Soteria Finance Holdings Limited
Annual report and accounts 2020

Principal Activities and Business Updates

Soteria Finance Holdings Limited ('SFHL' and the 'Company') is a holding company. SFHL was incorporated on 28 May 2020. The principal activity of the Company is as a holding company of Soteria Insurance Limited ('SIL' and together the 'Group'), a UK-based General Insurer.

On 2 December 2020, the Company purchased SIL following approval by the Prudential Regulation Authority (PRA). At the same date, SIL entered into an outsourcing agreement with the Markerstudy Group to provide insurance services to SIL.

On 11 February 2021, the SIL Board, as part of the Group's strategy, made the decision to place SIL into run-off and subsequently made an application to the PRA for SIL's regulatory permissions to effect new insurance contracts to be cancelled. This application was approved on 29 March 2021. SIL's last new insurance policy was entered into with effect from 24 February 2021.

Financial Position & Performance

The financial position of the Group and the Company at 31 December 2020 is shown in the Statement of Financial Position on pages 15 and 16 with the trading results shown in the Income Statement on page 13. A summary of the trading result for the Group, which represents the results of SFHL from incorporation and the results of SIL from acquisition, is shown below.

Highlights

	2020 £m
Net earned premiums	20.7
Net policyholder claims and benefits incurred	(15.5)
Investment return	1.5
Commission and expenses	(11.5)
Other income	3.5
Finance costs	(1.0)
Loss before gain on bargain purchase	(2.3)
Gain on bargain purchase	146.5
Profit before taxation	144.2

The 2020 financial result for the period was a profit before taxation of £144.2m. The reported loss before the gain on bargain purchase was £2.3m.

The gain on bargain purchase represents the difference between the amount SFHL paid for SIL and the fair value of net assets acquired. In part, the discounted purchase price relative to net asset value reflects the additional costs that will be incurred by SIL in effecting an orderly run-off.

Commission and expenses includes £1.0m of administrative expenses incurred by SFHL, predominantly relating to costs incurred due to the acquisition of SIL.

Capital

The Group has monitored available capital on a Solvency II basis since the purchase of SIL on 2 December 2020, with a Standard Formula Solvency Capital Requirement (SCR) coverage at 31 December 2020 of 125%. Owing to the decision made by the SIL Board in February 2021 to cease writing insurance business, this SCR coverage ratio has been determined on a run-off basis. Had this decision not been made and the SCR coverage ratio had been determined on the basis that SIL was to continue to underwrite insurance business it is estimated that the SCR coverage as at 31 December 2020 would have been 138%.

The Group funds its business through share capital and reserves attributable to equity holders and through the issue of subordinated loans to equity holders. On incorporation SFHL issued 1 ordinary share of £0.01 at par. Subsequently the Company issued a further 9,999,999 ordinary shares of £0.01 each for a total consideration of £37m.

On 2 December 2020 the Group entered into an agreement with Soteria AOF Solutions Limited (SAOFS) to provide SIL access on request to funding of £25m, which was approved by the PRA to be treated as Tier 2 Ancillary Own Funds. SAOFS is a company related to SFHL through having the same shareholders. SIL did not draw upon this funding in the period.

On 2nd December 2020, the Group issued £12m of a subordinated perpetual loan charged at 17.5% interest per annum to GSO Capital Opportunities Fund III (Luxembourg) S.à r.l. (GSO) (£11m) and TF Special Opportunities – Frisco Limited (TF) (£1m). GSO and TF are companies related to SFHL through being investors in the Company. This subordinated loan is classified as Tier 1 Restricted capital within Solvency II Own Funds.

On 2nd December 2020, the Group issued £60m of a subordinated term loan due in 2030 at par, charged at 16.875% interest per annum to GSO (£56m) and TF (£4m). This subordinated loan is classified as Tier 2 capital within Solvency II Own Funds.

Business Strategy and Objectives

As disclosed above, SFHL's only subsidiary, SIL, has ceased to write insurance business. No insurance business has been written since February 2021. SIL will continue to administer existing policies in force and settle outstanding claims. The focus of the Directors is to ensure that SIL meets all obligations to customers throughout a solvent run-off, to fulfil all regulatory requirements and, to the extent the Group has surplus capital above a prudent risk appetite to meet its liabilities and regulatory requirements, it aims to distribute this capital to its owners. The Group has a Solvency Capital Requirement (SCR) coverage at 31 December 2020, calculated on a run-off basis, of 125% and projections show headroom with the ability to continue to meet regulatory requirements and risk appetite over the going concern assessment period.

The Group has not been significantly impacted by Brexit and is not expected to be in 2021. The Group is predominantly a UK business, however it does have exposure to financial markets and is exposed to potential supply chain issues as imported goods and services are used by suppliers in order to fulfil insurance claims, including from the European Union (EU). There remains the risk that costs could increase due to the impact to the supply chain and increased administrative requirements for customers travelling to the EU.

The Civil Liability Act received Royal Assent in December 2018. This Act and associated changes are expected to reduce the cost of whiplash claims arising from road accidents, but the planned implementation date has been deferred until May 2021 in light of delays caused by the Covid-19 pandemic.

Coronavirus (Covid-19) impact

The coronavirus (Covid-19) pandemic has caused challenges and uncertainty across the insurance industry and is likely to continue to do so in 2021. The Group itself has not been significantly affected, having only begun trading on 2 December 2020, and has benefitted from the strengthening of business continuity arrangements by SIL, to enable greater numbers of colleagues to work from home, prior to purchase.

Financially, the primary impact of the pandemic on SIL has been to reduce loss ratios owing to there being fewer cars on the road during lockdown, leading to fewer accidents and fewer claims, only partially countered by upward pressure on average costs for some claim types. The pandemic also caused increased volatility in the investment markets, however the Group has been relatively protected owing to a conservative approach to investment, holding predominantly cash and highly-rated government and corporate bonds, which fluctuated in value less than other asset classes.

In 2021, the Group is well prepared both operationally and financially for the impact of the pandemic. The Group remains vigilant to changing customer behaviour giving rise to different patterns of insurance claims or policy cancellations, and to claims supply chain disruption affecting the cost or service level to handle claims. Any increased costs of claims or administrative expenses are expected to be relatively modest in the context of the Group's financial resources and will be monitored through the usual governance mechanisms, including the Board's regular oversight of solvency capital coverage and other strategic monitoring triggers. Investments will continue to be monitored through the usual governance mechanisms.

Business Environment - Market Background

The UK general insurance market remains highly competitive and price driven with multiple insurance providers. This competitive environment led to a reduction in average motor premiums of 1% year on year, which is the lowest level since 2016 (Q4 2020 ABI Premium Tracker Report). Just as the Group is doing, the industry as a whole supported motorists throughout the pandemic, continuing to honour policies despite inevitable changes in people's circumstances. This included financial support to pay via instalments.

In the Home market, premiums for individual buildings, contents insurance, and combined policies continued to increase, having risen steadily over the last few years.

Investment yields continue at historically low levels, being particularly adversely impacted by the global pandemic. Despite this, the Group's investments have performed well, due in part to investments in collective investment assets.

Business Environment - Regulatory Background

At the end of 2019, the PRA and FCA issued a number of consultation papers outlining their proposed approach to firms' operational resilience and outsourcing/third party risk management. The expectation at the time was that consultation would take place by April 2020 with proposed implementation of the various requirements ranging from December 2020 and the second half of 2021. However all of this was subsequently pushed back as a result of Covid -19 with implementations going out until 2021. The Group is supportive of the approach to prioritise operational resilience and will continue to comply with all requests and requirements, and in particular to maintain robust governance over the business activities that have been outsourced.

In September 2020 the FCA published its final report of its market study into the pricing of Motor and Home insurance. The FCA is proposing major reform to these markets. These reforms should not materially impact the Group owing to the decision taken to stop writing Motor and Home business.

Key Performance Indicators

The business strategy for the Group measures success in the following key areas: financial and trading; customer and capital adequacy & risk. This 'balanced scorecard' approach helps ensure focus on the implications to areas identified as being key in progressing towards the Group's strategic vision.

Indicator	**2020**
Financial and trading *Financial and trading measures focus on profitability*	
Net assets This shows the value of net assets held by the group	£182.4m
Loss before gain on bargain purchase This shows the level of loss before tax (excluding goodwill on acquisition)	£(2.3)m
Customer *Customer measures report on customer contacts throughout the customer journey*	
Net Promoter Score (NPS) A cross industry standard metric to track promoters and detractors, producing a clear measure of an organisation's performance through its customers' eyes (An NPS above zero is regarded as good, above 50 is excellent)	**36.5**
Capital adequacy & risk *Risk measures focus on capital adequacy and risk appetite*	
Risk appetite For each principal risk, the SFHL and SIL Boards have approved risk appetite statements with underpinning metrics	Risk appetite metrics have approved limits within which business operations are to be conducted, along with thresholds to give early warning of emerging issues
Capital buffer There are a number of different methodologies for calculating the minimum level of capital that the Group must maintain. At any one time, the Group must ensure it has sufficient capital to meet the most onerous of these requirements. The principal externally imposed capital requirement is the SCR under Solvency II, which is assessed quarterly. The SCR at 31 December 2020 has been calculated on a run-off basis.	125%

Non-Financial Information Statement

Under sections 414CA and 414CB of the Companies Act 2006 the Group is required to include in the strategic report a non-financial information statement. Disclosures are shown in the table below:

Reporting requirement	Disclosure	Page
Environmental matters	See 'Corporate responsibility and the environment' within the Directors' Report	7
Employees	See 'Employees and employment of people with disability' within the Directors' Report	7
Social matters	See 'Section 172(1) statement & stakeholder Engagement' below	5-6
Respect for Human Rights	The Group had policies which take into account its view of the importance of human rights, including in regard to its investment portfolio. See 'Corporate responsibility and the environment' within the Directors' Report	7
Anti-Bribery and Anti-corruption	The Group has financial crime risk policies in place and seeks to ensure that controls are put in place to prevent such activity	n/a
Business Model	See 'Business strategy and objectives' earlier within this report	3
Principal Risks	See 'Principal risks and uncertainties' within this report	5
Non-Financial KPI's	See 'Key Performance Indicators' within this report and Streamlined Energy and Carbon Reporting in the Directors' Report. See 'Corporate responsibility and the environment' within the Directors' Report.	4 and 7

Principal Risks and Uncertainties

The following are considered to be the principal risks facing the Group:

Risk Type	Definition	Page
Strategic and business risk	The risk of not meeting strategic and business objectives caused by poor or sub-optimal strategy implementation, deployment of resources, decision making, strategic change programmes, economic, regulatory or other environmental factors resulting in lost earnings and capital	49
Conduct risk	The risk that the Company's (or its subsidiary's) processes, behaviours, offerings or interactions will result in unfair outcomes for customers and a damage to reputation.	49
Regulatory risk	The risk of regulatory sanctions, regulatory censure, material financial loss, or loss to reputation the Group may suffer as a result of failure to comply with regulations, rules, related self-regulatory organisation standards and codes of conduct applicable to its activities	49
Insurance (Premium) risk	The inherent uncertainties as to the occurrence, amount and timing of insurance liabilities or unearned exposure	49-50
Insurance (Reserving) risk	The risk of loss, or of adverse change in the value of insurance liabilities, resulting from fluctuations in the timing, frequency and severity of insured events for earned policies, and in the timing and amount of claim settlements	50
Market risk	The risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers including interest rates, market prices of assets and liabilities	50-52
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events	52
Liquidity risk	The current and prospective risk to earnings or solvency arising from the Group's inability to meet its obligations when they come due without incurring unacceptable losses	52-53
Credit risk	The risk to earnings and capital arising from a debtor's failure to meet their legal and contractual obligations	54

A detailed description of each risk type can be found on pages 49 to 54.

For each of the principal risks the SFHL and SIL Boards have approved risk appetite statements, risk policies and control standards with underpinning metrics. The metrics have approved limits within which business operations are to be conducted, along with thresholds to give early warning of emerging issues.

The ongoing impacts of the Covid-19 pandemic are currently a source of risk and uncertainty for the Group. The main effects of the pandemic would be expected to impact Insurance (Premium) Risk (positive impact due to terms of reduced claims as a result of lockdown) and Market Risk (increased volatility). Operational Risks associated with Covid-19 have been largely managed and all staff are currently able to work from home with no major impact. The Board is aware of the potential impact of remote working on the mental health of the Group's employees and management are in regular contact with all colleagues in order that any issues or concerns can be identified and addressed.

Section 172(1) Statement & Stakeholder Engagement

The Board of SFHL considers that it has, in good faith, acted in a way that it considers would be most likely to promote the success of the Group for the benefit of its members as a whole, and, in doing so, has had regard to and recognised the importance of considering all stakeholders and other matters (as set out in s.172 (1) (a-f) of the Act) when making decisions.

Overview
Good corporate governance underpins how we conduct ourselves as a Board; our culture, values, behaviours and how we do business. As a Board, we are conscious of the impacts that our business and decisions have on our direct stakeholders as well as our wider societal impact.

The Board of SFHL is aware of its duties under the Companies Act, including the matters set out in s. 172. It has approved terms of reference for matters delegated to its committees and reviews these periodically to ensure they accord with best practice.

For any principal decisions approved by the Board, a discussion takes place around impact on our key stakeholders, including our colleagues and our customers. The relevance of each stakeholder group may vary by reference to the issue in question, so the Board seeks to understand the needs of each stakeholder group and any potential conflicts as part of its decision-making.

Section 172(1) Statement & Stakeholder Engagement (continued)

Board Decisions

The table below sets out examples of our key stakeholders, our approach to engaging with them, and how they are taken into regard in Board considerations.

Key Stakeholders	Board Matter	Board Considerations
Members The Group Board maintains open and regular dialogue with its investors. The Board hold regular meetings, with each investor having a director on the SFHL Board. Members of the SIL Management team attend the SFHL Board to understand the concerns and priorities of the investors.	Performance & Risks	In all discussions the Board regularly considers if and how it is acting in the best interest of its investors, whilst ensuring that any actions: • Do/will not breach any regulatory requirements applicable to the Group or the Board. • Do/will not have any adverse effect on the security of the Group's policyholder benefits. • Comply with any legislation applicable to the Group. The SFHL Board, on which the investors sit, receives performance updates on SIL, which includes the SIL Management team attending the Board.
Customers Protecting our customers and improving their overall customer experience remains at the heart of what we do. The Group proactively monitors and manages customer opinion and has a customer focused culture to ensure fair outcomes for all.	Migration of customer data from legacy systems to Markerstudy Insurance Services Limited (MISL) systems.	The Board considered the impact of migration on customers and only proceeded with migration activity once 'dress rehearsal' practice runs had shown that there would be minimal risk of any detriment caused to the customers. Evaluating the results of the practice runs had the customer impact as its main focus.
Colleagues SFHL does not have any employees. At the point of acquisition of SIL by SFHL, the majority of colleagues formerly contracted by CFS Management Services Limited and primarily allocated to SIL were TUPE transferred to Markerstudy Insurance Services Limited (MISL). We recognise the importance of engaging our colleagues, ensuring their views are considered when making decisions and supporting their wellbeing.	Change in business strategy, including migration and run-off. SIL entered into a service agreement with MISL to provide services. This resulted in the TUPE transfer of a large proportion of colleagues previously seconded to SIL.	The SIL Board considered, amongst other things, people implications including: • The impacted colleagues. • The TUPE consultation process and pack. • The Business Case shared with the Trade Unions. • Oversight/Governance Structure. • Colleague communications.

Approved by the Board on 19 May 2021 and signed on its behalf by:

John Hastings-Bass
Director

Directors' report
Report of the Board of Directors

General Information
SFHL was incorporated on 28 May 2020 as a Limited Company registered in England & Wales under the Companies Act 2006 (registered number 12629263). SFHL is a holding company. Its sole subsidiary, SIL, is authorised by the Prudential Regulation Authority (PRA) and regulated by the Financial Conduct Authority (FCA) and the PRA (FRN 435022). The Group is supervised by the PRA.

On 2 December 2020, the Company purchased SIL following approval by the PRA.

Post Balance Sheet Events
As disclosed in the Strategic Report on page 2 on 11 February 2021 the SIL Board, as part of the Group's strategy, made the decision to place SIL into run-off and ceased to write new insurance business from 24 February 2021. The PRA approved SIL's application to remove its permission to effect new insurance contracts from 29 March 2021.

Results and Dividends
The financial statements set out the financial position of the Group and the Company and the results of the Group for the period ended 31 December 2020 and are shown on pages 13 to 19. The Directors did not propose any dividend payment in the period or prior period.

Political Donations
There were no political donations during the period.

