| B | Underlying profit after tax attributable to ordinary shareholders | 402 | 282 |
| | Opening shareholders' funds | 3,642 | 3,825 |
| | Less: preference share capital | (125) | (125) |
| C | Opening ordinary shareholders' funds | 3,517 | 3,700 |
| | Less: goodwill & intangibles | (679) | (800) |
| D | Opening tangible ordinary shareholders' funds | 2,838 | 2,900 |
| | Return on equity | | |
| A/C | Reported | 0.5% | 6.1% |
| B/C | Underlying | 11.4% | 7.6% |
| | Return on tangible equity | | |
| A/D | Reported | 0.6% | 7.8% |
| B/D | Underlying | 14.2% | 9.7% |

Notes:

1. Using underlying assumed tax rate of 24% in FY 2016 and 28% in FY 2015
2. Stated non-controlling interest adjusted for share of goodwill write down in Oman

Notes

Notes



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