Directors' Details
The Directors of SFHL during the financial period are listed below. Their appointments were for the full period unless otherwise stated:

Non-Executive Directors:
Keith Barber (appointed 12 November 2020)
John Pantekidis (appointed 12 November 2020)
Sharon Ludlow (appointed 2 December 2020)
John Hastings-Bass (appointed 2 December 2020)
Kathryn Morgan (appointed 2 December 2020)
Barnabas Hurst-Bannister (appointed 2 December 2020)
Alex Howell (appointed 9 June 2020)
Madalena Nunes Godhinho Ramos (appointed 9 June 2020, resigned 12 November 2020)
Michael Mount (appointed 28 May 2020, resigned 12 November 2020)

Secretary:
Vistra Company Secretaries Limited (appointed 2 December 2020)

Employees and employment of people with disability
The Group employs a small number of colleagues to oversee the key functions of the business, with additional services provided by Markerstudy Insurance Services Limited (MISL) through the outsourcing agreement.

The Group actively encourages all employees to become involved in the Group's activities and information is shared on a regular basis through email correspondence and weekly meetings so that employees are aware of factors affecting them and the performance of the business. Further information on the systematic provision of information to colleagues is included in the 'Section 172' section of the Strategic report on page 7.

The Group is committed to the fair and equitable treatment of all of its employees irrespective of gender, race, age, religion, disability or sexual orientation.

The Group gives full and fair consideration to applications for employment from disabled persons, equally with those who do not have a disability and to retain and re-train any employees that become disabled during their working life.

Corporate responsibility and the environment
Under the Companies Act 2006 and in line with Streamlined Energy and Carbon Reporting (SECR) the Group is required to disclose information in relation to its energy usage. The Group's main source of energy use is in the office space used by the trading subsidiary, SIL. In the year to 31 December 2020 the energy usage by SIL is estimated to be 2015MWh. Energy usage was reduced in the period through moving from large offices to an outsourced model which uses significantly less office space. Within the period since acquisition, where SIL had moved to the outsourced model, energy usage is estimated to be 14MWh. Energy usage has been estimated using data provided by the supplier for premises occupied, where available, and using data for similar properties, where data for the premises occupied is not available.

Report of the Board of Directors

Statement of Going Concern

The Annual Report and Accounts are prepared on a going concern basis and the Directors are satisfied that the Company and the Group have the resources to continue in business over the going concern assessment period, which covers the period from the date of approval of the financial statements up to 31 December 2022. In making this assessment the Directors have performed a detailed analysis of future capital and liquidity.

The going concern assessment performed takes into account that SIL has ceased to write insurance business from February 2021 and continues as a going concern as, during the run-off period, SIL operates its business of administration of existing policies in force and the settlement of outstanding claims. Projections take into account the recognition of all future expenses within technical provisions at the point SIL went into run-off. The Group's ability to continue as a going concern has been considered by reference to its projected coverage of solvency capital requirement, its liquidity and its resilience to withstand foreseeable stress scenarios over the period to 31 December 2022. The Company's ability to continue as a going concern has been considered by reference to its net asset value, its liquidity and its resilience to withstand foreseeable stress scenarios over the period to 31 December 2022.

In the Group's central forecast case, solvency projections show a low point in the SCR coverage of 118% in June 2021 as a consequence of the business entering run-off, but this quickly starts to recover as the solvency requirement falls owing to ceasing underwriting. Liquidity projections assess expected liquid assets (cash, overnight reverse repos and UK gilts) and stressed investments (the value of investments in a stressed scenario after applying a haircut, which considers the type of asset and maturity. See liquidity risk section of note 29 on page 53). Both projected liquid investments and stressed investments are expected to be in excess of the Board's risk appetite throughout the period of review.

The Directors have then considered the potential impact of various stresses including, but not limited to, a series of weather events, adverse claims experience and a fall in the market value of assets. In addition the Directors have also considered a specific COVID-19 stress scenario which includes the impact of a delay in collecting premiums. In the three most extreme stressed scenarios, SCR coverage could fall briefly below 110%, particularly if the event occurred in the first half of 2021, however, in all cases the SCR coverage naturally recovers to above 110% within 6 months without any need for management actions. In each scenario the Group has sufficient liquidity to pay liabilities as they fall due. Even in the event of an extreme stress scenario it is projected that the Group would be able to meet the majority of payments solely from existing cash holdings and investment maturities, with only modest reliance on either additional income from premium cashflow or the sale of highly liquid short-dated gilts or highly rated corporate bonds.

The Directors have also considered a reverse stress test, which involves several of the stress scenarios happening concurrently, and is therefore extremely unlikely. In this scenario, the SCR coverage ratio is projected to fall below 100% but assets continue to exceed liabilities and solvency coverage recovers naturally to over 100% within 6 months. In this scenario the Group would still be expected to be able to meet all of its liabilities as they fall due through the sale of corporate bonds.

In the Company's central forecast the value of net assets is forecast to remain positive over the going concern assessment period. The Company also forecasts holding liquid assets in excess of SFHL's risk appetite over the going concern assessment period, except for a temporary dip between June and November 2022 due to the planned payment of interest on subordinated loans. Nevertheless, the Company retains sufficient liquid assets to meet its liabilities as they fall due. This is on the basis that SFHL would, as agreed with SIL, defer the planned reimbursement of expenses to SIL until it receives the first dividend payment from its subsidiary. If SFHL were to have insufficient liquid assets, the payment of subordinated interest would be cancelled (perpetual instrument) or deferred (term instrument) as the instruments include a solvency condition which requires that SFHL has sufficient cash to pay its other creditors before interest payments can be made.

Stressed investments are projected to be in excess of SFHL's risk appetite, except from March to November 2022 due to the deferred subordinated term instrument interest and the quarterly interest for both the perpetual and term subordinated instruments projected to be paid in the next two quarters. However, as stated above, if SFHL were to have insufficient liquid assets, the interest would be cancelled (perpetual instrument) or deferred (term instrument).

The Directors have also considered a reverse stress test for the Company, which involves a large unexpected expense being incurred at the same time as not receiving forecast dividends from its subsidiary, and is extremely unlikely. In this scenario, the Company would maintain sufficient liquidity through the deferment of the subordinated term instrument interest payments and/or defer the reimbursement of expenses to its subsidiary.

Risk Management and Internal Controls

The SFHL and SIL Boards have overall responsibility for the Group's internal control systems and for monitoring their effectiveness. Implementation and maintenance of the internal control systems are the responsibility of the Board and senior management.

The SFHL and SIL Boards have established a management structure with defined lines of responsibility and clear delegation of authority. The control framework cascades through the business, detailing clear responsibilities for ensuring appropriate controls are in place at an operational level, including controls relating to the financial reporting process. The Group's approach to Risk Management is set out in further detail on pages 49 to 54.

The Group's internal control systems are designed to manage, rather than eliminate, the risks of failure to meet business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss. In assessing what constitutes reasonable assurance, the Board has regard to materiality and to the relationship between the cost of, and benefits from, internal control systems.

On behalf of the Board, the SFHL Risk and Audit Committee regularly reviews the effectiveness of the Group's internal control systems. Its monitoring covers all material controls. Principally it reviews and challenges, on an ongoing basis, reports from management, the internal audit function and external auditors. This enables it to consider how to manage or mitigate risk in line with the Group's risk strategy. The Risk and Audit Committee did not identify or report any material failings to the Board in 2020.

Report of the Board of Directors

Whenever any significant control weaknesses are identified actions are taken, or agreed plans are put in place and tracked by the Board to implementation.

Annual Report and Accounts

So far as the Directors are aware, there is no relevant audit information of which the Group's auditors are unaware, and the Directors have taken all steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the Group's auditors have been made aware of that information.

Statement of Directors' responsibilities in respect of the report of the Board of Directors and the Annual Report and Accounts

The Directors are responsible for preparing the Annual Report and Accounts in accordance with applicable United Kingdom law and regulations.

Company law requires the Directors to prepare accounts for each financial period. Under that law the Directors have elected to prepare the Company and Group's accounts in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006.

As required by Law, the Directors must not approve the Report and Accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and Group and of the Group's profit or loss for that period. In preparing these accounts, the Directors are required to:

- select suitable accounting policies in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- in respect of the financial statements, state whether international accounting standards in conformity with the requirements of the Companies Act 2006 have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the accounts on the going concern basis unless it is appropriate to presume that the Company or Group will not continue in business.
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- provide additional disclosures when compliance with the specific requirements in international accounting standards in conformity with the requirements of the Companies Act 2006 is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group and Company financial position and financial performance.

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

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report and a Directors' Report that comply with that law and regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on SFHL's website. Legislation in the UK governing the preparation and dissemination of annual report and accounts may differ from legislation in other jurisdictions.

By order of the Board
John Hastings-Bass
Director
40 Berkeley Square
London
W1J 5AL

19 May 2021

Opinion

We have audited the financial statements of Soteria Finance Holdings Limited ('the parent company') and its subsidiaries (the 'group') for the period ended 31 December 2020 which comprise the Consolidated Income Statement, Consolidated Statement of Comprehensive Income, Consolidated Statement of Financial Position, Company Statement of Financial Position, Consolidated Statement of Cash Flows, Company Statement of Cash Flows, Consolidated and Company Statement of Changes in Equity and the related notes 1 to 33 (except for that section of note 29 (i) which is marked as unaudited), including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Accounting Standards in conformity with the requirements of the Companies Act 2006 and, as regards the parent company financial statements, as applied in accordance with section 408 of the Companies Act 2006.

In our opinion:

- the financial statements give a true and fair view of the group's and of the parent company's affairs as at 31 December 2020 and of the group's profit for the period then ended;
- the group financial statements have been properly prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006;
- the parent company financial statements have been properly prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 as applied in accordance with section 408 of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the group and parent company's ability to continue as a going concern from when the financial statements are authorised for issue until 31 December 2022.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's ability to continue as a going concern.

Other information

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

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

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us 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 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.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 9, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the group and determined that the relevant laws and regulations related to elements of company law and tax legislation, and the financial reporting framework. Our considerations of other laws and regulations that may have a material effect on the financial statements included permissions and supervisory requirements of the Prudential Regulation Authority ('PRA'), the Financial Conduct Authority ('FCA') and the Jersey Financial Services Commission ('JFSC').

- We understood how the group is complying with those frameworks by making enquiries of management, internal audit and those responsible for legal and compliance matters. We also reviewed correspondence between the group and UK regulatory bodies; reviewed minutes of the Board and Board committees and gained an understanding of the group's approach to governance, demonstrated by the Board's approval of the group's governance framework and the Board's review of the group's risk management framework and internal control processes.

- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved making enquiry of those charged with governance and senior management for their awareness of any non-compliance with laws or regulations, inquiring about the policies that have been established to prevent non-compliance with laws and regulations by officers and employees, inquiring about the group's methods of enforcing and monitoring compliance with such policies and inspecting significant correspondence with the PRA, FCA and JFSC.

- We assessed the susceptibility of the group's financial statements to material misstatement, including how fraud might occur by considering the controls that the group has established to address risks identified by the entity, or that otherwise seek to prevent, deter or detect fraud. We also considered the impact of COVID-19 on the group's control environment. These procedures included an assessment of the financial processes and controls in place within the group as it operated remotely for a significant proportion of 2020.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud (continued)

- We also considered areas of significant judgment, including performance targets, external pressures and the impact these have on the control environment. .

  The fraud risk, including management override, was considered to be higher in respect of;

  - the setting of claim reserves (specifically IBNR) and the recognition and measurement of the management margin; and
  - the inappropriate recognition of premium income (specifically premium income recognised through manual journals).

  We performed audit procedures to address the risk as detailed in our communication with those charged with governance.

- We also performed journal entry testing, with a focus on manual journals and journals indicating large or unusual transactions based on our understanding of the business, incorporating unpredictability into the nature, timing and/or extent of our testing, and challenged assumptions and judgments made by management in setting significant estimates.
- The group operates in the insurance industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team and concluded that the team had the appropriate competence and capabilities, which included the use of specialists, where appropriate.

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

Use of our report

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

Giles Watson (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
Manchester
20 May 2021

Notes:
1. The maintenance and integrity of the Soteria Finance Holdings Limited web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.

2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated Income Statement

For the period ended 31 December 2020

All amounts are stated in £m unless otherwise indicated

	Notes	2020
Income		
Gross earned premiums		**31.2**
Less premiums ceded to reinsurers		**(10.5)**
Net earned premiums	2	**20.7**
Fee and commission income	3	**3.5**
Investment income	4	**0.5**
Gains less losses arising from financial instruments	5	**1.0**
Net income		**25.7**
Claims paid	6	**(30.7)**
Less amounts receivable from reinsurers	6	**7.7**
Net policyholder claims and benefits paid	6	**(23.0)**
Change in insurance contract liabilities	22c	**7.4**
Change in reinsurance assets	22c	**0.1**
Net policyholder claims and benefits incurred		**(15.5)**
Fee and commission expenses	7	**(0.5)**
Other acquisition expenses	8	**(0.8)**
Administration expenses	8	**(10.2)**
Finance costs	9	**(1.0)**
Loss before gain on bargain purchase and taxation		**(2.3)**
Gain on bargain purchase	10	**146.5**
Profit before taxation		**144.2**
Income tax	11	**(0.4)**
Profit for the financial period		**143.8**

The consolidated income statement for the period comprises SFHL's results from incorporation (28 May 2020) and SIL's results from acquisition (2 December 2020) which is when control was achieved.

Consolidated Statement of Comprehensive Income/(Expense)

For the period ended 31 December 2020

All amounts are stated in £m unless otherwise indicated

	Notes	**2020**
Profit for the financial period		**143.8**
Items that are or may be reclassified to the income statement:		
Net changes in fair value in financial assets at fair value through other comprehensive income		**2.1**
Income tax	23	**(0.5)**
Other comprehensive income for the financial period, net of income tax		**1.6**
Total comprehensive income for the financial period		**145.4**

Consolidated Statement of Financial Position

For the period ended 31 December 2020
All amounts are stated in £m unless otherwise indicated

	Notes	2020
Assets		
Property, plant and equipment	12	**1.1**
Reinsurance assets	22	**66.1**
Financial investments at fair value through income or expense	14	**141.0**
Financial assets at fair value through other comprehensive income	15	**526.1**
Current tax assets	23	**3.1**
Insurance receivables and other assets	16	**167.7**
Cash and cash equivalents	17	**28.6**
Total assets		**933.7**
Capital and reserves attributable to equity holders		
Share capital	18	**0.1**
Share premium	19	**36.9**
Retained earnings	20	**143.8**
Other reserves	20	**1.6**
Total equity		**182.4**
Liabilities		
Insurance contract liabilities	22	**630.7**
Lease liabilities and borrowings	21	**71.0**
Deferred tax liabilities	23	**1.8**
Corporation tax liabilities	23	**1.8**
Reinsurance liabilities	24	**10.3**
Insurance and other payables	25	**29.7**
Overdrafts	17	**6.0**
Total liabilities		**751.3**
Total equity and liabilities		**933.7**

John Hastings-Bass, Director

Keith Barber, Director

Company Statement of Financial Position

For the period ended 31 December 2020

All amounts are stated in £m unless otherwise indicated

Assets		
Investment in group undertakings	13	**104.0**
Insurance receivables and other assets	16	**0.5**
Cash and cash equivalents	17	**1.8**
Total assets		**106.3**
Capital and reserves attributable to equity holders		
Share capital	18	**0.1**
Share premium	19	**36.9**
Retained earnings	20	**(1.9)**
Total equity		**35.1**
Liabilities		
Borrowings	21	**69.8**
Insurance and other payables	25	**1.4**
Total liabilities		**71.2**
Total equity and liabilities		**106.3**

The retained earnings disclosed above represent the Company's loss for the period to 31 December 2020.

John Hastings-Bass, Director

Keith Barber, Director

Consolidated Statement of Cash Flows

For the period ended 31 December 2020

All amounts are stated in £m unless otherwise indicated

	Notes	2020
Cash flows from operating activities		
Profit before taxation		**144.2**
Adjustment for:		
Interest payable		**1.0**
Gain on bargain purchase		**(146.5)**
Investment income		**(0.5)**
Gains less losses arising from financial instruments		**(1.0)**
Increase in reinsurance assets		**(4.1)**
Net proceeds of sale of financial instruments at value through income and expense		**28.8**
Decrease in insurance receivables and other assets		**11.0**
Decrease in insurance contract liabilities		**(25.9)**
Increase in reinsurance liabilities		**3.7**
Investment interest received		**2.1**
Net proceeds of sales on investments held as AFS		**5.1**
Increase in insurance and other payables		**2.5**
Net cash flows from operating activities		**20.4**
Cash flows from investing activities		
Purchase of subsidiary		**(104.0)**
Net cash flows from investing activities		**(104.0)**
Cash flows from financing activities		
Issuance of share capital		**37.0**
Issuance of Tier 1 Restricted perpetual subordinated notes		**12.0**
Issuance of Tier 2 10 year subordinated notes		**60.0**
Costs in relation to issue of subordinated notes		**(2.2)**
Interest paid		**(0.1)**
Net cash flows from financing activities		**106.7**
Net increase in cash and cash equivalents		**23.1**
Cash and cash equivalents acquired as part of business combination		**(0.5)**
Cash and cash equivalents at the end of the financial period	17	**22.6**

Cash flows from operating activities

The Group classifies the cash flows for the acquisition and disposal of financial assets as operating cash flows. This is because purchases are funded from the cash flows associated with the origination of insurance contracts, net of the cash flows for payments of claims incurred for insurance contracts, which are classified under operating activities.

Cash and cash equivalents in the Consolidated Statement of Cash Flows above represents Cash and cash equivalents shown as an asset in the Consolidated Statement of Financial position net of Overdrafts included in liabilities (see note 17).

Company Statement of Cash Flows

For the period ended 31 December 2020
All amounts are stated in £m unless otherwise indicated

	Notes	2020
Cash flows from operating activities		
Loss before taxation		**(1.9)**
Adjustment for:		
Interest payable		**1.0**
Increase in insurance receivables and other assets		**(0.5)**
Increase in insurance and other payables		**0.4**
Net cash flows from operating activities		**(1.0)**
Cash flows from investing activities		
Purchase of subsidiary		**(104.0)**
Net cash flows from investing activities		**(104.0)**
Cash flows from financing activities		
Issuance of share capital		**37.0**
Issuance of Tier 1 Restricted perpetual subordinated loan		**12.0**
Issuance of Tier 2 10 year subordinated loan		**60.0**
Costs in relation to issue of subordinated notes		**(2.2)**
Net cash flows from financing activities		**106.8**
Net increase in cash and cash equivalents		**1.8**
Cash and cash equivalents at the beginning of the financial period		**-**
Cash and cash equivalents at the end of the financial period	17	**1.8**

Consolidated and Company Statement of Changes in Equity

For the period ended 31 December 2020

All amounts are stated in £m unless otherwise indicated

Group	Share capital	Share premium	Other reserves	Retained earnings	Total
2020					
Balance at incorporation	-	-	-	-	-
Total comprehensive expense for the financial period:					
Profit for the period	-	-	-	**143.8**	**143.8**
Other comprehensive income	-	-	**1.6**	-	**1.6**
Transactions with owners:					
Issuance of new share capital	**0.1**	**36.9**	-	-	**37.0**
Balance at the end of the financial period	**0.1**	**36.9**	**1.6**	**143.8**	**182.4**

Company	Share capital	Share premium	Retained earnings	Total
2020				
Balance at incorporation	-	-	-	-
Total comprehensive expense for the financial period:				
Loss for the period	-	-	**(1.9)**	**(1.9)**
Transactions with owners:				
Issuance of new share capital	**0.1**	**36.9**	-	**37.0**
Balance at the end of the financial period	**0.1**	**36.9**	**(1.9)**	**35.1**

1. Basis of preparation and significant accounting policies

Soteria Finance Holdings Limited (SFHL or the Company), a Limited Company registered in England under the Companies Act 2006, together with its subsidiary, Soteria Insurance Limited (SIL), are collectively referred to as the Group. SFHL's registered office is 40 Berkeley Square, London, W1J 5AL. The Group operates primarily in the UK General Insurance market (Motor and Home) and underwrote insurance until 24 February 2021, when it went into run-off. The Group and Company financial statements were authorised for issue by the Board of Directors on 19 May 2021.

Basis of preparation

The consolidated financial statements of the Group and the financial statements of the Company have been prepared on a going concern basis and approved by the Directors in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. In accordance with the Companies Act 2006 the Company is exempt from the requirement to publish its individual profit and loss account and the related notes on the condition that the company's individual balance sheet shows the Company's loss for the financial period.

The financial information has been prepared under the historic cost convention as modified by the inclusion of certain financial assets and financial liabilities held at fair value as permitted or required by IFRS. The Group and Company apply the recognition, measurement and disclosure requirements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006..

Basis of consolidation

The Group financial statements comprise a consolidation of SFHL and SIL, per the requirements of IFRS 10 whereas the Company financial statements comprise solely of SFHL. IFRS 10 requires entities to consolidate entities it controls. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Control of SIL was achieved on acquisition and as such consolidation is from the period after 2 December 2020.

Going concern

In preparing the Group and Company's annual report and accounts on a going concern basis the directors have made an assessment considering the Group and Company's financial position, their ability to meets their obligations, as and when they fall due, and the Group's projected coverage of its solvency capital requirement over the going concern assessment period, which covers the period from the date of approval of the financial statements up to 31 December 2022. In making this assessment the Directors have performed a detailed analysis of future capital and liquidity.

In the Group's central forecast case, solvency projections show a low point in the SCR coverage of 118% in June 2021 as a consequence of the business entering run-off, but this quickly starts to recover as the solvency requirement falls owing to ceasing underwriting. Liquidity projections assess expected liquid assets (cash, overnight reverse repos and UK gilts) and stressed investments (the value of investments in a stressed scenario after applying a haircut, which considers the type of asset and maturity. See liquidity risk section of note 29 on page 53). Both projected liquid investments and stressed investments are expected to be in excess of the Board's risk appetite throughout the period of review.

The Directors have then considered the potential impact of various stresses including, but not limited to, a series of weather events, adverse claims experience and a fall in the market value of assets. In addition the Directors have also considered a specific COVID-19 stress scenario which includes the impact of a delay in collecting premiums. In the three most extreme stressed scenarios, SCR coverage could fall briefly below 110%, particularly if the event occurred in the first half of 2021, however, in all cases the SCR coverage naturally recovers to above 110% within 6 months without any need for management actions. In each scenario the Group has sufficient liquidity to pay liabilities as they fall due. Even in the event of an extreme stress scenario it is projected that the Group would be able to meet the majority of payments solely from existing cash holdings and investment maturities, with only modest reliance on either additional income from premium cashflow or the sale of highly liquid short-dated gilts or highly rated corporate bonds.

The Directors have also considered a reverse stress test, which involves several of the stress scenarios happening concurrently, and is therefore extremely unlikely. In this scenario, the SCR coverage ratio is projected to fall below 100% but assets continue to exceed liabilities and solvency coverage recovers naturally to over 100% within 6 months. In this scenario the Group would still be expected to be able to meet all of its liabilities as they fall due through the sale of corporate bonds.

In the Company's central forecast the value of net assets is forecast to remain positive over the going concern assessment period. The Company also forecasts holding liquid assets in excess of SFHL's risk appetite over the going concern assessment period, except for a temporary dip between June and November 2022 due to the planned payment of interest on subordinated loans. Nevertheless, the Company retains sufficient liquid assets to meet its liabilities as they fall due. This is on the basis that SFHL would, as agreed with SIL, defer the planned reimbursement of expenses to SIL until it receives the first dividend payment from its subsidiary. If SFHL were to have insufficient liquid assets, the payment of subordinated interest would be cancelled (perpetual instrument) or deferred (term instrument) as the instruments include a solvency condition which requires that SFHL has sufficient cash to pay its other creditors before interest payments can be made.

Projected stressed investments are expected to be in excess of SFHL's risk appetite, except from March to November 2022 due to the deferred subordinated term instrument interest and the quarterly interest for both the perpetual and term subordinated instruments projected to be paid in the next two quarters. However, as stated above, if SFHL were to have insufficient liquid assets, the interest would be cancelled (perpetual instrument) or deferred (term instrument).

The Directors have also considered a reverse stress test for the Company, which involves a large unexpected expense being incurred at the same time as not receiving forecast dividends from its subsidiary, and is extremely unlikely. In this scenario, the Company would maintain sufficient liquidity through the deferment of the subordinated term instrument interest payments and/or defer the reimbursement of expenses to its subsidiary.

1. **Basis of preparation and significant accounting policies (continued)**

Going concern (continued)
Following their assessment the directors are satisfied that the Group and Company will be able to operate over the going concern assessment period and therefore the annual report and accounts have been prepared on a going concern basis.

Adoption of new and revised standards
No new or revised standards were issued since incorporation which had significant impact on the Group.

Standards and interpretations issued but not yet effective

IFRS 17 'Insurance Contracts'
In May 2017, the IASB issued IFRS 17 Insurance Contracts, a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure, which replaces IFRS 4 Insurance Contracts.

In contrast to the requirements in IFRS 4, which are largely based on grandfathering previous local accounting policies for measurement purposes, IFRS 17 provides a comprehensive model (the general model) for insurance contracts, supplemented by the premium allocation approach mainly for short-duration which typically applies to certain non-life insurance contracts.

In June 2020, the International Accounting Standards Board issued amendments to IFRS 17 Insurance Contracts aimed at helping companies implement the Standard and making it easier for them to explain their financial performance. It decided that the effective date of the Standard will be deferred to annual reporting periods beginning on or after 1 January 2023. The Board also decided to extend the exemption currently in place for some insurers regarding the application of IFRS 9 Financial Instruments to enable them to implement both IFRS 9 and IFRS 17 at the same time. This exemption does not apply to the Group.

Early application is permitted; provided the entity also applies IFRS 9 on or before the date it first applies IFRS 17. The Group has not early adopted IFRS 17.

The impact of adopting IFRS 17 has yet to be fully assessed by Group, but it is expected there will be significant impacts relating to the measurement and presentation of contracts within scope of the standard.

Significant accounting policies

Use of estimates and judgments
The preparation of the annual report and accounts requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the annual report and accounts, are described within the significant accounting policies below.

Information about estimation uncertainty, that has the most significant effect on the amounts recognised in the annual report and accounts, relates to the determination of the ultimate liability arising from claims made under insurance contracts. Details of the methodology, key assumptions and sensitivities are provided in note 22. Additionally further reference is made within the risk management section in relation to insurance risk on pages 49 and 50.

In deriving the fair value of assets and liabilities the methods and assumptions used by the Group and Company are detailed within the fair values of financial assets and liabilities in note 32 (pages 56 to 58).

The accounting policies set out below have been applied consistently to all periods presented in this annual report and accounts. The accounting policies are split between insurance and non-insurance specific accounting policies. The insurance accounting policies are detailed in accounting policy 15 on pages 25 to 27. The major methods and assumptions used in estimating the fair values of financial instruments are detailed in note 32.

1. Basis of preparation and significant accounting policies (continued)

(1) Business combinations and goodwill
Business combinations are accounted for using the acquisition method. Under this method the acquirer recognises the acquiree's fair value of the identifiable assets, liabilities (including contingent liabilities) at the acquisition date.

Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired. Goodwill is measured on initial recognition at cost. Following initial recognition, goodwill is stated at cost less any accumulated impairment losses. Goodwill is not amortised but is tested for impairment annually or when there is evidence of possible impairment. For impairment testing, goodwill is allocated to relevant cash generating units. Goodwill is impaired when the recoverable amount is less than the carrying value.

A gain on bargain purchase, or negative goodwill, arising on an acquisition is recognised directly in the income statement.

(2) Investments in subsidiaries
Subsidiaries are entities that the Company controls, by being exposed to, or having rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated with the parent company in the Group financial statements and carried as an asset in the Company financial statements.

Investment in subsidiaries in the Company financial statements are held at cost less accumulated impairment losses, and are considered for impairment at each reporting date.

(3) Property, plant and equipment
Property, plant and equipment is stated at cost or deemed cost less accumulated depreciation and impairment losses.

Depreciation is charged to the income statement on a straight line basis to allocate the difference between cost and residual value over the estimated useful lives when assets are commissioned for use. Estimated useful lives are as follows:

- Leasehold property — Over the term of the lease

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and are recognised net within operating expenses in the income statement.

Costs that are directly associated with the internal production of tangible assets that will generate future economic benefit are capitalised and recognised as tangible assets in the course of construction. Assets in the course of construction are only depreciated when they are commissioned for use.

(4) Financial instruments
The Group classifies its financial assets (excluding derivatives) as either:
- financial assets at fair value through other comprehensive income; or
- financial assets at fair value through income or expense; or
- loans and receivables.

i) Recognition of financial assets and financial liabilities
Financial assets are recognised by the Group on the trade date which is the date it commits to purchase the instruments. All other financial instruments are recognised on the date that they are originated.

ii) Derecognition of financial assets and financial liabilities
Financial assets are derecognised when they are sold and:
- the rights to receive cash flows from the assets have ceased; or
- the Group has transferred substantially all the risks and rewards of ownership of the assets.

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires. When an existing liability is replaced by the same counterparty on substantially different terms or the terms of an existing liability are substantially modified, the original liability is derecognised and a new liability is recognised, with any difference in carrying amounts recognised in the income statement.

iii) Financial assets classified as fair value through other comprehensive income
The Group's holdings in debt securities are classified as financial assets at fair value through other comprehensive income under IFRS 9, on the basis cashflows are 'Solely Payments of Principal and Interest' (SPPI) and the assets are held to collect and sell. Initial measurement is at fair value, being purchase price on the date on which the Group commits to purchase plus directly attributable transaction costs.

Subsequent valuation is at fair value with movements recognised in other comprehensive income as they arise. Interest is recognised on the effective interest rate basis in the income statement, refer to accounting policy note 10 (page 24) for further details. Allowance is made for impairment through the calculation of expected credit losses in accordance with IFRS 9. For further information refer to accounting policy note 4 (vii) on page 23. An effective interest rate for each holding is calculated on initial recognition and subsequently recognised in the income statement over the lifetime of the bond.

On disposal, gains or losses previously recognised in other comprehensive income are transferred to the income statement.

1. Basis of preparation and significant accounting policies (continued)

iv) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and the Group does not intend to sell immediately or in the near term. For the Group, this includes insurance premium debt receivables but excludes salvage and subrogation. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently, these are measured at amortised cost. The amortised cost is the initial amount at recognition less principal repayments, plus or minus the cumulative amortisation using the effective interest rate method of any difference between the initial amount and the maturity amount, less impairment provisions for expected credit losses.

v) Financial investments at fair value through income or expense

Investments are classified as financial assets at fair value through income or expense, where they do not meet the criteria of IFRS 9 to be measured at amortised cost or at fair value through other comprehensive income. Assets held at fair value through income or expense are managed and their performance is evaluated on a fair value basis in accordance with a documented risk management or investment strategy, and information is provided internally to key management personnel on that basis. This includes investments in collective investment assets.

Initial measurement is at fair value, being purchase price on the date on which the Group commits to purchase. Directly attributable transaction costs are expensed immediately on recognition. Subsequent valuation is at fair value with changes in fair value being recognised in gains less losses within the income statement in the period in which they arise. Where there is no active market or the investments are unlisted, the fair values are based on commonly used valuation techniques.

(vi) Financial liabilities

Financial liabilities, which primarily represent borrowed funds, are contractual obligations to deliver cash or other financial assets. Financial liabilities are initially recognised at the value of issue proceeds net of directly attributable transaction costs. Subsequent measurement is at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest rate method.

Borrowings are primarily subordinated bond issues.

vii) Impairment of financial assets

Assessment

At the statement of financial position date, the Group assesses its financial assets not carried at fair value through income or expense for objective evidence that an impairment loss has occurred.

Objective evidence that financial assets are impaired can include default by a borrower or issuer, indications that a borrower or issuer will enter bankruptcy or the disappearance of an active market for that financial asset because of financial difficulties.

Impairment of financial assets at fair value through other comprehensive income

In accordance with IFRS 9 the Group is required to recognise expected credit losses (ECLs) based on unbiased forward-looking information.

It is first assessed whether the credit risk relating to the assets has increased significantly since initial recognition. The assessment uses credit ratings provided by the Group's investment manager's. For the period ended 31 December 2020 the credit rating, at the reporting date of each individual investment was compared against the credit rating from the same source as at the acquisition date, which for the Group was 2 December 2020. If credit risk has not increased significantly then the expected 12 month ECL is calculated. If it has increased significantly then lifetime ECLs are used.

ECLs are calculated using the probability of default applied to the value of the asset held at the reporting date. The Group's portfolio of assets focuses on higher rated corporate bonds and gilts which have a low probability of default.

Impairment losses are recognised by transferring the cumulative loss that has been recognised through other comprehensive income to the income statement.

Impairment of financial assets carried at amortised cost

The amount of the impairment loss on assets carried at amortised cost is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

A write off is made when all or part of an asset is deemed uncollectable or forgiven after all the possible collection procedures have been completed and the amount of loss has been determined. Write offs are charged against previously established provisions for impairment or directly to the income statement.

Any additional recoveries from borrowers, counterparties or other third parties made in future periods are offset against the write off charge in the income statement once they are received.

Provisions are released at the point when it is deemed that following a subsequent event the risk of loss has reduced to the extent that a provision is no longer required.

1. Basis of preparation and significant accounting policies (continued)

viii) Gains less losses arising from financial assets
Gains less losses arising from financial assets represents unrealised fair value movements of assets held at fair value through income or expense as well as realised gains/losses on financial assets at fair value through other comprehensive income.

(5) Sale and repurchase arrangements
The Group participates in reverse sale and repurchase transactions whereby the Group buys gilts but is contractually obliged to sell them at a fixed price on a fixed future date. Cash loaned under reverse repo arrangements is classified on the statement of financial position as deposits with credit institutions within financial investments at fair value through income or expense.

(6) Cash and cash equivalents
Cash and cash equivalents comprises cash balances and balances with a maturity of three months or less from the acquisition date, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Banking facilities that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the cash flow statement.

(7) Offsetting
IFRS 4 prohibits the offsetting of reinsurance assets against the related insurance liabilities unless the appropriate legal requirements are met. Financial assets and liabilities arising under the quota share arrangements are offset and the net amount reported in the statement of financial position as there is a legally enforceable right to set off the amounts, and there is an intention to settle on a net basis. The contractual terms of the funds withheld quota share agreement require such a set-off of associated amounts.

(8) Impairment of non-financial assets
The carrying value of the Group's and Company's non-financial assets, excluding deferred tax assets, is reviewed at the statement of financial position date to determine whether there is any indication of impairment. If impairment is indicated, the asset's recoverable amount (being the greater of fair value less cost to sell and value in use as assessed by reference to discounted future cash flows) is estimated.

An impairment loss is recognised in the income statement to the extent that the carrying value of an asset exceeds its recoverable amount. An impairment loss is reversed if there has been an increase in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent of the asset's carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(9) Provisions
A provision is recognised in the statement of financial position if the Group or Company has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(10) Revenue recognition
Revenue principally comprises:

Premium income from insurance contracts

The Group's accounting policy in respect of revenue arising from insurance contracts is set out within the insurance specific accounting policy note 15(i) on page 26.

Investment income
Interest income on financial assets designated as financial assets at fair value through other comprehensive income and loans and receivables is recognised within investment income on an effective interest rate (EIR) basis, inclusive of directly attributable incremental transaction costs and fees, and discounts and premiums where appropriate.

The EIR basis spreads the interest income over the expected life of the instrument. The EIR is the rate that, at inception of the instrument, exactly discounts expected future cash payments and receipts through the expected life of the instrument back to the initial carrying amount. When calculating EIR, the Group estimates cash flows considering all contractual terms of the instrument (for example prepayment options) but does not consider future credit losses.

Interest income on assets designated as fair value through income or expense is recognised within investment income in the income statement as it accrues on an effective interest rate basis.

Dividend income
Dividend income is recognised when the right to receive the payment is established, which is generally when the Directors approve the dividend as final. Interim dividends are recognised when the dividend is paid.

Fee and commission income
Fees and commission receivable mainly relates to administration fee income and brokerage commission received for products and services administered by third parties.

1. Basis of preparation and significant accounting policies (continued)

Revenue is recognised as the Company satisfies the related performance obligation in accordance with IFRS 15. In the case of services such as policy administration fees, the Group's performance obligations are met when the third party makes adjustments in its administration of the policy. At this point, the Group's commission income is recognised in full at the contracted rate. The resulting receivable to the Group is settled by the third party to contract terms of 30 days following the month end the service was completed. All obligations in respect of the service, including obligations for returns, refunds and other similar obligations are completed by the third party. There are no warranty or related obligations for which the Group is liable.

Commission receivable on third party product sales is recognised upon the sale as all Group obligations are met immediately. The resulting receivable to the Group is settled by the third party to contract terms of 30 days following the month end the transaction was completed. The Group receivable is fixed per policy per contract terms with the third party. The Group has no future obligation for the commission received on sale of that product through warranty or any other related obligations. Obligations for returns, refunds and other similar obligations are met by the third party.

Profit commission due under reinsurance arrangements
Profit commission due under reinsurance arrangements is recognised in the income statement in line with the associated premiums ceded and ceded incurred claim costs, in accordance with the contractual terms to which they are subject.

(11) Fee and commission expenses
Fees and commission expenses mainly relates to commission payable to insurance intermediaries that is recognised over the lifetime of the related policy. All other fees and commission expenses is recognised on an accruals basis as the service is provided.

(12) Income tax
Tax in the income statement for the period comprises current and deferred tax, which is recognised in the income statement except to the extent that it relates to items in other comprehensive income, in which case it is recognised in the statement of comprehensive income.

Current tax
Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at the statement of financial position date, and any adjustment to tax payable in respect of previous years.

When there is uncertainty over the income tax treatment, if it is probable that a particular tax treatment is accepted, the Group and Company determine taxable profit/(tax loss), tax bases, unused tax losses, unused tax credits or tax rates consistently with the tax treatment included in the Group and Company's corporation tax filing. If it is not probable that a particular tax treatment is accepted, the Group and Company use the most likely amount or the expected value of the tax treatment when determining taxable profit/(tax loss), tax bases, unused tax losses, unused tax credits and tax rates, whichever gives better predictions of the resolution of the uncertainty.

Deferred tax
Deferred tax is provided using the statement of financial position method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

The amount of deferred tax provided for is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the statement of financial position date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(13) Foreign currencies
The functional and presentational currency for the Group and Company is sterling. Substantially all transactions conducted by the Group and Company are in sterling. All amounts presented are stated in pound sterling and millions, unless stated otherwise.

(14) Dividends to shareholders
Dividends are only recognised in the annual report and accounts by the Group and Company once they have been approved by the shareholders in a general meeting.

(15) Insurance accounting policies
Contracts under which the Group accepts significant insurance risk from another party (the policyholder), by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary, are classified as insurance contracts. A contract that qualifies as insurance remains an insurance contract until all the risks and obligations are extinguished or expire.

All contracts of general insurance business written by the Group are classified as insurance contracts. General insurance business is accounted for on an annual basis.

1. Basis of preparation and significant accounting policies (continued)

i) Premiums
Gross written premiums comprise premiums receivable on those contracts which incepted during the financial period, irrespective of whether they relate in whole or in part to a later accounting period, together with any adjustments in the accounting period relating to premium receivable in respect of business written in prior periods.

Gross written premiums:

- are stated gross of commission and exclude any taxes or levies based on premiums;
- include an estimate for cancellations for those renewal contracts which incepted prior to the year-end but which may be cancelled after the statement of financial position date; and
- include an estimate of pipeline premium, using historic average trends.

Gross written premium (whether paid in advance or by instalments) is earned evenly over the period of the contract.

ii) Unearned premium provision
For general insurance business, the proportion of written premiums relating to periods of risk beyond the year-end is carried forward to future accounting periods. The relevant proportion is calculated using the daily pro rata basis.

Outward reinsurance premiums are treated as earned in accordance with the profile of the reinsured contracts.

iii) Claims incurred
Insurance claims incurred comprises claims paid during the period, together with related claims handling costs and the change in the gross liability for claims in the period, net of related recoveries including salvage and subrogation.

iv) Claims outstanding
Claims outstanding comprises provisions representing the estimated ultimate cost of settling:

- estimates on claims reported by the statement of financial position date ('claims reported'); and
- expected additional cost in excess of claims reported for all claims occurring by the statement of financial position date ('claims incurred but not reported').

Aggregate claims provisions, which include attributable claims handling expenses, are set at a level such that no adverse run off deviations are expected. Adverse run off deviations, which are material in the context of the business as a whole, would be separately disclosed in the notes to the annual report and accounts including the claims development tables.

Anticipated reinsurance recoveries and estimates of salvage and subrogation recoveries are disclosed separately within assets under the headings of 'reinsurance assets' and 'insurance receivables and other assets' respectively.

Outstanding reserves are discounted in respect of periodical payments and a portion of historic liability claims from the electric industry for which separate assets are held of similar duration.

v) Unexpired risk provision
Additional provision is made for unexpired risks where the claims and expenses, likely to arise after the end of the financial period in respect of contracts concluded before that date, are expected to exceed the unearned premiums less deferred acquisition costs carried forward for those contracts.

Unexpired risk provision is calculated for each category of business. Where categories of business are managed together a combined calculation is performed. Surpluses and deficits within each category are offset within the calculation. The provision is determined after taking account of future investment return arising on investments supporting the unearned premium provision and unexpired risk provision.

Such provisions seek to ensure that the carrying amount of unearned premiums provision less related deferred acquisition costs is sufficient to cover the current estimated future cash flows, including claims handling expenses and therefore meets the requirements of the liability adequacy test as set out in IFRS 4 (Insurance Contracts).

vi) Reinsurance
Contracts with reinsurers that give rise to a significant transfer of insurance risk are accounted for as reinsurance contracts. Amounts recoverable under such contracts are recognised in the same period as the related claim. Premiums, claims and receivables are presented on a gross basis in the income statement and statement of financial position.

Amounts recoverable under reinsurance contracts are assessed for impairment at each statement of financial position date. If objective evidence of impairment exists, reinsurance assets are reduced to the level at which they are considered to be recoverable and an impairment loss is recognised in the income statement.

1. Basis of preparation and significant accounting policies (continued)

vii) Quota share

The quota share reinsurance contract transfers insurance risk on a proportional basis. The income statement is shown net of premiums ceded, claims recoverable and commission earned under this arrangement.

Premiums ceded are held in a notional funds withheld account, against which claims paid recoveries, earned commission and margin paid, are deducted. The funds withheld balance is offset against expected recoveries for claims outstanding and future profit commission in the statement of financial position.

For the purposes of classification in the income statement, commutation of the contract is not assumed, such that future recoveries in the funds withheld account are recognised against claims incurred. At the point of commutation, outstanding recoveries in the funds withheld account would be earned as further commission.

(16) Right-of-use assets and Lease liabilities

Right-of-use assets

The Group recognises right-of-use assets at the commencement date of the lease i.e. the date the underlying asset is available for use. Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Unless the Group is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognised right-of-use assets are depreciated on a straight-line basis over the shorter of its estimated useful life and the lease term. Right-of-use assets are subject to impairment.

Lease liabilities

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating a lease if the lease term reflects the Group exercising the option to terminate. The variable lease payments that do not depend on an index or a rate are recognised as expense in the period in which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Group uses the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made.

In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset.

Short-term leases and leases of low-value assets

The Group applies the short-term lease recognition exemption to its short-term leases of machinery and equipment i.e. those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option. It also applies the lease of low-value assets recognition exemption to leases of office equipment that are considered of low value i.e. below £5,000. Lease payments on short-term leases and leases of low-value assets are recognised as expenses on a straight-line basis over the lease term.

All amounts are stated in £m unless otherwise indicated

2. Net earned premiums

	2020
Gross premiums	
Gross written premiums	**14.2**
Change in unearned premium provision	**17.0**
Gross earned premiums	**31.2**
Outward reinsurance premiums	
Premiums ceded	**(12.6)**
Change in unearned premium provision	**2.1**
Premiums ceded to reinsurers	**(10.5)**
Net earned premiums	**20.7**

3. Fee and commission income

	2020
Fee income	**0.5**
Reinsurance commission earned	**2.9**
Other commission	**0.1**
	3.5

Fee income is in respect of policy administration fees and commission from third party arrangements, predominantly within Motor and is considered revenue from contracts with customers per IFRS 15.

Reinsurance commission earned relates to profit commission due under reinsurance arrangements. For further details see *Profit commission due under reinsurance arrangements* on page 25.

Other commission is in respect of ancillary income from aggregator business within Motor and is also considered revenue from contracts with customers per IFRS 15. For further details see *Fee and Commission income* on page 24.

4. Investment income

	2020
Interest income (calculated using Effective Interest Rate) from financial assets at fair value through other comprehensive income:	
Listed debt securities	**0.5**
	0.5

5. Gains less losses arising from financial instruments

	2020
Net gains arising on financial assets:	
Net fair value gains on financial assets at fair value through income or expense	**1.0**
	1.0

The net gains arising on financial assets above are all unrealised as at 31 December 2020.

6. Net policyholder claims and benefits paid

	2020
Gross claims paid	
Current year claims	16.4
Prior year claims	16.7
Gross claims paid	33.1
Less salvage and subrogation	
Current year claims	(1.7)
Prior year claims	(0.7)
Salvage and subrogation received	(2.4)
Claims paid	30.7
Less amounts receivable from reinsurers	
Current year claims	(4.5)
Prior year claims	(3.2)
Amounts receivable from reinsurers	(7.7)
Net policyholder claims and benefits paid	23.0

7. Fee and commission expenses

	2020
Commission paid	0.5
	0.5

8. Operating expenses

	2020
Other acquisition expenses	0.8
Administration expenses	10.2
Operating Expenses	11.0

The Group has had a small number of employees to oversee key functions, with other services provided by MISL. Key management compensation is disclosed in note 31. Staff costs, included within administrative expenses, are shown below. The average number of employees is shown for the period from 2 December 2020 in order to show a representative number since the Group had employees.

Staff costs

	2020 £000
Wages and salaries	133
Social security costs	23
Pension costs - defined contribution scheme	8
	164

Average number of employees

Administration	6
Management	7
	13

8. Operating expenses (continued)

Amounts payable to auditors

	2020 £'000
Audit of these financial statements	**240**
Audit of subsidiary financial statements	**429**
Amounts receivable by SFHL's auditor and its associates in respect of:	
Other assurance services	**115**
	784

Other assurance services relate to assurance provided on the Group's and the subsidiary Solvency II reporting for £35,000 and £80,000 respectively.

The above amounts are exclusive of VAT.

9. Finance costs

	2020
Subordinated loans interest expenses	**1.0**
	1.0

Interest expenses relate to the perpetual and term subordinated loans issued on 2 December 2020.

10. Gain on bargain purchase

	Total
Gain on bargain purchase of SIL	**146.5**
Gain on bargain purchase	**146.5**

On 2 December 2020, SFHL acquired 100% of the issued share capital of Soteria Insurance Limited, for £104m cash consideration. The net assets acquired, recorded at their fair value, were £250.5m giving rise to a gain on bargain purchase of £146.5m. Further details of this business combination are disclosed in note 26.

All amounts are stated in £m unless otherwise indicated

11. Income tax

	2020
Current tax	
UK tax charge for the current period	**(0.1)**
Total current tax charge	**(0.1)**
Deferred tax	
Origination and reversal of temporary differences	**(0.3)**
Total deferred tax charge	**(0.3)**
Total tax charge recognised in the income statement	**(0.4)**

Further information about deferred tax is presented in note 23.

Reconciliation of effective tax rate

The tax charge in the income statement differs from the theoretical amount that would arise using the corporation tax rate in the UK as follows:

	2020
Profit before taxation	**144.2**
Tax calculated at domestic corporation tax rate of 19%	**(27.4)**
Effect of:	
Goodwill on acquisition of SIL not subject to corporation tax	**27.8**
Deferred tax not recognised	**(0.1)**
Expenses not deductible for tax purposes	**(0.7)**
Income tax charge	**(0.4)**

12. Property, plant and equipment

	Leasehold property	Total
2020		
Cost		
At incorporation	-	-
Acquired through business combinations	1.1	1.1
At the end of the financial period	1.1	1.1
Depreciation		
At incorporation	-	-
Depreciation charge for the period	-	-
At the end of the financial period	-	-
Carrying amount		
At the end of the financial period	1.1	1.1
At incorporation	-	-

The leasehold properties comprise 2 right of use properties used for client service activities by the Group.

All amounts are stated in £m unless otherwise indicated

13. Investment in group undertakings

Company	2020
At incorporation	-
Acquisition during the period	104.0
At end of the period	104.0

The Company acquired 100% of the ordinary shares of Soteria Insurance Limited (SIL) on 2nd December 2020 for £104m.

14. Financial investments at fair value through income or expense

	2020
Reverse repo arrangement with credit institutions	92.0
Collective investment assets	49.0
	141.0

All amounts are expected to be recovered within one year. Within the above are secured deposits of £92.0m. Collateral of £92.0m, in the form of gilts is held against these deposits. Please see the credit risk note on page 53 for further details.

Other than the Collective investment assets all items within this category comprises short term fixed rate deposits which are designated as fair value through income and expense upon initial recognition. The Collective investment assets are investments in unit funds. These funds have no maturity date and units are readily tradeable.

Under IFRS 9, these instruments would fail the 'Solely Payments of Principal and Interest' (SPPI) test and would be classified as held for trading as they are managed on a fair value basis.

15. Financial assets at fair value through other comprehensive income

	2020
Listed debt securities - fixed rate	472.5
Listed debt securities - floating rate	53.6
	526.1

At 31 December 2020, debt securities of £355.9m are expected to be recovered more than 12 months after the reporting date..

16. Insurance receivables and other assets

Group

	2020
Receivables arising from insurance:	
Arising from insurance operations	123.0
Salvage and subrogation recoveries	32.1
Reinsurance ceded	0.2
Other receivables:	
Accrued interest	4.8
Prepayments	4.3
Other receivables	3.3
	167.7

No amounts are due after more than one year.

All amounts are stated in £m unless otherwise indicated

16. Insurance receivables and other assets (continued)

Other receivables are net of a bad debt provision of £0.2m. This is a specific provision against receivables from Repair Workshops that are over 84 days past due. Receivables arising from insurance operations are stated net of an impairment provision of £0.4m. The provision is calculated based on an assessment of insurance receivables for objective evidence that an impairment loss has been incurred. Any adjustment to the level of the provision is recorded within the income statement as an adjustment to written premium.

Amounts overdue but not impaired are £nil.

Assets past due typically comprise high volume/low value balances for which the Group does not seek collateral but continues to work with counterparties to secure settlement.

Amounts receivable relating to contracts with customers under IFRS 15 is £1.2m.

Other receivables includes £0.5m due from the Group's investors in in relation to expenses settled on their behalf.

Company	**2020**
Other receivables	**0.5**
	0.5

Other receivables are amounts due from the Company's investors in in relation to expenses settled on their behalf.

17. Cash and cash equivalents

Group	**2020**
Cash and cash equivalents	**28.6**
Overdrafts	**(6.0)**
Net cash and cash equivalents	**22.6**

This balance is included as cash and cash equivalents for the purpose of the statement of cash flows. The balance represents the net position across the Group and Company's various bank accounts. Included in cash and cash equivalents is £21.5m held in the Group's custodian account for investment purposes.

Company	**2020**
Cash and cash equivalents	**1.8**
Cash and cash equivalents	**1.8**

18. Share capital

Consolidated and company	**2020**	**2020**
	Number	**£**
Authorised shares		
Ordinary shares of £0.01 each	10,000,000	100,000
	Number	**£**
Issued and fully paid		
At incorporation	1	0.01
Issued on 12 November 2020	9,999,999	99,999.99
At the end of the financial period	**10,000,000**	**100,000**

At incorporation 1 ordinary share was issued at par. During the period, the authorised share capital was increased by £99,999.99 by the issue of 9,999,999 ordinary shares of £0.01 for £37,000,000. All the shares constitute a single class of ordinary share.

All amounts are stated in £m unless otherwise indicated

19. Share premium

Consolidated and company

	2020
	£
Share premium	
At incorporation	-
Issued on 12 November 2020	36,900,000.01
At the end of the financial period	**36,900,000.01**

The issue of 9,999,999 ordinary shares of £0.01 created share premium of £36,900,000.01.

20. Retained earnings and other reserves

Group	2020
Retained earnings	
At incorporation	-
Profit for the financial period	**143.8**
At the end of the financial period	**143.8**

	2020
Other reserves	
Financial assets at fair value through other comprehensive income reserve	**1.6**
	1.6

Any retained earnings would represent amounts available for dividend distribution to the equity shareholder of the Group, subject to certain conditions being met.

Company	2020
Retained earnings	
At incorporation	-
Loss for the financial period	**(1.9)**
At the end of the financial period	**(1.9)**

All amounts are stated in £m unless otherwise indicated

21. Lease liabilities and borrowings

Group	2020
Lease liabilities	1.2
17.5% subordinated perpetual loan	11.6
16.9% subordinated term loan	58.2
	71.0
At incorporation	-
Acquired with business combinations	1.2
Issued in the period, net of issue costs	69.8
Lease liabilities and borrowings at the end of the financial period	71.0

On 2nd December 2020, the Group issued £12m of a subordinated perpetual loan charged at 17.5% interest per annum.

On 2nd December 2020, the Group issued £60m of a subordinated term year loan charged at 16.9% interest per annum.

The Group incurred costs of £2.2m in relation to issue of subordinated loans in the period. These costs have been capitalised.

There were no defaults or breaches of contractual obligations attaching to the subordinated loans during the financial period.

Finance costs incurred during the financial period include £1.0m in relation to interest on the subordinated loans. £0.2m of this interest relating to the 17.5% subordinated perpetual loan was cancelled on 31 March 2021.

The lease liabilities relates to right of use assets denominated in sterling and maturing between 2021 and 2026, with interest rates ranging from 9.5% to 9.9%. Any lease options have been ignored as they are not reasonably certain to be exercised. Since the reporting date the lease liabilities and right of use assets have been transferred to MISL (see note 27).

Company	2020
17.5% subordinated perpetual loan	11.6
16.9% subordinated term loan	58.2
	69.8
At incorporation	-
Issued in the period, net of issue costs	69.8
Lease liability at the end of the financial period	69.8

On 2nd December 2020, the Company issued £12m of a subordinated perpetual loan charged at 17.5% interest per annum.

On 2nd December 2020, the Company issued £60m of a subordinated term loan due 2030 at par, charged at 16.9% interest per annum.

The Company incurred costs of £2.2m in relation to issue of subordinated loans in the period.

There were no defaults or breaches of contractual obligations attaching to the subordinated loans during the financial period.

Finance costs incurred during the financial period include £1.0m in relation to interest on the subordinated loans. £0.2m of this interest relating to the 17.5% subordinated perpetual loan was cancelled on 31 March 2021.

All amounts are stated in £m unless otherwise indicated

22. Insurance contract liabilities and reinsurance assets

(a) Analysis of insurance contract liabilities

	2020
Gross	
Claims reported	**349.6**
Claims incurred but not reported	**102.2**
Claims settlement expenses	**10.6**
Unexpired risk provision	**-**
Unearned premiums	**168.3**
Total gross insurance liabilities	**630.7**
Recoverable from reinsurers	
Claims reported	**(108.6)**
Claims incurred but not reported	**(25.8)**
Unearned premiums	**(5.7)**
Quota Share*	**74.0**
Total reinsurers' share of insurance liabilities	**(66.1)**
Net	
Claims reported	**241.0**
Claims incurred but not reported	**76.4**
Claims settlement expenses	**10.6**
Unexpired risk provision	**-**
Unearned premiums	**162.6**
Quota Share*	**74.0**
Total net insurance liabilities	**564.6**

Reinsurance is used to limit risk to the statement of financial position for the various classes of general insurance business. Proportional and non-proportional types of reinsurance cover have been purchased in accordance with assumptions made regarding the possible levels of losses and required returns on equity.

* Quota share recoverable amounts are shown net of amounts payable, regarding premiums ceded and amounts receivable regarding commission income. See accounting policies note 15 (vii) on page 27 for details.

The balance in the quota share funds withheld account is £97.1m.

(b) General insurance contracts – assumptions, changes in assumptions and sensitivity

i) Basis of assessing liabilities

The Group uses a combination of recognised actuarial and statistical techniques to assess the ultimate cost of claims. These include:

- projecting historic claims payment and recoveries data;
- projecting numbers of claims;
- deriving average costs per claim to apply to claim numbers; and
- projecting historic claims paid and incurred data (payment plus estimates) – statistical actuarial techniques including chain ladder, Bornhuetter-Ferguson and Cape Cod.

22. Insurance contract liabilities and reinsurance assets (continued)

(b) General insurance contracts – assumptions, changes in assumptions and sensitivity (continued)

Detailed claims data, including individual case estimates, are used to derive patterns in average claims costs and timings between occurrence and estimate/payment of claims. The most common method used is the chain ladder method. This technique involves the analysis of historical claims development trends and the selection of estimated development factors based on this historical pattern. The selected development factors are then applied to cumulative claims data for each accident quarter, which is not yet fully developed, to produce an estimated ultimate claims cost for each accident quarter. A degree of judgment is required in selecting the most appropriate development factors.

The chain ladder method can be volatile for relatively undeveloped origin periods so a Bornhuetter-Ferguson/Cape Cod method is often used in such cases. These methods use some prior expectation of the ultimate claims and stabilise the projected ultimate by weighting between the prior expected ultimate and that projected based on the assumed development factors. The Cape Cod method differs from the Bornhuetter-Ferguson method in that it uses a trending of ratios (such as the average cost) to arrive at a prior expected ultimate for use in the projections.

The work is undertaken and supervised by suitably qualified personnel. Claims provisions are separately computed for each claim type such as bodily injury, accidental damage, storm, flood and subsidence. All provisions are calculated with explicit allowance for reinsurance and subrogation recoveries. Provisions are not discounted for investment return other than any required additional provision for unexpired risks, periodic payment settlements and provisions relating to exposure within the electric industry.

Discounted reserves in respect of periodic payment settlements are £51.2m and historic liability claims from the electric industry discounted reserve amounts to £2.4m. Further details around expected settlement patterns for claims arising on these reserves are disclosed within the market risk section on page 53.

The historic liability claims from the electric industry reserve was based on a report produced for the industry at the end of 2018 by Willis Towers Watson, an actuarial consultancy. This gave Willis Towers Watson's estimate of both the undiscounted and discounted incurred but not reported (IBNR) reserves as at the end of June 2018. This was the most recent report available when the Group calculated its year end 2020 reserves.

As outlined within the risk management section, there is significant uncertainty in the assessment of liabilities and provisions are set to be adequate to cover the anticipated eventual cost. A management margin is added to the 'actuarial best estimate', so that no adverse run-off deviations are envisaged. Sensitivity analysis is performed to assist the selection of key parameters and, hence, the provisions adopted. Provisions are subject to detailed review regarding the appropriateness of key assumptions and the quantum of the provisions established.

The overall objective of the Group's reserving policy is to produce reliable and accurate reserves. Assumptions underlying the reserving calculations are agreed by SIL's Quarterly Reserving Committee (QRC). Methodologies are peer reviewed throughout the calculation process. Provisions are approved and signed off by the Actuarial Function Actuary within SIL in consultation with the QRC, and any margin above the actuarial best estimate reserve is set by SIL's Chief Financial Officer (CFO). The Board has a risk appetite that adopted reserves will include a management margin above the actuarial best estimate such that adopted reserves fall between the 70th and 80th percentiles of a distribution of possible outcomes. The Group's reserves are within this risk appetite.

Monthly reports are produced by the actuarial team and presented to the CFO in order to advise management of the performance of the business. More detailed reports are produced on a quarterly basis providing information on the performance of the business against plan. These reports form the basis of reporting the performance to the SIL and SFHL Boards.

All amounts are stated in £m unless otherwise indicated

22. Insurance contract liabilities and reinsurance assets (continued)

(b) General insurance contracts – assumptions, changes in assumptions and sensitivity (continued)

ii) Key assumptions
Principal assumptions underlying the claims provisions include:

• The future development pattern for claims payments and incurred amounts being in line with those observed in the past. The impact of the on-going Covid-19 pandemic has disrupted this assumption resulting in judgement being applied to allow for lower claims experience and delays in recognition of some incurred amounts;

• Allowance for future inflation rates being different to those implied in the claims data;

• The pattern of future claims notifications relating to mesothelioma claims decaying as projected; and

• for bodily injury claims, allowance has been made for:

i. use of the appropriate Ogden Tables;
ii. awards for general damages in accordance with the 15th edition of the Judicial College Guidelines;
iii. a proportion of large claims being settled by periodic payments; and
iv. improvements in the case estimation techniques resulting in earlier recognition of the size of claims.

The gross insurance provision of £312.9m for claims and loss adjustment expenses arising in respect of prior years has not changed significantly since the balance was acquired on 2 December 2020.

iii) Sensitivity analysis
There is greater uncertainty over motor claims provisions than other provisions as they often involve claims for bodily injury and associated legal costs which typically have a longer period to settlement. Motor provisions represent the most significant proportion of the total general insurance outstanding claims liabilities. Latent liability claims represent a much smaller element of the general insurance outstanding claims liabilities but the run-off of these claims is very uncertain, with a wide range of possible best estimate assumptions. Sensitivity information is given for motor claims provisions together with limited information for all other classes. The following table indicates the effect on gross claims provisions (gross of reinsurance) of changes in key assumptions. The impact of the increased uncertainty on the income statement is mitigated through holding management margin on the best estimate reserves that is proportionate to the level of uncertainty.

2020 Assumption	Change in parameter	Effect on gross provision	% Effect
Motor			
Average cost of claims for last three years - bodily injury and legal	+10%	32.4	9.7%
Mean term to settlement - bodily injury and legal	+½ year	7.4	2.2%
Rate of future inflation - bodily injury and legal	+1%	10.4	3.1%
Other classes			
Mean term to settlement (liability)	+½ year	0.3	1.5%
Mean term to settlement (non-liability)	+½ year	0.6	1.5%
Rate of future inflation (liability)	+1%	1.4	7.7%
Rate of future inflation (non-liability)	+1%	0.5	1.3%
Slower decay of future notifications of Mesothelioma claims (liability)	AWP curve	10.3	55.2%

All amounts are stated in £m unless otherwise indicated

22. Insurance contract liabilities and reinsurance assets (continued)

(c) Change in general insurance liabilities and reinsurance asset

i) Change in insurance contract liabilities (net of salvage and subrogation)

	Gross	Unexpired risk provision	Salvage & subrogation	Net
2020				
At incorporation	-	-	-	-
Acquired with business combinations	471.2	-	(33.4)	437.8
Movement in the financial period	(8.8)	-	1.4	(7.4)
At the end of the financial period	462.4	-	(32.0)	430.4

ii) Claims and loss adjustment expenses

	Gross 2020	Reinsurance 2020	Net 2020
Claims reported	358.8	(108.9)	249.9
Claims incurred but not reported	101.6	(25.5)	76.1
Claims settlement expenses	10.8	-	10.8
	471.2	(134.4)	336.8
Quota Share	-	76.1	76.1
Acquired with business combinations	471.2	(58.2)	413.0
Claims paid during the period	(33.1)	7.7	(25.4)
Increase/(decrease) in liabilities:			
Arising from current period claims	24.3	(7.8)	16.5
	(8.8)	(0.1)	(8.9)
Quota Share	-	(2.1)	(2.1)
Total movement	(8.8)	(2.2)	(11.0)
Claims reported	349.6	(108.6)	241.0
Claims incurred but not reported	102.2	(25.8)	76.4
Claims settlement expenses	10.6	-	10.6
Unexpired risk provision	-	-	-
	462.4	(134.4)	328.0
Quota Share	-	74.0	74.0
At the end of the financial period	462.4	(60.4)	402.0

All amounts are stated in £m unless otherwise indicated

22. Insurance contract liabilities and reinsurance assets (continued)

(c) Change in general insurance liabilities and reinsurance assets

iii) Provisions for unearned premiums

	Gross 2020	Reinsurance 2020	Net 2020
At incorporation	-	-	-
Acquired with business combinations	185.3	(3.6)	181.7
Increase in the financial period	14.2	(12.6)	1.6
Release in the financial period	(31.2)	10.5	(20.7)
Movement in the financial period	(17.0)	(2.1)	(19.1)
At the end of the financial period	168.3	(5.7)	162.6

All amounts are stated in £m unless otherwise indicated

22. Insurance contract liabilities and reinsurance assets (continued)

(iv) Analysis of claims development

	Accident year										
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	**Total**
Gross of reinsurance											
At end of the accident year:	497.0	502.1	368.1	284.7	285.5	353.5	367.8	401.7	414.6	**299.1**	**3,774.1**
One year later	530.2	473.3	346.9	269.0	268.1	371.6	358.0	393.0	412.8		**3,422.9**
Two years later	527.4	473.0	343.1	263.9	259.9	351.0	353.4	394.4			**2,966.1**
Three years later	518.0	467.9	335.4	260.7	259.2	345.5	354.9				**2,541.6**
Four years later	515.1	458.2	340.6	259.5	256.2	353.1					**2,182.7**
Five years later	508.1	452.2	336.2	258.2	256.3						**1,811.0**
Six years later	509.4	451.9	337.5	258.9							**1,557.7**
Seven years later	512.4	452.5	338.3								**1,303.2**
Eight years later	513.9	452.4									**966.3**
Nine years later	515.0										**515.0**
Estimate for cumulative claims	515.0	452.4	338.3	258.9	256.3	353.1	354.9	394.4	412.8	**299.1**	**3,635.2**
Cumulative payments to date	(510.4)	(451.0)	(333.3)	(257.6)	(252.0)	(322.7)	(320.8)	(345.1)	(317.0)	**(155.0)**	**(3,264.9)**
Gross outstanding claims liabilities before discounting	4.6	1.4	5.0	1.3	4.3	30.3	34.1	49.3	95.8	**144.1**	**370.2**
Provision for prior years											**81.6**
Gross outstanding claims liabilities											**451.8**
Gross claims reported											**349.6**
Gross claims incurred but not reported											**102.2**
Gross outstanding claims liabilities											**451.8**

Included in the analysis above is £51.2m of discounted reserves relating to PPOs. PPO reserves are discounted at 4.4%, reflecting the expected yield on the investments held to back the PPO claims, adjusted for credit risk. Undiscounted reserves relating to PPOs are £109.2m. The above analysis excludes claim handling expenses.

All amounts are stated in £m unless otherwise indicated

22. Insurance contract liabilities and reinsurance assets (continued)

(iv) Analysis of claims development (continued)

	Accident year										
	2011	2012	2013	2014	2015	2016	2017	2018	2019	**2020**	**Total**
Net of reinsurance											
At end of the accident year:	481.2	489.8	350.9	275.9	267.9	347.7	268.3	294.4	295.0	**219.1**	**3,290.2**
One year later	514.8	456.3	330.4	260.6	256.8	357.8	262.1	289.1	293.1		**3,021.0**
Two years later	516.5	458.7	329.7	255.0	247.7	339.3	259.6	289.8			**2,696.3**
Three years later	509.4	456.3	322.0	251.3	247.5	335.9	260.6				**2,383.0**
Four years later	506.9	448.1	325.8	252.0	245.6	338.5					**2,116.9**
Five years later	502.3	445.4	325.0	250.9	245.5						**1,769.1**
Six years later	503.3	445.3	326.4	251.5							**1,526.5**
Seven years later	506.1	445.9	326.9								**1,278.9**
Eight years later	507.3	445.8									**953.1**
Nine years later	508.5										**508.5**
Estimate for cumulative claims	508.5	445.8	326.9	251.5	245.5	338.5	260.6	289.8	293.1	**219.1**	**3,179.3**
Cumulative payments to date	(503.9)	(444.5)	(325.6)	(250.4)	(241.7)	(320.1)	(236.5)	(254.7)	(227.7)	**(113.4)**	**(2,918.5)**
Net outstanding claims liabilities before discounting	4.6	1.3	1.3	1.1	3.8	18.4	24.1	35.1	65.4	**105.7**	**260.8**
Provision for prior years											**56.6**
Net outstanding claims liabilities											**317.4**
Net claims reported											**241.0**
Net claims incurred but not reported											**76.4**
Net outstanding claims liabilities											**317.4**

Included in the analysis above is £23.6m of discounted reserves relating to PPOs. It is to be expected that releases will normally be made to prior years' claims as current reserves are set such that no adverse deterioration is expected. However, from time to time the random occurrence of significant large individual claims or events being worse than expected can give rise to a required strengthening, in addition to normal claims development being adverse. The 2020 result includes movement on prior year reserves of £19.2m.

All amounts are stated in £m unless otherwise indicated

23. Taxation

Group

	2020
Current tax	
Asset acquired through business combinations	1.4
Tax charged to the income statement	(0.1)
Asset at the end of the financial period	1.3
Asset relating to group relief not yet received	3.1
Liability relating to amount due to HMRC	(1.8)
Asset at the end of the financial period	1.3

	2020
Deferred tax liability	
Liability acquired through business combinations	(1.0)
Tax charged to the income statement	(0.3)
Tax charged to statement of comprehensive income	(0.5)
Liability at the end of the financial period	(1.8)
Analysis of deferred tax liability	
Claims equalisation reserve	(0.9)
Capital allowances on fixed assets	0.2
Deferred tax on fair value adjustments on acquisition of SIL	2.8
Financial assets at fair value through other comprehensive income	(3.9)
Liability at the end of the financial period	(1.8)

The Finance Act 2012 abolished the tax relief for the equalisation reserves of general insurers with effect from 1 January 2016. However, the Act allows for the release of the reserve equally over a period of six years for tax purposes, with £4.8m being released by SIL in 2020 (£0.4m since 2 December 2020). The balance as at 31 December 2020 was £4.8m which had previously been treated as tax deductible, however for accounts purposes the corresponding value is nil. The difference has been recognised as part of the Deferred Tax liability at 19%.

The Finance Act 2015 reduced the main rate of corporation tax to 19% from 1 April 2017 and to 17% from 1 April 2020. On 11 March 2020 it was announced that the corporation tax rate would remain at 19% from 1 April 2020 and this was substantively enacted on 17 March 2020. The deferred tax liability at 31 December 2020 has been calculated based on an estimate of the rate at which the asset will reverse, using the tax rates substantively enacted at the statement of financial position date, being 19%.

On 3 March 2021 the UK Government announced that the main UK corporation tax rate will increase to 25% from 1 April 2023. This change has not yet been substantively enacted. As a result, existing temporary differences on which deferred tax has been provided may unwind in periods subject to the 19%/25% rates. The estimated value of the deferred tax asset using a rate of 25% from 1 April 2023 is immaterial.

SFHL has £0.1m of carried forward tax losses for which no deferred tax asset has been recognised, as at this time management does not foresee sufficient future taxable profits to derive a benefit from the utilisation of the tax losses.

All amounts are stated in £m unless otherwise indicated

24. Reinsurance liabilities

	2020
Arising from reinsurance operations	10.3
	10.3

Premiums due to reinsurers including adjustment premiums due under catastrophe and motor excess of loss contracts, expected reinstatement premium under the catastrophe excess of loss contract and premiums payable under the IPA reinsurance contract.

25. Insurance and other payables

Group	2020
Arising out of direct insurance operations	0.8
Accruals and deferred income	12.1
Insurance premium taxation payable	10.2
Provisions	0.1
Other payables	6.6
	29.7

Reconciliation of movement of provisions:

	Marketing Campaigns	Software Licence	Total
At incorporation	-	-	-
Acquired from business combinations	0.5	0.1	0.6
Utilisation of provision	(0.5)	-	(0.5)
Released to Income Statement	-	-	-
At 31 December 2020	-	0.1	0.1

- Marketing Campaigns is a provision for redemption of "Co-op Food Vouchers" issued as part of sales promotions. This provision was transferred to Co-op Insurance Services Limited in December 2020.
- Software Licence is a provision for an onerous contract that expires March 2021.

Company	2020
Accruals and deferred income	1.4
	1.4

All amounts are stated in £m unless otherwise indicated

26. Business combinations

Soteria Insurance Ltd

On 2 December 2020, SFHL acquired 100% of the issued share capital of Soteria Insurance Limited (SIL), for £104m cash consideration. SIL is a UK based general insurer which, until February 2021, underwrote insurance, predominantly in personal lines (Motor and Home). The assets acquired and liabilities assumed have been recorded at their fair value for the purposes of the acquisition balance sheet and included in the consolidated financial statements of the Group, in accordance with IFRS 3 Business combinations. SIL contributed £20.7m to net earned premium and a loss of £0.4m to the Group since acquisition. If the Group had acquired SIL from 1 January 2020 then the full year impact to net earned premium would have been £291.8m and to profit before tax would have been £7.2m.

The table below shows the fair value of the 100% share of the net assets acquired, liabilities assumed, consideration paid and the resulting goodwill.

	Recognised values on acquisition
Property, plant and equipment	**1.1**
Reinsurance assets	**62.0**
Financial investments at fair value through income or expense	**168.8**
Financial assets at fair value through other comprehensive income	**531.2**
Current tax assets	**3.1**
Insurance receivables and other assets	**178.7**
Cash and cash equivalents	**3.8**
Total assets	**948.7**
Insurance contract liabilities	**(656.5)**
Lease liabilities and borrowings	**(1.2)**
Deferred tax liabilities	**(1.0)**
Current tax liabilities	**(1.7)**
Reinsurance liabilities	**(6.6)**
Insurance and other payables	**(26.9)**
Overdrafts	**(4.3)**
Total liabilities	**(698.2)**
Net identifiable assets	**250.5**
Total consideration	**104.0**
Goodwill recognised on acquisition	**(146.5)**

There were no intangible assets or contingent considerations recognised on acquisition. The resulting £146.5m gain on bargain purchase has been fully recognised in the Group consolidated income statement. In part, the discounted purchase price relative to net asset value reflects the additional costs that will be incurred by SIL in effecting an orderly run-off. These were not reflected in the fair value of net assets at the date of acquisition, as this was assessed on the basis of continuing to write insurance business. The discounted purchase price also represents the reward to SFHL for taking on the risk of running SIL, including ensuring that it remains adequately capitalised, and the risk that SFHL's ability to realise the net asset value is reduced or delayed. Transaction cost of £0.5m were expensed and are included in administrative expense.

27. Contingent assets and liabilities

The Group does not have any contingent assets.

In January 2021 a property lease, included in the disclosure in note 21, was transferred from the Group to MISL. From this date the liability to pay the 3rd party landlord became the responsibility of MISL. As part of the contract to re-assign the lease to MISL, the Group have guaranteed the payment of rent and other sums payable under the lease should MISL fail to pay. The lease contains a break option in December 2021. The maximum amount of rent and service charges that the Group could have to pay up to this date is £0.3m. The Group does not expect to make any payments under this guarantee.

In April 2021 a second property lease, included in the disclosure in note 21, was transferred from the Group to MISL. From this date the liability to pay the 3rd party landlord became the responsibility of MISL. As part of the contract to re-assign the lease to MISL, the Group have guaranteed the payment of rent and other sums payable under the lease should MISL fail to pay. The lease end date is September 2021. The maximum amount of rent and service charges that the Group could have to pay up to this date is £0.2m. The Group does not expect to make any payments under this guarantee.

27. Contingent assets and liabilities (continued)

As a financial services provider, the Group is subject to extensive and comprehensive regulation. It must comply with numerous laws and regulations, including the Consumer Credit Act, which significantly affect the way it does business. Whilst the Group believes there are no unidentified areas or failures to comply with these laws and regulations which would have a material impact on the financial statements, there can be no guarantee that all issues have been identified.

28. Contingent contract obligations

The Group has no contingent contract obligations.

29. Risk Management and Capital Management

i) Risk Management

The Group issues contracts that transfer insurance risk and is exposed to financial risk through its holdings of financial assets and liabilities. This section summarises these risks and the way Group manages them.

Our approach to risk management

The Risk Management Framework (RMF) identifies processes, ownership, responsibilities and the oversight required to support effective implementation of Risk Management across the Group.

Effective Risk Management is essential for the achievement of business success and is everyone's responsibility. Customers, members, regulators and other stakeholders expect the Group to manage risk effectively.

The Group operates a Risk Management Framework (RMF), the majority of which has been in operation for several years in SIL, prior to its acquisition by SFHL. It is noted that since SIL was placed into run-off, changes have been required to simplify the RMF so that it better reflects the risk profile and operating model; i.e. that the Group's only trading subsidiary, SIL, is a run off insurer and that much of the day to day operations are now outsourced. However, the overarching framework and culture of robust risk management remain in place.

The RMF has been built around the 'Three Lines of Defence' model as follows:

- First line: manage risk in day to day operations.
- Second line: provide oversight and challenge.
- Third line (Internal Audit): provide assurance that the RMF is being executed as intended.

As the Group is largely an outsourced model, much of first line work is carried out by third parties, with finance and risk accountability being assumed by the Soteria management team.

Risk assessment of SFHL

The principal risks of the Group are risks associated with the business of the Group's trading subsidiary, SIL. An assessment of the principal risks facing the business at the time of acquisition by SFHL has been undertaken, as well as a projection of how these risks are expected to evolve over the coming months as the risk profile changes. These risks are summarised on page 5.

The SIL RMF requires the Executive Team to attest that they understand the risks and controls in their areas of accountability and support an open risk management culture. In support of the attestation, each Executive and/or Risk Framework Owner (RFO) is required to undertake a Risk and Control Self-Assessment (RCSA), which identifies the risks to the achievement of their objectives and the controls in place to mitigate these risks, together with an assessment of the effectiveness of the controls (Design and Performance with appropriate testing of control performance). The RCSA is designed to cover all material controls including financial, operational and compliance controls as well as the minimum requirements set out in SIL's risk policies and control standards.

Risk management structure

The SFHL Board is responsible for approving the strategy and the level of acceptable risks articulated through its statement of risk appetite. The SFHL Board is also responsible for overall corporate governance, which includes ensuring that there is an adequate system of risk management in place.

The Group has developed and implemented a governance and organisation structure, which supports the SFHL Board with its responsibilities. The SFHL and SIL Boards have established separate risk and audit committees to:

- Oversee and advise the Boards of SFHL and SIL on current and potential risks and the overall risk framework.
- Ensure that risk appetite is appropriate and adhered to and that key risks are identified and managed.
- Review the effectiveness of internal controls and risk management systems.

To assist the SFHL Board in carrying out its functions and to ensure that there are internal controls and risk management, the SFHL and SIL Boards have delegated certain responsibilities to a set of Board committees and, in the case of SIL, to the SIL Chief Executive Officer (CEO). The CEO has in turn, delegated elements of these responsibilities to appropriate members of the senior management team. To ensure independent oversight the Chief Risk Officer (CRO) also has accountability to the SIL Board Risk Committee (BRC).

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

All Board sub-committees have Terms of Reference describing the authority delegated to them by their Board, and the Board ensures that each committee is provided with sufficient resources to enable its duties to be undertaken.

SIL Board
The purpose of the SIL Board is to oversee all risks associated with the Group's trading subsidiary, SIL, either directly or through the Board sub-committees which it has set up. Responsibilities include:

- Providing oversight and advice to the SFHL Board on current and potential risks and risk management strategies.
- Reviewing and approving the Risk Strategy, Risk Appetite and risk limits and tolerances within SIL.
- Review and oversight of the financial performance and capital adequacy of SIL.
- Review and approval of changes to the Investment Mandate and investment strategy.

SFHL Risk and Audit Committee (BRAC)
The purpose of the BRAC is to oversee and advise the SFHL Board on current and potential risks and the overall risk framework. The committee also oversees SFHL's risk management arrangements, ensuring that Risk Appetite is appropriate and adhered to and that key risks are identified and managed. It also assists the SFHL Board in discharging its responsibilities for the integrity of SFHL's financial statements, to review the effectiveness of internal controls and risk management systems and to monitor the effectiveness and objectivity of internal and external auditors. Responsibilities include:

- Review and oversight of financial statements and annual reports before submission to the SFHL Board.
- Exercising oversight of identified risk control framework failings and weaknesses as well as management actions taken to resolve them.
- Oversight of internal and external assurance and audit.
- Providing oversight and advice to the Board on current and potential risks and risk management strategies.
- Reviewing and approving the Risk Strategy, Risk Appetite and risk limits and tolerances.
- Reviewing and challenging internal controls and processes of risk management including the coverage of the risk taxonomy.

SFHL Governance and Remuneration Committee
The purpose of this committee is to ensure the overall Governance is adequate for the SFHL Group and is the Nominations Committee for SFHL Board membership. Responsibilities include:

- Ensuring adequacy of overall Group Governance.
- Determining the remuneration policy for the SFHL non-executive directors.
- Determining the fees payable to the Board Chair.

SIL Board Risk Committee (BRC)
The purpose of the Committee is to oversee and advise the SIL Board on current and potential risks and the overall risk framework. The Committee also oversees SIL's risk management arrangements, ensuring that Risk Appetite is appropriate and adhered to and that key risks are identified and managed. Responsibilities include:

- Providing oversight and advice to the Board on current and potential risks and risk management strategies.
- Reviewing and approving the Risk Strategy, Risk Appetite and risk limits and tolerances.
- Reviewing and challenging the design of the Risk Management Framework, recommending to the Board for approval.
- Reviewing and challenging internal controls and processes of risk management including the coverage of the risk taxonomy.

SIL Board Audit Committee (BAC)
The purpose of the Committee is to assist the SIL Board in discharging its responsibilities for the integrity of SIL's financial statements, to review the effectiveness of internal controls and risk management systems and to monitor the effectiveness and objectivity of internal and external auditors. Responsibilities include:

- Review and oversight of financial statements and annual reports before submission to the SIL Board.
- Exercising oversight of identified risk control framework failings and weaknesses as well as management actions taken to resolve them.
- Oversight of internal and external assurance and audit.

SIL Board Investment Committee (BIC)
The purpose of the Committee is to assist the SIL Board in discharging its responsibilities in relation to the Prudent Person Principle by overseeing the Company's out-sourced investment activities and to ensure investments are made in line with the approved strategy and mandate. Responsibilities include:

- Reviewing and recommending to the SIL Board proposed changes to the Investment Mandate.
- Considering the implications of investment strategy on capital requirements and providing guidance to management on the appropriate balance between risk and reward.
- Review and oversight of the performance of investments against investment strategy and mandate.
- Exercising oversight of out-sourced investment managers.

All amounts are stated in £m unless otherwise indicated

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

SIL Remuneration Committee (RemCo)
The purpose of the Committee is to determine the Remuneration Policy for SIL in respect of its Executive and Key Function Holders and set/approve remuneration. Reward and remuneration arrangements for other colleagues are maintained by the CEO, with appropriate input from the Committee. Responsibilities include:

- Determining the remuneration policy for the SIL Executive, in conjunction with the Group Remuneration Committee, ensuring that this is in line with Group Remuneration policy and complies with relevant regulatory guidance.
- Having responsibility for setting the remuneration for each of the SIL Executives.
- Determining the fees payable to the Board Chair.

SIL maintains a Responsibilities Map which sets out the accountabilities delegated by the CEO to each member of the Executive Team, which are also reflected within their individual job descriptions. These accountabilities include the Senior Managers & Certification Regime (SM&CR) senior management function and prescribed responsibilities which are considered in conjunction with delegated authorities. In addition to Board level committees, there are a number of Executive Management Committees:

SIL Executive Committee (ExCo)
The purpose of ExCo is to monitor performance of the business, oversee its customer and business strategic direction, and ensure both timely issue resolution and decision making for matters and decisions referred to it from sub-committees. Responsibilities include:

- Ensuring the implementation of the risk strategy set by the Board so as to deliver an effective risk management environment for SIL.
- Ensuring that all key strategic elements are governed fostering a culture that emphasises and demonstrates the benefits of a risk-based approach to decision making, internal control and management.
- Management of mitigating actions relating to any risks to the strategic direction, plans and business model of SIL.

Insurance Services and Run Off Agreement (ISARA) Governance Committee
Subsequent to the sale of SIL to SFHL this committee was put in place to monitor the overall service performance of the service contracts with MISL and Affinity Insurance Services Limited, being the ISARA and BUA (Binding Underwriting Authority) respectively.

Transitional Services Agreement (TSA) Oversight Committee
Subsequent to the sale of SIL to SFHL this committee was in place to monitor the overall service performance of the service contracts with Co-op Group.

Senior Management Committees
SIL has other committees that advise and support the CEO and members of the senior management team in carrying out their responsibilities, and provide detailed oversight and monitoring. These include the Reserving Committee and the Finance Committee.

Level 1 Risks
Within the SFHL Group the vast majority of risks arise within SIL. Risks are classified into Level 1 and Level 2 categories. Business activity can be exposed to one or a combination of the following risk types. The Level 1 risks are the highest category of inherent financial and non-financial risks to which the Group is exposed:

Risk Type	Definition	Page
Strategic and business risk	The risk of not meeting strategic and business objectives caused by poor or sub-optimal strategy implementation, deployment of resources, decision making, strategic change programmes, economic, regulatory or other environmental factors resulting in lost earnings and capital	49
Conduct risk	The risk that the Group's processes, behaviours, offerings or interactions will result in unfair outcomes for customers and a damage to reputation.	49
Regulatory risk	The risk of regulatory sanctions, regulatory censure, material financial loss, or loss to reputation the Group may suffer as a result of failure to comply with regulations, rules, related self-regulatory organisation standards and codes of conduct applicable to its activities	49
Insurance (Premium) risk	The inherent uncertainties as to the occurrence, amount and timing of insurance liabilities or unearned exposure	49-50
Insurance (Reserving) risk	The risk of loss, or of adverse change in the value of insurance liabilities, resulting from fluctuations in the timing, frequency and severity of insured events for earned policies, and in the timing and amount of claim settlements	50
Market risk	The risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers including interest rates, market prices of assets and liabilities	50-52
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events	52
Liquidity risk	The current and prospective risk to earnings or solvency arising from the Group's inability to meet its obligations when they come due without incurring unacceptable losses	52-53
Credit risk	The risk to earnings and capital arising from a debtor's failure to meet their legal and contractual obligations	54

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

For each of the risks, the Group appoints an RFO. The RFO is required to define and document a risk framework, which comprises a Risk Policy, associated Control Standard(s) and risk appetite and to certify to the effectiveness of the control framework used to manage the risk on a semi-annual basis.

Strategic and Business risk

Strategic and Business risk is defined as the risk of not meeting strategic and business objectives caused by poor or sub-optimal strategy implementation, deployment of resources, decision making, strategic change programmes, economic, regulatory or other environmental factors, resulting in lost earnings and capital. Strategic risks cover those risks over the longer term time horizon around the strategic plan and they align to the strategic risk profile. Business risks are in period performance against plan and align to the material risk profile.

The Group's financial objective in managing these risks is to hold a sufficient capital buffer in excess of minimum regulatory capital requirements to cover projected risks and meet liabilities as they fall due. The SFHL and SIL Boards have defined detailed risk appetite measures and limits underpinning these objectives, which are measured, monitored and reported regularly to management, Risk Committees and Boards. The outsourcing of operations, post acquisition of SIL by SFHL, and migration to modern systems in Q1 2021 has resolved the key strategic risk faced by the Group of a business model for SIL which was unviable in the long term, largely caused by inefficient legacy systems.

Conduct risk

Conduct risk is the risk that the Group's processes, behaviours, offerings or interactions will result in unfair outcomes for customers. Accordingly, conduct risk may arise from any aspect of the way a business is conducted, the sole test being whether the outcome is an unfair one for customers. Conduct risk is a key area of focus across the financial services industry, with close scrutiny from the FCA.

Regulatory risk

Regulatory risk is the risk of regulatory sanctions, regulatory censure, material financial loss or loss to reputation the Group may suffer as a result of its failure to comply with regulations, rules, related self-regulatory organisation standards, and codes of conduct applicable to its activities. The Group's objective is to be compliant with all relevant regulatory requirements and manage its regulatory risks so as to minimise the probability and potential impact of breaches and to remedy promptly and comprehensively the consequences of any that do occur.

Regulatory risk has remained heightened into 2021 with the PRA interest in successful system migration for SIL and maintenance of capital adequacy.

Insurance risk

Insurance risk comprises the risk of loss resulting from:

- Future claims events other than catastrophes (Premium Risk).
- Adverse change in the value of insurance liabilities (Reserve Risk).
- Natural or man-made catastrophe events (Catastrophe Risk).
- The assumptions underlying expenses not being borne out in practice (Expense Risk).

Until migration was completed in Q1 2021, the Group continued to underwrite renewals, and limited new business, of UK private Motor and Home policies, either written directly or through brokers, all of which cover a 12 month duration. After this point, the Group does not intend to continue to underwrite insurance. Historically, other classes of business were underwritten by SIL, which are now in run off, and residual liabilities mainly relate to employer's liability and commercial motor business.

Key risks under Motor policies are bodily injury to third parties, accidental damage to property and theft of or from policyholders' vehicles. The most significant factors affecting the frequency and severity of motor claims are judicial, legislative and inflationary changes and the frequency and severity of large bodily injury claims. Periodic Payment Orders (PPOs) are being used to settle injury claims in the UK, with compensation being paid to claimants at regular intervals, rather than in a single lump sum award. This introduces further risk to the insurer as the term of the payments is dependent upon length of life expectancy and the payments increase with care worker future inflation.

Key risks under Home policies are damage from storm and flood, fire, escape of water, subsidence, theft of or accidental damage to contents and liability risks.

At the statement of financial position date there were no significant concentrations of insurance risk.

Insurance Risk - Objective and strategy

The Group outsources the management of insurance risk to a third party (MISL). Oversight is in place to ensure that the following principles are adhered to:

- Insurance risks are underwritten in accordance with underwriting strategy and priced to reflect the underlying risk. The objective of the underwriting strategy is to ensure that the underwritten risks are diversified in terms of type and amount of risk, industry/demographic profile and geography, and only those risks which conform with underwriting criteria are accepted.
- Reserve risk volatility is minimised through proactive claims handling, the claims provisioning process and robust reserving and modelling approaches.

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

These are considered in turn below.

The objective of the underwriting strategy is to ensure that the underwritten risks are diversified in terms of type and amount of risk, industry/demographic profile and geography, and only those risks which conform with underwriting criteria are accepted. Exposure mix and the frequency and average costs of claims are monitored throughout the period and where significant deviations from expectation are identified remedial action is taken.

The overriding objective in claims handling is to ensure all claims are properly scrutinised and paid where they fall within the terms and conditions of the policy. The proper scrutiny of claims is facilitated by the use of various technical aids such as weather validation and fraud databases, and the use of claims specialists. The basis for assessing claims provisions is set out in note 22 (pages 37 to 38).

The nature of insurance contracts is that the obligations of the insurer are uncertain as to the timing or quantum of liabilities arising from contracts. The Group takes all reasonable steps to ensure that it has information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established. The Group manages this risk through the SIL Reserving Committee, which supports the SIL CFO in their responsibility to formally review claims reserves on a quarterly basis.

Insurance Risk – Reinsurance
The Group uses reinsurance to manage insurance risk, and in particular to mitigate the cost of catastrophe events such as storms and floods and the cost of large claims arising within its motor account. The appropriate level of reinsurance is proposed by management and approved by the SIL Board.

In 2020, the Group had three main reinsurance programmes in place: catastrophe excess of loss cover, motor excess of loss cover and a quota share arrangement on both its Motor and Home business.

The quota share reinsurance arrangement within SIL, which commenced at the beginning of 2017 and remained in place in 2020, enhances the Standard Formula capital coverage by reducing exposure to premium, catastrophe and reserve risk.

Market risk
Market risk is the risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market risk drivers such as interest rates and market prices of assets and liabilities.

The Group's investments are held within the trading subsidiary, SIL. SIL invests in high-quality fixed and variable interest bonds issued by corporations ("corporate bonds") and the UK government ("gilts"), and in short-term sterling deposits with financial institutions (reverse repo transactions). The value of, or income from, assets held is subject to volatility from changes in both market interest rates and additional spreads related to the specific credit-worthiness of the issuer ("credit-spreads"). Proceeds from maturing investments are also subject to risk over the future return on reinvestment.

SIL is also exposed to market interest rates through the discounted present value placed upon future claims. All future claims are discounted for assessing solvency on both an economic and regulatory basis. However, IFRS short term insurance reserves (normally less than five years) are not directly affected by market interest rates as they are undiscounted.

SIL invests in a limited amount of Index linked bonds, UK equities and collective investment funds which are of a more long term nature to match the long term liabilities.

The Group wrote contracts of insurance in the United Kingdom and insurance liabilities and borrowings are denominated in sterling. Funds are invested solely in assets denominated in sterling and consequently there is no direct exposure to currency risk.

The Group is not exposed to any pensions risk.

In summary, the key market risks that the Group is exposed to are:
- Fluctuations in interest rates, allowing for the impact on both asset and liability values, and investment income.
- Movements in credit-spreads which impact the market value of corporate bonds.
- Changes in the relationship between interest rates which have similar but not identical characteristics.
- Fluctuations in the market value of equities and other assets.

Market Risk - Objective and strategy
The Group's objective is to achieve acceptable returns through the use of highly rated UK government and corporate bonds while managing volatility by minimising exposure to equities and other volatile instruments. To enhance certainty over the investment return generated from these assets, management practice is generally to maintain holdings to maturity.

The Group's investments are managed by Royal London Asset Management and, from February 2021, TwinFocus Limited, with whom the Group has agreed investment mandates with limits for exposure by asset type, credit-rating, maximum terms and maximum exposure to individual counterparties.

The Group manages credit-spread and default risks from corporate bonds through the limits for exposure to credit-ratings and individual counterparties. Other risk mitigation techniques employed to manage exposure to counterparty default include transacting only through a diversified range of authorised counterparties and ensuring that any cash deposits (in excess of counterparty limits) are collateralised on a daily basis. The Capital, Liquidity, Investment and Pension Committee (CLIP) and SIL's Investment Committee supports the SIL CFO in overseeing the monitoring and management of these risks and exposures against limits.

All amounts are stated in £m unless otherwise indicated

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

Market Risk (continued)

The investment mandate sets strategic asset allocation and limits on the types and duration of investments. The mandate has been set by considering the risk/reward trade off and the impact upon capital adequacy and solvency of the overall business. The mandate has maintained the very risk adverse stance since the formation of the Group , with the allowance for some equities and Collective Investment Assets to match the longer term liabilities.

Interest-rate risk is managed through investing in fixed interest securities with a similar duration profile to the liabilities under the general insurance contracts. The Group matches the average duration of assets and liabilities in this portfolio by estimating their mean duration. The mean duration of financial assets is measured against the investment mandate and remained within these boundaries during the period. The mean duration of insurance liabilities is calculated using historical claims data to determine the expected settlement pattern for claims arising from insurance contracts in force at the statement of financial position date (both incurred claims and future claims arising from the unexpired risks at the statement of financial position date).

	2020
For the period ended 31 December 2020	**(years)**
Insurance liabilities	**3.0**
Financial assets	**3.3**

Specific assets are used to match periodic payment orders (PPOs) and provisions relating to exposure within the historic liability claims from the electricity industry by amount and appropriate to the long duration of these liabilities. In order to do this, an expert opinion on claimants' life expectancy is used along with an expectation of long term average earnings.

Mean durations for these exposures are:

2020

	Amount	**Duration**
Periodical payments		**Years**
Insurance liabilities	**23.4**	**16.3**
Financial assets		
Index linked bonds	**32.4**	**20.2**
Collective investment assets	**49.0**	**n/a**

There is no explicit duration accompanying these collective investment assets.

EIROS claims	**Amount**	**Duration**
		Years
Insurance liabilities	**1.8**	**8.5**
Financial assets	**2.7**	**6.7**

Insurance liabilities are shown net of reinsurance. The liabilities are assessed against assets on a net basis, as this represents the Group's residual risk. Gross liabilities in respect of periodic payment settlements are £51.2m and EIROS claims amount to £2.4m.

Market Risk - Sensitivity analysis

The most significant aspect of market risk to which the Group is exposed is the effect of changes in value of collective investment funds and changes in credit-spreads on corporate bonds. The resulting movements in the market values of corporate bonds directly affect the Group's solvency. As movements in the value of the majority of investment assets held by the Group are recognised in other comprehensive income, they have no impact on reported IFRS profits.

An increase of 100 basis points in credit-spreads would reduce the value of the Group's assets at the end of the financial period by approximately £16.8m. This would reduce the Group's solvency (on all bases) by £13.6m net of tax, although it is likely that the overall net impact on solvency would be lower than this as the fall would be partially offset by a reduction in the value of liabilities arising from the use of the Volatility Adjustment (under Solvency II) to value claims provisions. The impact of a decrease of 100 basis points in credit-spreads would have similar but opposite effects.

All amounts are stated in £m unless otherwise indicated

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

Climate Change

The Group has incorporated Climate Change into its Risk Management Framework and Investment Mandate and has assigned an owner who is responsible for the management and reporting of climate change.

The Group has made a high level assessment of its risk with the conclusion that the main risk category impacted is Market risk. The risks include a fall in the value of corporate bonds in carbon intensive companies due to stranded assets or legislation to deal with climate change. Furthermore, as more investors move to sustainable investment strategies there is the risk that investments that fall outside these criteria fall in price as a result. A review of the Group's investment portfolio has concluded that there is not an undue level of risk. During the year, the Group's financial assets at fair value through other comprehensive income did not include any bonds in companies involved in the extraction or refining of, or power generation from, fossil fuels.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or external events. The Group's objective is to minimise operational risk through the implementation of a robust control environment which minimises the potential for loss as a result of the failure of processes, people and technology or due to external events.

The Group has defined the following sub-categories within operational risk, which represent the major areas of operational risk exposure. Each sub-category has its own RFO, and is supported by underlying control standards:

- Financial Reporting Risk.
- Technology Risk (including Cyber Risk).
- Third Party Supplier Risk.
- Change Risk.
- Information Risk.
- Financial Crime Risk.
- People Risk.
- Physical Risks (inc. Business Disruption Risk and Health and Safety Risk).

Under the Group's operating model, Markerstudy Group (MSG) are responsible for managing a significant amount of the Group's operational risks. Post migration, operational risks will significantly reduce, as the trading subsidiary, SIL, will be operating off MSG's IT systems rather than the legacy Co-op systems. However there will remain some element of Operational risk whilst the new MSG processes are embedded. A significant review and simplification of the suite of level 2 operational risks is expected following the successful completion of migration.

Third Party Risk will remain high given the Group's reliance on MSG for the management of policies and claims. This will be managed via the ISARA agreement and monitoring meetings that have been put in place. The risk with regard to People Risk is that there are only a small number of staff. Although this may mean that people risk is lower overall, it does increase key person dependency. This risk is managed individually with detailed succession planning and retention strategies.

The Group has a corporate insurance programme to transfer specific risks to insurers as part of its risk management approach which, in 2020 included; property and business interruption, financial crime, employer's liability and Directors and Officers. Owing to the changes to the business in 2021 it has not been necessary to renew the property and business interruption or financial crime insurance.

Liquidity risk

Liquidity risk is the current and prospective risk to earnings or solvency arising from the Group's inability to meet its obligations when they come due without incurring unacceptable losses. The Group's objective is to maintain at all times, liquid resources which are adequate to meet all policyholder and other funding obligations as they fall due primarily through the use of cash and highly liquid UK government and corporate bonds.

The model to assess liquidity takes into account the change to the business during run-off. Liquidity is assessed against minimum requirements for stressed assets and liquid assets. The values of stressed investments are the market values of the investments less haircuts which are based on the credit rating of the investment. Liquid assets are cash and gilts. Both are assessed against forecast cash flows that would be required under stress scenarios. At 31 December 2020 liquid assets of £145.8m were held against a minimum requirement of £139.9m. £75m of assets were also held on 1 month reverse-repo which were not included in the value of liquid assets. The stressed value of investments at 31 December 2020 was calculated as £608.9m versus a minimum requirement of £299.7m. The amounts noted in this paragraph are unaudited. The haircuts applied to stressed investments are:

Credit Rating	Maturity	Government %	Corporate %
AAA to AA-	≤ 1 year	0.5	1.5
AAA to AA-	> 1 ≤ 5 years	1.5	5.5
AAA to AA-	> 5 years	3	11
A+ to BBB-	≤ 1 year	1.5	2.5
A+ to BBB-	> 1 ≤ 5 years	4	8.5
A+ to BBB-	> 5 years	6	17
BB+ and lower	≤ 1 year	100	100
BB+ and lower	> 1 ≤ 5 years	100	100
BB+ and lower	> 5 years	100	100
Equity funds, Bond OEICs & Property funds	N/a	100	100
Cash	N/a	0	0

All amounts are stated in £m unless otherwise indicated

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

Liquidity risk (continued)

The actual and projected levels of cash and other assets held are monitored and managed through SIL's Capital, Liquidity, Investment and Pensions Committee (CLIP), with oversight by the SIL BRC and SIL Board. In addition, in between CLIP meetings, monthly monitoring of liquid assets against risk appetite limits is undertaken.

The following table indicates the time profile of undiscounted cash flows arising from financial liabilities (based upon contractual maturity).

As at 31 December 2020	Carrying value	Gross nominal outflow	Up to 1 year	1 - 2 years	2 - 3 years	3 - 4 years	4 - 5 years	More than 5 years
Insurance contract liabilities	451.9	510.3	182.0	92.1	55.5	32.6	20.8	127.3
Financial Liabilities at amortised cost:								
Borrowed funds	71.0	116.0	8.8	8.7	8.6	8.6	8.6	72.7
Reinsurance liabilities	10.3	10.3	10.3	-	-	-	-	-
Insurance and other payables	29.7	29.7	29.7	-	-	-	-	-
Overdrafts	6.0	6.0	6.0	-	-	-	-	-
	568.9	**672.3**	**236.8**	**100.8**	**64.1**	**41.2**	**29.4**	**200.0**
Other liabilities	3.6							
Total recognised liabilities	**572.5**							

For SFHL the Company's primary cash outgoings relate to interest payments on subordinated debt and administrative expenses recharged by SIL. Liquidity risk is mitigated by agreement that if necessary SFHL could defer the reimbursement of expenses to SIL until it receives the first dividend from SIL. In addition, if SFHL does not hold sufficient cash the subordinated debt instruments require that the interest payments are cancelled (on the £12m subordinated debt) and deferred (on the £60m subordinated debt), respectively.

Credit risk

Credit risk is the risk to earnings and capital arising from a debtor's failure to meet their legal and contractual obligations. The Group does not aim to earn a return from credit risk hence its appetite for credit risk is very low. Potential losses arising from credit risk are minimised by the use of high quality reinsurers and highly rated investments.

The Group's key credit risk exposure is from default or delay in respect of insurance receivables, where default is defined as failure to pay resulting in financial loss to the Group. This could arise from the following:

- Reinsurance counterparties failing to meet financial obligations or entering into restructuring arrangements that may adversely affect reinsurance recoveries;
- Default or delay of repayment of loans and receivables; and
- Insurance counterparties, including MISL and AISL, failing to meet financial obligations.

The Group manages credit risks associated with cash and corporate bonds as part of market risk. See market risk section on pages 50 to 52 for details.

Where reinsurance is used to manage insurance risk, there is a risk that the reinsurer fails to meet its obligations in the event of a claim. The Group places limits over exposure to a single reinsurance counterparty, or counterparty group, based upon their credit-worthiness. These limits applied when reinsurance was initially placed, and are regularly monitored by the Capital, Liquidity, Investment and Pensions Committee. Where concern exists over the credit quality of a reinsurer, a review will be undertaken to determine the most appropriate management action.

The quota share reinsurance arrangement in place in SIL throughout 2017 – 2020 operates on a funds withheld basis, which means that only the reinsurer margin is transferred to the reinsurer.

Insurance receivable and other assets are primarily premium debtors due from customers and insurance intermediaries. Exposure to insurance intermediaries is managed in line with SIL's Credit risk policy.

The Group has a credit exposure of up to £60.0m with a trading counterparty that provides administrative services including the collection of premiums. Credit Insurance is purchased to bring this exposure to within risk appetite and will be in place until 31 May 2021, by which time the exposure with the trading counterparty is expected to be significantly reduced.

As at the statement of financial position date, the table below provides analysis of the credit rating of those assets subject to credit risk. The Group's policy for making provisions for possible impairment is described within the accounting policy section on page 23.

All amounts are stated in £m unless otherwise indicated

29. Risk Management and Capital Management (continued)

i) Risk Management (continued)

Credit risk (continued)

	AAA	AA	A	BBB and below	Not rated	Total
As at 31 December 2020						
Financial assets at fair value through income or expense:						
Cash deposits and reverse repo arrangements with approved credit institutions.	**-**	**-**	**92.0**	**-**	**-**	**92.0**
Collective Investment Assets	**-**	**-**	**-**	**-**	**49.0**	**49.0**
Financial assets at fair value through other comprehensive income :						
Listed debt (fixed rate)	**104.9**	**192.8**	**164.1**	**10.7**	**-**	**472.5**
Listed debt (variable rate)	**36.1**	**5.0**	**12.5**	**-**	**-**	**53.6**
Reinsurance assets	**-**	**44.0**	**21.5**	**-**	**0.6**	**66.1**
Insurance receivables and other assets	**1.0**	**1.6**	**2.2**	**-**	**130.8**	**135.6**
Cash and cash equivalents	**-**	**-**	**28.4**	**0.2**	**-**	**28.6**
	142.0	**243.4**	**320.7**	**10.9**	**180.4**	**897.4**
Salvage and subrogation						**32.1**
Assets not subject to credit risk						**4.2**
						933.7

The maximum exposure to credit risk, before making allowance for collateral held, is represented by the carrying value of each financial asset in the table. Collateral, in the form of gilts, of £92.0m is held against short term deposits which have been placed into a reverse repo transaction of £92.0m as at 31 December 2020. These short term deposits sit with approved credit institutions within financial investments at fair value through income or expense on the statement of financial position.

Eurozone risk

The Group has no direct exposure to the sovereign debt of European countries and solely exposure to European countries arising from corporate bonds as shown in the following table, all bonds are denominated in sterling. SIL has no exposures to European countries as a result of repo arrangements.

The following table shows exposure to European countries arising from corporate bonds.

	Up to 1 year	1 to 5 years	Over 5 years	Total
As at 31 December 2020				
Belgium	-	3.2	-	3.2
Finland	-	6.2	-	6.2
France	5.5	8.9	-	14.4
Germany	-	18.9	-	18.9
Ireland	-	9.5	-	9.5
Netherlands	6.9	4.2	-	11.1
Norway	-	13.2	-	13.2
Sweden	3.0	12.3	-	15.3
	15.4	76.4	-	91.8

29. Risk Management and Capital Management (continued)

ii) Capital Management

Objectives when managing capital
The Group's strategy in respect of capital management is to ensure that the following objectives are met:
- It has sufficient capital to meet all regulatory requirements.
- It has sufficient additional capital above the regulatory requirements ('SCR coverage') to make any breach of the regulatory requirement unlikely, ensuring that policyholders are protected and also that the Board's risk appetite is met.
- Subject to the above objectives being met, it makes the required return on equity.

Required capital
Under the Solvency II regulatory framework, the Prudential Regulation Authority (PRA) requires the Group to calculate a capital requirement and to hold sufficient capital to meet it.

(a) Regulatory required capital
The Solvency II regulatory regime came into force as at 1 January 2016. Under this solvency framework, the Group is required to hold capital at the greater of two measures, namely the Solvency Capital Requirement (SCR) and the Minimum Capital Requirement (MCR). These measures are described below.

i) SCR: The SCR is a risk-responsive capital measure, calibrated to ensure that an insurer will be able to meet its obligations over the next 12 months with a probability of at least 99.5%. The Group currently calculates its SCR using the Standard Formula (SF), adjusted to ensure that this appropriately reflects its risk profile. The Standard Formula is calibrated based on market wide data and not on a specific firm's data, so the PRA must approve the SF SCR as being appropriate for a particular firm.

ii) MCR: The calculation of the MCR is prescribed under the Solvency II guidance and is set at a lower level than the SCR. Initially, the MCR is calculated by applying set factors to net technical provisions and the previous 12 months' net written premiums and is then subject to a cap of 45% and a floor of 25% of the SCR.

(b) Internal required capital
The SFHL Board sets capital risk appetite, which defines how much additional capital (SCR coverage) the Group should hold over and above its most onerous regulatory capital requirement. As at 31 December 2020, the risk appetite is for the SCR coverage to be at least 120% as calculated on a run-off basis.

The Group has maintained capital above all its regulatory requirements since becoming an Insurance Group on acquisition by SFHL of SIL in December 2020. SCR coverage has been maintained to at least 120% throughout the period. Where forecasts have indicated a potential for coverage to fall below this level over the planning horizon, management have developed plans to bring coverage back within risk appetite. The Group reviews solvency continuously through monthly, or when appropriate more frequent, monitoring. Quarterly reports on the solvency of the Group are provided to the Board. Quarterly reports on the solvency of SIL, the Group's core insurance undertaking, are provided to the Capital, Liquidity, Investments and Pensions Committee and Board.

In the event that the Group falls below its risk appetite, it would be possible to reduce capital requirements by executing actions that reduce risk, albeit often resulting in reduced returns. Management have identified potential actions which fall into three main categories:
- Actions to reduce insurance risk through the purchase of reinsurance.
- Actions to reduce other types of risk – for example, de-risking the investment portfolio.
- Actions to increase available capital – for example, through possible issuance of additional subordinated debt.

Potential actions are routinely assessed at least once a year so that contingent management actions are available.

(c) Capital composition
The policies and processes employed by the Group are designed to benefit policyholder protection by giving the business an accurate understanding of the amount and quality of capital and resources. This helps the business ensure that sufficient capital is held to absorb unexpected losses and maintain solvency.

Under the Solvency II regime capital resources are referred to as own funds. Own funds correspond to capital and reserves which can serve as a buffer against risks and absorb financial losses. Each type of own funds is classified within a tier, with tier 1 being the highest quality capital.

All of the Group's excess of assets over liabilities, which comprises share capital and retained profits calculated on a Solvency II basis, is classified as tier 1 capital. At period end 2020 the Group holds £25m of ancillary own-funds, being a promise of equity backed by bank deposit in escrow, and which has required prior supervisory approval to be recognised under Solvency II as tier 2 capital. In addition, the perpetual subordinated debt and term subordinated debt held by the business, disclosed in note 21, served as tier 1 restricted and tier 2 capital respectively, and any deferred tax assets are classified as tier 3 capital.

100% of tier 1 own funds held at the end of the reporting period were eligible to meet the SCR and MCR. The Solvency II regulations restrict the use of lower tier capital to support the SCR, the value of Tier 2 and Tier 3 items not being permitted to exceed 50% of the value of the SCR. 100% of tier 1 capital, 20% of tier 2 capital and 0% of tier 3 capital is eligible to meet the MCR. Restricted Tier 1 items must form less than 20% of total Tier 1 items eligible to meet the SCR and MCR.

Further information, including an explanation of the valuation of assets and liabilities on a Solvency II basis, is included in the Group Solvency & Financial Condition Report published annually.

30. Parent company

SFHL owns 100% of the share capital of SIL and together they form the Group. The Group's investors are GSO Capital Opportunities Fund III (Luxembourg) S.à r.l, TF Special Opportunities – Frisco Limited and Markerstudy (Affinity) Holdings Limited. The results of SFHL and SIL are not consolidated into any other financial statements as no entity has a controlling interest in the Group.

31. Related party transactions

On 2nd December 2020, the Group issued £12m of a subordinated perpetual loan charged at 17.5% interest per annum to GSO Capital Opportunities Fund III (Luxembourg) S.à r.l.(GSO) (£11m) and TF Special Opportunities – Frisco Limited (TF) (£1m). GSO and TF are related to SFHL through being investors in the Group.

On 2nd December 2020, the Group issued £60m of a subordinated term loan due 2030 at par, charged at 16.875% interest per annum to GSO Capital Opportunities Fund III (Luxembourg) S.à r.l. (£56m) and TF Special Opportunities – Frisco Limited (£4m).

On 2nd December the investors transferred funds of £3.2m to SFHL in order for SFHL to settle the investor's expenses on their behalf. £3.7m of expenses were settled on behalf of the investors in the period. The amount owed by the investors at the end of the period, £0.5m, is included within Other Receivables.

Key management (as defined by IAS 24) is considered to include the members of the Company's Board and the Board and Executive committee members of its subsidiary, SIL.

Key management compensation

	2020
	£000
Salaries and short term benefits	**117**
Other long term benefits	**-**
	117

In respect of Executive and Non-Executive Directors

	2020
	£000
Salaries and short term benefits	**86**
Other long term benefits	**-**
	86

In respect of the highest paid director:

	2020
	£000
Salaries and short term benefits	**38**
Other long term benefits	**-**
	38

32. Fair values of financial assets and liabilities

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the annual report and accounts:

(a) Financial investments at fair value through income or expense

The fair value of financial assets designated at fair value through income or expense, being short term (less than one month) fixed rate deposits, approximates to their nominal amount.

(b) Financial assets at fair value through other comprehensive income

Fair value of listed debt securities is based on clean bid prices at the statement of financial position date without any deduction for transaction costs.

Financial assets at fair value through other comprehensive income are regularly reviewed for impairment. Objective evidence of impairment can include default by a borrower or issuer, indications that a borrower or issuer will enter bankruptcy or the disappearance of an active market for that financial asset because of financial difficulties. Expected credit losses are recognised, calculated in accordance with IFRS 9.

These reviews give particular consideration to evidence of any significant financial difficulty of the issuer or measurable decrease in the estimated cash flows from the investments.

All amounts are stated in £m unless otherwise indicated

32. Fair values of financial assets and liabilities (continued)

(c) Lease liabilities and borrowings

Fair value measurement is calculated on a current market price.

(d) Receivables and payables

For receivables and payables with a remaining life of less than one year, the nominal amount is deemed to reflect the fair value, where the effect of discounting is immaterial.

The table below shows a comparison of the carrying value and fair values of financial instruments for those liabilities not disclosed at fair value.

Financial liabilities	Carrying value 2020	Fair value 2020
Lease liabilities	1.2	1.2
Borrowed funds	69.8	72.0

Financial asset and liability classification

The table below analyses financial instruments by measurement basis as detailed by IAS 39 (Financial Instruments: Recognition and Measurement).

Statement of financial position categories

2020	FVTPL	Loans and receivables	FVTOCI	Other amortised cost	Total
Assets					
Financial assets at fair value through income or expense	141.0	-	-	-	141.0
Financial assets at fair value through other comprehensive income	-	-	526.1	-	526.1
Other financial assets	-	131.3	-	28.6	159.9
Total financial assets	141.0	131.3	526.1	28.6	827.0
Non-financial assets					106.7
Total assets					933.7

2020	FVTPL	Loans and receivables	FVTOCI	Other amortised cost	Total
Liabilities					
Lease liabilities and borrowings	-	-	-	71.0	71.0
Overdrafts	-	-	-	6.0	6.0
Other financial liabilities	-	-	-	29.6	29.6
Total financial liabilities	-	-	-	106.6	106.6
Non-financial liabilities					644.7
Total liabilities					751.3
Capital and reserves					182.4
Total liabilities and equity					933.7

All amounts are stated in £m unless otherwise indicated

32. Fair values of financial assets and liabilities (continued)

The following table provides an analysis of financial assets and liabilities that are valued or disclosed at fair value, by the three level fair value hierarchy as defined within IFRS 7 (Financial Instruments: Disclosure):

- 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 inputs 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 inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Based upon guidance issued by The Committee of European Securities Regulators (CESR), the Group classifies debt securities in Level 1 only if it can be demonstrated on an individual security by security basis that the price quotes obtained are representative of actual trades in an active market (through obtaining binding quotes or through corroboration to published market prices). Pricing providers cannot guarantee that the prices that they provide are based on actual trades in the market. Therefore all of the corporate bonds are classified as Level 2 and valued using the market prices as at the reporting date multiplied by the number of each security held.

Valuation of financial instruments 2020	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Financial assets at fair value through income or expense	**-**	**141.0**	**-**	**141.0**
Financial assets at fair value through other comprehensive income	**-**	**526.1**	**-**	**526.1**
Total financial assets at fair value	**-**	**667.1**	**-**	**667.1**

Investments in debt securities as:	**Carrying amount 2020**	**Fair value 2020**	**Amortised cost 2020**
Financial assets at fair value through other comprehensive income	**526.1**	**526.1**	**505.5**

33. Events after the Reporting Period

Subsequent to the Group's period end, the Board of SIL have taken the decision to cease writing insurance business and put SIL into a controlled run-off. This decision was taken on 11 February 2021 and no insurance business has been written since 24 February 2021. The PRA approved SIL's application to have its regulatory permission to effect new insurance contracts cancelled on 29 March 2021. The Group will continue to administer existing policies in force and settle outstanding claims. The focus of the Directors is to meet all obligations to customers throughout a solvent run-off, to fulfil all regulatory requirements and, to the extent the Group has surplus capital above a prudent risk appetite to meet liabilities and regulatory requirements, it aims to distribute this capital to its owners.

The financial impact of this event is a reduction in net assets of £18.4m. Insurance contract liabilities increase by £10.5m owing to an increase in claims settlement expenses of £6.6m and unexpired risk provision of £3.9m as a result of there being limited business written in the future to which to attribute expenses. Insurance and other payables increase by £7.9m as an industry levy becomes payable and is recognised immediately on ceasing underwriting business.